

PHOENIX RISING

Since 2003, Doug Foshee has been working to lead El Paso Corp. back from the brink of disaster. Now that the turnaround is complete, what's next?

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Houston-based El Paso Corp. is turning a new leaf, involved now in two industries, down from 20 a few years ago, according to Doug Foshee, chief executive.

While there is no shortage of chief executives who enjoy hearing a compelling turnaround story, few may volunteer to be at the center of one. When Doug Foshee took the helm as president and chief executive of Houston-based El Paso Corp. in 2003, the company's turnaround odds were iffy at best.

El Paso principally produces and transports natural gas. With 56,000 miles of pipelines and 26% of total U.S. capacity, it operates the nation's largest interstate gas pipeline system. Its E&P segment is one of the largest domestic independent operators with 2.7 trillion cubic feet of gas equivalent of proved reserves.

In 2002 and 2003, however, the company was suffering: It was involved in the California energy crisis and swirling litigation and investigation; strategic decisions were called into question; debt mounted and the company lost its investment-grade credit rating; a harsh and public proxy fight ensued; and investors lost faith in the company, and its stock plummeted.

The company turned to Foshee to reverse El Paso's course. Once onboard, Foshee and the company's board announced a long-range plan to restructure its assets, lift it out of debt and renew investor confidence. In January, the company said its restructuring was complete.

For 2006, El Paso aims to generate net income of \$667- to \$735 million, and achieve \$3.4- to \$3.6 billion of EBITDA (earnings before interest, taxes, depreciation and amortization). It plans to invest \$2 billion of capex in its two core businesses: pipelines and E&P. Several pipeline expansions are under way, as well as major infrastructure expansion at its Elba Island liquefied natural gas regasification terminal near Savannah, Georgia. This year, Foshee expects to see the company's average daily production climb to 825 million cubic feet equivalent, and he plans to continue the process of divesting up to \$1.2 billion of noncore assets.

Prior to joining El Paso, Foshee was executive vice president and chief operating officer for Halliburton Co. and president, chief executive and chairman of Nuevo Energy Co. He also held various positions at Torch Energy Advisors Inc. and spent seven years in commercial banking, primarily as an energy lender.

Oil and Gas Investor sat down with Foshee

recently to talk about the new structure of the company, his plans for growth and why he took on the El Paso challenge.

Investor How close is El Paso looking like you want it to be in the long term?

Foshee There are still things that we lumped into the category of legacy issues, which we have yet to deal with, but that list has gone from what would have been an entire book of slides to just one slide. So we're very close.

Investor If this has nine innings, in what inning is the El Paso restructuring now?

Foshee I think the restructuring is done. In the context of the baseball analogy, the game and the season are over and we're starting a new season.

Investor Which of your moves so far has been the most difficult to implement?

Foshee It's hard to ignore the human impact of going from a company that employed more than 15,000 people to one that employs 5,500. The difficult decisions about which businesses we sold drove much of the reduction in headcount. In terms of what's been most challenging to implement, it's rebuilding the culture.

This company was built through acquisitions, and each of them came with a corporate identity and traditions that had been around a long



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Doug Foshee,
El Paso Corp.

time. You’re talking about the culture and traditions of El Paso Natural Gas, Sonat, Tenneco and Coastal. Add in a very bitter and public proxy battle and a reduction of employees by two-thirds, and you get a sense that being an employee for the last two or three years has been a tough thing. Trying to get people bought into the direction that we decided to take for the company in 2003 has been challenging. I think we’ve made a great deal of headway, but it’s a long-term process.

Investor What’s on the horizon for E&P acquisitions?

Foshee For El Paso, acquisitions need to be something that we have as an arrow in our quiver all the time. It’s more likely that for us, given the scale of our existing pipeline infrastructure, most of our growth on the pipeline side is likely to be organic. On the E&P side, we’re constantly looking for acquisitions that make sense, but we’re not going to leave our capital discipline behind. Acquisitions have gotten more expensive since we acquired Medicine Bow Energy, so at the margin I’d say they’re more difficult to do today than they were a year ago.

For perspective, we’re a significant producer in the Gulf of Mexico and South Texas. We have a significant asset base in coalbed methane in the Black Warrior, Arkoma and Raton basins, plus the Rockies. On the oil side and in conventional oil and gas we have a growing presence in the Rockies, in addition to our position in Brazil as the second-largest international oil company, with 15 concessions. Anything that would be additive to those would have a lower hurdle than something that would add a new core area.

Investor What percent of revenues and earnings will be pipeline versus E&P?

Foshee If natural gas prices stay at current levels, the percentage will be about two-thirds pipeline and one-third E&P. How it will change depends on commodity prices and whether or not we make any acquisitions; otherwise, I see both businesses growing at a healthy rate.

Investor Was El Paso a greater challenge than you expected?

Foshee No, but I’d say the turnaround of our E&P business was more challenging than I anticipated when I joined the company. That has been largely offset by the work of a new leadership team and the benefits of high commodity prices.

Investor How did previous positions prepare you for your current role at El Paso?

Foshee Every experience that you have in business, whether you made a correct decision or an incorrect decision, prepares you for the next step if you’re willing to learn from it. I’ve had the privilege of working with some great companies and I’ve also been in stressful situations that might be termed “turnarounds.”

I was fortunate to lead Nuevo Energy when West Texas Intermediate was \$12 or less, and

because we were a heavy-oil producer we received \$5 at the wellhead. I saw how companies in that kind of high-stress situation survive. At Halliburton, I was a part of something that was, for me, one of the most challenging periods of my career, responding to the broadside of asbestos litigation. I was part of the team that turned the company around and saw it go from \$8 a share to above \$80 today.

Investor How has El Paso added to that experience?

Foshee It’s been gratifying to have a chance to, in my view, do things the right way and have that be seen and appreciated by our employees after some very difficult years—and then seeing some success come out on the other side by sticking to a few things that we want to be really good at. It reinforces that there is a lot of value associated with not overcomplicating business, sticking to a few principles and not trying to be good at everything. Three years ago, El Paso was involved in more than 20 industries.

Investor What are the benefits of the \$1-billion Continental Connector pipeline project?

Foshee We rolled out that project publicly months ago and had a non-binding open season, which got us about 3 billion cubic feet a day of expressions of interest. We’re in the process of converting that interest into firm commitments, so we can do the final scoping for the project.

I not only think we’re the right company for the project, I think we’re the only company for it. It essentially links our Western pipes with our Eastern pipes and virtually every other market in the Eastern U.S. We believe if you’re a producer in the Rockies, the Midcontinent, the Barnett Shale, or even down in the East Texas Cotton Valley-Bossier area, there are aspects of this project that make a lot of sense from a producer’s viewpoint.

Investor Which moves in 2006 will have the most impact on El Paso?

Foshee We put a real stake in the ground with our E&P business when we reported our year-end reserves, which were up 22%, at an all-in finding and development cost of \$2.36, and a significantly increased reserve life. In 2005, we replaced 94% of production volumes by drilling; including acquisitions, we replaced 275% of production. The most important thing that will happen for us in 2006 is a year of achievement in E&P. It will be another year of growth and delivering projects on time and on budget in the pipeline business.

When you add both of those together, we forecast \$1 per share in earnings, \$14 billion in net debt by the end of the year, a \$2-billion capital program and \$400 million-plus in free cash flow. That is essentially at or above where we told people in 2003 that we would be in 2006, and that’s an accomplishment we’re really proud of. While it may not sound as dramatic as predicting some big acquisition for El Paso in 2006, my view is that the results we’re aiming for are equally as powerful. □