
From: Richard Kahn [REDACTED]
Sent: Wednesday, September 14, 2016 4:30 PM
To: jeffrey E.
Subject: Fwd: ***Buy HES convert preferred following a 15% drop in the stock....

Richard Kahn
HBRK Associates Inc.
575 Lexington Avenue 4th Floor
New York, NY 10022
tel [REDACTED]
fax [REDACTED]
cell [REDACTED]

Begin forwarded message:

From: "Ens, Amanda" [REDACTED]
Subject: ***Buy HES convert preferred following a 15% drop in the stock....
Date: September 14, 2016 at 11:05:05 AM EDT
To: [REDACTED]

Macro Focus: Oil is down modestly in front of EIA at 10:30am.... PI was modestly bullish (+1.44m bbl, gasoline - 2.39m, distillate =5.31m, Cushing crude -1.12m) with a smaller build and a Cushing draw, but people are willing to wait for EIA... All eyes will be on DOE data at 10:30am after last week's draw of 14.5mmb which was the biggest draw going back to 1999. This was the result of storms and related shutins. This kicked off a massive short squeeze where higher beta outperformed lower risk in last week's rising commodity price environment. The IEA weighed on group yesterday along with stronger dollar) as they said the oil glut will last longer than initially estimated.

HES is down over 15% in the last couple of weeks after results for their Skipjack well disappointed investors. We believe that "shorts" have piled on and see a potential opportunity to get long the stock into year-end as they are due to announce the result of the Liza #3 well in 4Q.

Conclusions....Skipjack disappointed and HES equity has more than paid the price. While the lack of imminent news may weigh following the exploration miss, Guyana is not discounted in shares, and Liza #3 is an event that investors will have to revisit in coming weeks. Next catalysts are the Liza #3 appraisal (4Q16) and Payara (early 2017). The Liza #3 well, has the potential to further de-risk a resource base for the play opening Liza discovery currently suggested by XOM at between 800mm -1.4bn boe. At the mid-point this represents a 30% increase in Hess' net oil & gas reserves at y/end 2015. Following Liza #3, it is entirely possible that XOM and its partners could have an exploration test every 3/4 months in a block that covers the equivalent of ~150 GoM blocks. Recognizing exploration has risk we assume no value for incremental success - but Liza may already represent a ~0% uplift in current production by early

next decade with world class economics, even at current oil prices. For now the focus remains on the \$10/share net to HES we believe has yet to be recognized.

Earn yield + upside into a pending exploration catalyst with the mandatory convertible preferred.

HES 8% 2/01/2019 at 59.50 (HES A Pfd)

- 6.8% strip yield, vs common stock at 2.1% div yield
- It converts with a low strike of \$39 (1.28 shares) and high strike of \$45.82 (1.09 shares) at maturity in 2019
- If stock is up 25%, the preferred returns 24.8%. If stock is up 50%, the preferred returns 46.4% (held to maturity)
- If stock is down 25%, the preferred returns -7.1%. If stock is down 50%, the preferred returns -32.4% (held to maturity)
- \$575mm notional, \$725mm market value outstanding (good liquidity)

(This is not a product of BAML Research)

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Amanda Ens
Director
Bank of America Merrill Lynch
Merrill Lynch, Pierce, Fenner & Smith Incorporated
One Bryant Park, 5th floor, New York, NY 10036

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