PZENA Investment Management

June 2020

# Fuel for Value Investors

**Pzena's Perspective**

*Concurrent oil demand and supply shocks led to a dramatic drop in the valuations of oil services businesses.*

The oil services industry is dependent on the capital expenditures (capex) of oil and natural gas producers.

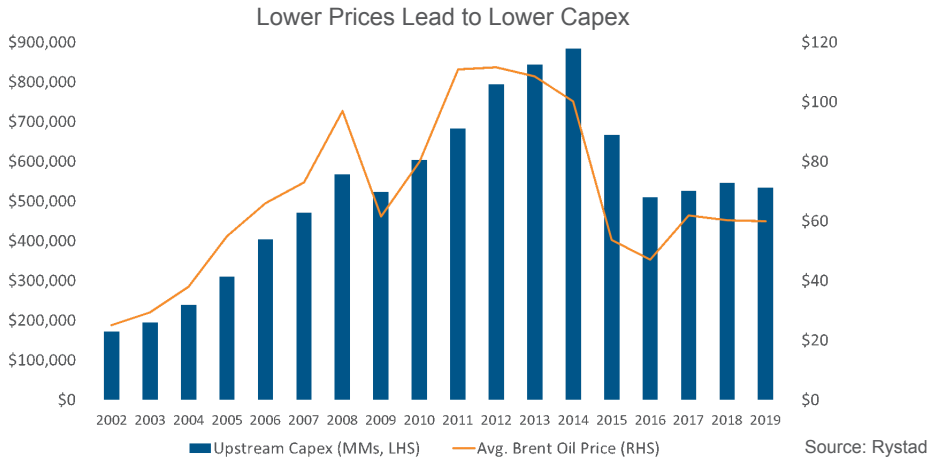
Oil services companies are feeling the pain of low oil prices and reduced capital spending by upstream companies.

The extent to which the capitalization of these companies fell is staggering; some by 90%* since 2014.

Oil service providers have a long history of riding the ups and downs in the energy market. They ramp up rigs and workers when oil is more expensive, and cut back when the market drops.

A clear relationship exists between upstream capex and the Brent crude price. Energy producers spend more on oil services when oil prices are high, and less when they are low.

While the market is speculating how quickly demand will recover and inventory will be drawn down, production cuts are occurring.




## With declining capex, where does this leave oil services business?

The leading franchises are taking aggressive action to protect their balance sheets and mitigate the effect of disruptions on their operations.

Current valuations of many oil services businesses reflect almost no possibility of higher oil prices or capital spending in the future.

Ultimately, low oil prices lead to low capex, leading to lower supply. Energy companies cannot maintain their current course without depleting reserves; oil production historically lags capex by three years. Therefore, capex must increase. The more resilient oil services companies are set up for profitable growth.

Extreme Opportunity for Oil Service Stocks

*Read on for our complete report on the opportunity in oil service stocks.*

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