



# PRIVATE EQUITY PERSPECTIVES PODCAST

## EPISODE 4: MAKING CREATIVE CAPITAL INVESTMENTS IN ENERGY

INSIGHTS FROM THE BDO PRIVATE EQUITY PRACTICE

**Todd Kinney:** Good morning and welcome to another episode of BDO's Private Equity Perspectives podcast. I'm your host, Todd Kinney. I'm a director in the Private Equity practice here at BDO, based in New York City. Happy to announce our guest today is Ethan Shoemaker. Ethan is a managing director and principal at Orion Energy Partners here in New York. And he's about to open their office in Houston, so he's a busy man. So, Ethan, we appreciate you taking some time with us today.

**Ethan Shoemaker:** Yeah. Thanks so much for the invitation, Todd.

### **A CREDIT-ORIENTED PRIVATE EQUITY FIRM [0:47 – 2:14]**

**Kinney:** Of course, of course. Your firm's a great brand and a very important relationship to BDO, so we're happy to offer you the guest seat. I guess to kick things off, I always like to give our guests an opportunity to tell us a little bit more about their firm and really their investment strategy. So I guess, Ethan, I would say, "Floor's open to you." What would you like to tell our listeners about Orion?

**Shoemaker:** So Orion Energy Partners is a credit-oriented private equity firm. We focus on making creative capital investments in energy and energy infrastructure companies in North America. And what that basically means is we are a flexible, creative lender to primarily lower middle market and middle market energy companies.

And our niche has evolved into being focused on partnering with family-owned businesses, privately-owned businesses, entrepreneur-driven or developer-driven businesses, across the energy value chain, particularly in the midstream, the downstream, and also in the power and renewal space, and all of the services that serve those.

As you mentioned, we have offices here in New York and, starting on Monday, in Houston. And we have about a billion dollars of capital under management and have been investing under this Orion Energy platform for about two years now.

### **TOPICS DISCUSSED INCLUDE:**

[A Credit-Oriented Private  
Equity Firm \[0:47 – 2:14\]](#)

[Finding Niche Opportunities  
\[2:15 – 4:40\]](#)

[The Lending Landscape  
\[4:41- 6:23\]](#)

[Tax Reform: A Net Positive  
\[6:24 – 8:36\]](#)

[A Constructive Oil Price  
Environment \[8:37 – 10:49\]](#)

## FINDING NICHE OPPORTUNITIES [2:15 – 4:40]

**Kinney:** Excellent. Well, you're certainly our first private-lender guest to the podcast. I think all the folks were kind of traditional PE growth investment and buyout. So it's going to be great to get your perspective. I guess as you just said, Ethan, clearly many of your investments are in niche areas. Within the energy infrastructure space, in this environment of really frothy valuations and obviously intense competition, I would think this approach would help you find attractive opportunities that are often overlooked by other traditional investors kind of broadly looking at the space. Do you care to share your thoughts there?

**Shoemaker:** Yeah. I think everyone's got their own niche. I think what we've found is that there's a real dearth of capital focused on particularly the lower middle market and middle market space in energy. A lot of the private capital, private credit strategies that you've seen emerge over the last five or six years have been very sponsor-focused, LBO-focused, really targeted on writing larger checks that were previously provided through institutional capital markets, Term Loan B market, project finance market. And that space, as you said, both generally and for energy, is very competitive and has seen a lot of capital raised over the last several years. Our niche is a little bit more down-market. From a size perspective, we're typically making investments in the \$50 million to \$150 million size range and tends to be less sponsor-driven.

We can absolutely do sponsor deals, but we find the most receptivity for our capital from people that actually own their own business and maybe don't want the restrictions and other lack of flexibility that comes with traditional capital sources - banks, regional banks, otherwise. But also, aren't interested in selling their business, or giving up control, or being diluted by traditional energy private equity. And it's sort of that niche where we find ourselves and where we've deployed across quite a few investments over the last two years.

## THE LENDING LANDSCAPE [4:41- 6:23]

**Kinney:** I guess going off some of your commentary there, then, as I think about the traditional banking sector, there's certainly been a lot of talk of the repeal of leverage guidance. Just a few years ago, the SEC called on banks to cap their leverage at about six times EBITDA. But even recently, the head of the OCC said that the guidance is no longer official. So I guess the question to you is do you think this is going to bring more traditional lenders into the energy space?

**Shoemaker:** I think with respect to the leverage lending guidance in particular, there's no doubt about it that overall regulations and the increase in regulations post-financial crisis were supportive of alternative forms of capital like Orion Energy. We're not focused on any one particular regulation changing and don't view, necessarily, the leverage lending guidance being modified or repealed as fundamentally changing the competitive landscape.

We find that in our niche, which is particularly focused on, like I said, the lower middle market and family-owned, privately-owned businesses, that our competition is equity, and also regional banks, and other smaller traditional lenders, many of whom are less aggressive lending in the energy space not because of any particular regulatory rule or change but simply because there's been a lot of commodity price volatility and a lot of pain that they've felt in that space over the last two years. And so for folks that are career energy professionals and have a lot of experience, we feel like that specialization is really valuable and allows us to really put capital to work in a smart way.

## TAX REFORM: A NET POSITIVE [6:24 – 8:36]

**Kinney:** I certainly agree with you that the specialization is going to work in your favor. I guess in addition to leverage guidance, which seems to be a pretty popular topic, I want to transition into tax reform, and get your general thoughts on tax reform, and how you think it might affect your business and your companies.

**Shoemaker:** Overall, I'd say it's sort of net positive. I think there are definitely certain aspects of it that remain to be seen in terms of the impact on our borrower universe and our strategy. But overall, we feel pretty positive about the net impact.

Probably number one in terms of a positive impact would be increased economic activity. Given we target many owner-operator, private businesses, the kind of lower tax rates should provide a tailwind.

Another big one is the accelerated tax deductibility of capital expenditures. Our borrowers are typically taking our capital to expand, to acquire, to build new assets. And there's no doubt about it that accelerated depreciation can be a real driver of some of those capital decisions.

Kind of falling on the increased economic activity should lead to a boost in maybe energy infrastructure spending as part of that stimulus. And spending on alternative energy can also be viewed to accelerate due to some more favorable tax deductibility and other sort of demand-driven factors.

And then, the other is that higher interest rates that come from higher inflation make the relative difference between our cost of capital and traditional sources tighter and should drive, potentially, increased opportunity for us.

The only negative that we're evaluating is that tax deductibility of interest is obviously different. Now, it's capped at 30% of EBITDA, roughly, for the next several years and kind of getting more restrictive after that. So we don't expect that to have a material impact on our business, but it's one of the things that we're monitoring closely.

## **A CONSTRUCTIVE OIL PRICE ENVIRONMENT [8:37 – 10:49]**

**Kinney:** As a fan of Orion, I'll hope that the stuff that you highlighted as hopefully helping out your business will play out that way. I guess this is the point in our podcast where I get to ask our guest to pull out their crystal ball and talk about the future. Certainly, there's been a lot of turmoil over the last 24-48 months generally in the energy sector, but here's an opportunity to share with our listeners kind of your outlook for the near and longer term in the sector.

**Shoemaker:** Yeah. It's definitely been a dynamic 24 months. And I don't think we see any reason for that to change. Right now, the mood, I would say for multiple reasons, both we find ourselves

in a relatively constructive oil price environment, a relatively constructive economic environment, feels pretty good.

And so I think we are, and our borrowers, and I think also other capital providers to this space are generally pretty cautiously optimistic. And I think volatility is certainly helpful in some ways to creating opportunity, but as a lender, it's always a little bit better, I would say, to have some degree of stability. And it feels like we're in a relatively stable environment, at least for the time being. And so let's hope that continues.

**Kinney:** Well, I think the folks at BDO, certainly our energy and natural resources folks, tend to agree with you. I would certainly like to invite our listeners to read BDO's Energy 2020 Vision report. To learn more about our outlook for the oil and gas industry, you can find that report on [BDO.com](https://www.bdo.com).

So, Ethan, you're a busy man. I wish all the best to you and the team at Orion Energy. You're certainly a great brand in the marketplace. And we appreciate the relationship and finding ways to expand it. So thanks again for joining us.

**Shoemaker:** Yeah. Thanks for having me today. And thanks for all the support from BDO on all of our transactions. I look forward to continuing to work together.

**Kinney:** Great. Thanks for your time, Ethan.

For more information on how BDO supports private equity sponsors, funds, and their portfolio companies with a full spectrum of accounting, tax, and advisory services, please visit us at [BDO.com](https://www.bdo.com).

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