Matador Resources Co
Form 10-Q
August 05, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2016
OR
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission File Number 001-35410

Matador Resources Company
(Exact name of registrant as specified in its charter)

Texas	27-4662601
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
5400 LBJ Freeway, Suite 1500 Dallas, Texas	75240
(Address of principal executive offices)	(Zip Code)

(972) 371-5200
(Registrant’s telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. x Yes ¨ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). x Yes ¨ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer x	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). ¨ Yes x No

As of August 3, 2016, there were 93,307,151 shares of the registrant's common stock, par value $0.01 per share, outstanding.

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FORM 10-Q
FOR THE QUARTER ENDED JUNE 30, 2016
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Part I – FINANCIAL INFORMATION
Item 1. Financial Statements — Unaudited

Matador Resources Company and Subsidiaries
CONDENSED CONSOLIDATED BALANCE SHEETS - UNAUDITED
(In thousands, except par value and share data)

	June 30, 2016	December 31, 2015
ASSETS		
Current assets		
Cash	$40,873	$ 16,732
Restricted cash	460	44,357
Accounts receivable		
Oil and natural gas revenues	25,382	16,616
Joint interest billings	16,641	16,999
Other	5,137	10,794
Derivative instruments	117	16,284
Lease and well equipment inventory	3,002	2,022
Prepaid expenses	3,017	3,203
Total current assets	94,629	127,007
Property and equipment, at cost		
Oil and natural gas properties, full-cost method		
Evaluated	2,272,738	2,122,174
Unproved and unevaluated	397,883	387,504
Other property and equipment	122,374	86,387
Less accumulated depletion, depreciation and amortization	(1,802,464)	(1,583,659)
Net property and equipment	990,531	1,012,406
Other assets	928	1,448
Total assets	$ 1,086,088	$ 1,140,861
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$9,468	$ 10,966
Accrued liabilities	80,754	92,369
Royalties payable	16,646	16,493
Amounts due to affiliates	4,032	5,670
Derivative instruments	9,760	—
Advances from joint interest owners	5,783	700
Deferred gain on plant sale	5,903	4,830
Amounts due to joint ventures	3,522	2,793
Income taxes payable	—	2,848
Other current liabilities	210	161
Total current liabilities	136,078	136,830
Long-term liabilities		
Senior unsecured notes payable	391,845	391,254
Asset retirement obligations	18,498	15,166
Amounts due to joint ventures	3,228	3,956
Derivative instruments	7,538	—
Deferred gain on plant sale	99,286	102,506
Other long-term liabilities	7,086	2,190

Total long-term liabilities	527,481	515,072
Commitments and contingencies (Note 10)		
Shareholders’ equity		
Common stock - $0.01 par value, 120,000,000 shares authorized; 93,374,455 and 85,567,021 shares issued; and 93,290,199 and 85,564,435 shares outstanding, respectively	934	856
Additional paid-in capital	1,172,983	1,026,077
Retained deficit	(752,437)	(538,930)
Total Matador Resources Company shareholders’ equity	421,480	488,003
Non-controlling interest in subsidiaries	1,049	956
Total shareholders’ equity	422,529	488,959
Total liabilities and shareholders’ equity	$ 1,086,088	$ 1,140,861

The accompanying notes are an integral part of these financial statements.

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Matador Resources Company and Subsidiaries
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS - UNAUDITED
(In thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Revenues				
Oil and natural gas revenues	$69,336	$87,848	$113,262	$150,314
Realized gain on derivatives	2,465	13,780	9,528	32,285
Unrealized loss on derivatives	(26,625)	(23,532)	(33,464)	(32,090)
Total revenues	45,176	78,096	89,326	150,509
Expenses				
Production taxes and marketing	10,556	10,258	18,459	17,308
Lease operating	13,174	14,950	28,664	27,996
Depletion, depreciation and amortization	31,248	51,768	60,170	98,239
Accretion of asset retirement obligations	289	132	552	244
Full-cost ceiling impairment	78,171	229,026	158,633	296,153
General and administrative	13,197	12,961	26,360	26,372
Total expenses	146,635	319,095	292,838	466,312
Operating loss	(101,459)	(240,999)	(203,512)	(315,803)
Other income (expense)				
Net gain (loss) on asset sales and inventory impairment	1,002	—	2,067	(97)
Interest expense	(6,167)	(5,869)	(13,365)	(7,939)
Interest and other income	877	502	1,396	886
Total other expense	(4,288)	(5,367)	(9,902)	(7,150)
Loss before income taxes	(105,747)	(246,366)	(213,414)	(322,953)
Income tax provision (benefit)				
Deferred	—	(89,350)	—	(115,740)
Total income tax benefit	—	(89,350)	—	(115,740)
Net loss	(105,747)	(157,016)	(213,414)	(207,213)
Net income attributable to non-controlling interest in subsidiaries	(106)	(75)	(93)	(111)
Net loss attributable to Matador Resources Company shareholders	$(105,853)	$(157,091)	$(213,507)	$(207,324)
Earnings (loss) per common share				
Basic	$(1.15)	$(1.89)	$(2.40)	$(2.65)
Diluted	$(1.15)	$(1.89)	$(2.40)	$(2.65)
Weighted average common shares outstanding				
Basic	92,346	82,938	88,826	78,379
Diluted	92,346	82,938	88,826	78,379

The accompanying notes are an integral part of these financial statements.

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Matador Resources Company and Subsidiaries
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY - UNAUDITED
(In thousands)
For the Six Months Ended June 30, 2016

	Common Stock		Additional paid-in capital	Retained deficit	Treasury Stock		Total shareholders' equity attributable to Matador Resources Company	Non-controlling interest in subsidiary	Total shareholders' equity
	Shares	Amount			Shares	Amount			
Balance at January 1, 2016	85,567	$ 856	$ 1,026,077	$ (538,930)	2	$ —	$ 488,003	$ 956	$ 488,959
Issuance of common stock	7,500	75	142,275	—	—	—	142,350	—	142,350
Cost to issue equity	—	—	(830)	—	—	—	(830)	—	(830)
Stock-based compensation expense related to equity-based awards	—	—	5,464	—	—	—	5,464	—	5,464
Stock options exercised	11	—	—	—	—	—	—	—	—
Restricted stock issued	273	3	(3)	—	—	—	—	—	—
Restricted stock forfeited	—	—	—	—	82	—	—	—	—
Vesting of restricted stock units	24	—	—	—	—	—	—	—	—
Current period net loss	—	—	—	(213,507)	—	—	(213,507)	93	(213,414)
Balance at June 30, 2016	93,375	$ 934	$ 1,172,983	$ (752,437)	84	$ —	$ 421,480	$ 1,049	$ 422,529

The accompanying notes are an integral part of these financial statements.

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Matador Resources Company and Subsidiaries
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS - UNAUDITED
(In thousands)

	Six Months Ended June 30,	
	2016	2015
Operating activities		
Net loss	$(213,414)	$(207,213)
Adjustments to reconcile net loss to net cash provided by operating activities		
Unrealized loss on derivatives	33,464	32,090
Depletion, depreciation and amortization	60,170	98,239
Accretion of asset retirement obligations	552	244
Full-cost ceiling impairment	158,633	296,153
Stock-based compensation expense	5,553	5,131
Deferred income tax benefit	—	(115,740)
Amortization of debt issuance cost	592	—
Net (gain) loss on asset sales and inventory impairment	(2,067)	97
Changes in operating assets and liabilities		
Accounts receivable	(2,751)	(12,161)
Lease and well equipment inventory	(514)	(269)
Prepaid expenses	186	(1,143)
Other assets	520	446
Accounts payable, accrued liabilities and other current liabilities	2,451	13,316
Royalties payable	153	4,253
Advances from joint interest owners	5,083	447
Income taxes payable	(2,848)	(444)
Other long-term liabilities	3,837	(56)
Net cash provided by operating activities	49,600	113,390
Investing activities		
Oil and natural gas properties capital expenditures	(162,381)	(237,027)
Expenditures for other property and equipment	(47,548)	(32,885)
Business combination, net of cash acquired	—	(23,671)
Restricted cash	43,437	—
Restricted cash in less-than-wholly-owned subsidiaries	460	(413)
Net cash used in investing activities	(166,032)	(293,996)
Financing activities		
Repayments of borrowings	—	(476,982)
Borrowings under Credit Agreement	—	125,000
Proceeds from issuance of senior unsecured notes	—	400,000
Cost to issue senior unsecured notes	—	(8,789)
Proceeds from issuance of common stock	142,350	188,720
Cost to issue equity	(768)	(1,172)
Proceeds from stock options exercised	—	10
Capital contribution from non-controlling interest owners in less-than-wholly-owned subsidiaries	—	600
Taxes paid related to net share settlement of stock-based compensation	(1,009)	(1,565)
Net cash provided by financing activities	140,573	225,822
Increase in cash	24,141	45,216
Cash at beginning of period	16,732	8,407

Cash at end of period	$40,873	$53,623

Supplemental disclosures of cash flow information (Note 11)

The accompanying notes are an integral part of these financial statements.
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Matador Resources Company and Subsidiaries
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED
NOTE 1 - NATURE OF OPERATIONS
Matador Resources Company, a Texas corporation ("Matador" and, collectively with its subsidiaries, the "Company"), is an independent energy company engaged in the exploration, development, production and acquisition of oil and natural gas resources in the United States, with an emphasis on oil and natural gas shale and other unconventional plays. The Company's current operations are focused primarily on the oil and liquids-rich portion of the Wolfcamp and Bone Spring plays in the Delaware Basin in Southeast New Mexico and West Texas. The Company also operates in the Eagle Ford shale play in South Texas and the Haynesville shale and Cotton Valley plays in Northwest Louisiana and East Texas.
NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
Interim Financial Statements, Basis of Presentation, Consolidation and Significant Estimates
The interim unaudited condensed consolidated financial statements of Matador and its subsidiaries have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission ("SEC") but do not include all of the information and footnotes required by generally accepted accounting principles in the United States of America ("U.S. GAAP") for complete financial statements and should be read in conjunction with the Company's audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2015 (the "Annual Report") filed with the SEC. The Company proportionately consolidates certain subsidiaries that are less-than-wholly-owned and the net income and equity attributable to the non-controlling interest in these subsidiaries have been reported separately as required by Accounting Standards Codification ("ASC") 810. The Company proportionately consolidates certain joint ventures that are less-than-wholly-owned and are involved in oil and natural gas exploration. All intercompany accounts and transactions have been eliminated in consolidation. In management's opinion, these interim unaudited condensed consolidated financial statements include all adjustments, consisting only of normal, recurring adjustments, which are necessary for a fair presentation of the Company's interim unaudited condensed consolidated financial statements as of June 30, 2016. Amounts as of December 31, 2015 are derived from the Company's audited consolidated financial statements in the Annual Report.
The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. These estimates and assumptions may also affect disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The Company's interim unaudited condensed consolidated financial statements are based on a number of significant estimates, including accruals for oil and natural gas revenues, accrued assets and liabilities primarily related to oil and natural gas operations, stock-based compensation, valuation of derivative instruments and oil and natural gas reserves. The estimates of oil and natural gas reserves quantities and future net cash flows are the basis for the calculations of depletion and impairment of oil and natural gas properties, as well as estimates of asset retirement obligations and certain tax accruals. While the Company believes its estimates are reasonable, changes in facts and assumptions or the discovery of new information may result in revised estimates. Actual results could differ from these estimates.
Change in Accounting Principle
During the second quarter of 2016, the Company adopted Accounting Standards Update ("ASU") 2016-09, Compensation - Stock Compensation (Topic 718), which simplifies several aspects of the accounting for employee share-based payment transactions, including accounting for income tax, forfeitures, statutory tax withholding requirements, classifications of awards as either equity or liability and classification of taxes in the statement of cash flows, requiring either retrospective, modified retrospective or prospective transition. The amended guidance also requires an entity to record excess tax benefits and deficiencies in the income statement. The adoption of this ASU had no impact on any period presented for (i) the Company's financial position or statements of operations, as the Company currently has a valuation allowance against its net deferred tax assets, or (ii) the Company's statements of cash flows, as the Company has historically accounted for taxes paid for net share settlement as a financing activity as required under this ASU. In addition, the Company uses historical forfeiture rates to estimate future forfeitures

attributable to the service-based vesting requirements not being met and will continue to do so upon adoption of this ASU.

Property and Equipment

The Company uses the full-cost method of accounting for its investments in oil and natural gas properties. Under this method, the Company is required to perform a ceiling test each quarter which determines a limit, or ceiling, on the capitalized costs of oil and natural gas properties based primarily on the after-tax estimated future net cash flows from oil and natural gas properties using a 10% discount rate and the arithmetic average of first-day-of-the-month oil and natural gas prices for the prior

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

12-month period. Due primarily to declines in oil and natural gas prices, the capitalized costs of oil and natural gas properties exceeded the cost center ceiling, and as a result, the Company recorded impairment charges to its net capitalized costs in its unaudited condensed consolidated statements of operations of $78.2 million and $229.0 million for the three months ended June 30, 2016 and 2015, respectively, and $158.6 million and $296.2 million for the six months ended June 30, 2016 and 2015, respectively.

As a non-cash item, the full-cost ceiling impairment impacts the accumulated depletion and the net carrying value of the Company’s assets on its consolidated balance sheet, as well as the corresponding consolidated shareholders’ equity, but it has no impact on the Company’s consolidated net cash flows as reported. Changes in oil and natural gas production rates, oil and natural gas prices, reserves estimates, future development costs and other factors will determine the Company’s actual ceiling test computation and impairment analyses in future periods.

The Company capitalized approximately $4.0 million and $1.9 million of its general and administrative costs for the three months ended June 30, 2016 and 2015, respectively, and approximately $1.7 million and $1.3 million of its interest expense for the three months ended June 30, 2016 and 2015, respectively. The Company capitalized approximately $6.0 million and $3.5 million of its general and administrative costs for the six months ended June 30, 2016 and 2015, respectively, and approximately $2.2 million and $2.3 million of its interest expense for the six months ended June 30, 2016 and 2015, respectively.

Earnings (Loss) Per Common Share

The Company reports basic earnings (loss) per common share, which excludes the effect of potentially dilutive securities, and diluted earnings (loss) per common share, which includes the effect of all potentially dilutive securities unless their impact is anti-dilutive.

The following table sets forth the computation of diluted weighted average common shares outstanding for the three and six months ended June 30, 2016 and 2015 (in thousands).

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Weighted average common shares outstanding				
Basic	92,346	82,938	88,826	78,379
Dilutive effect of options, restricted stock units and preferred shares	—	—	—	—
Diluted weighted average common shares outstanding	92,346	82,938	88,826	78,379

A total of 2.9 million options to purchase shares of the Company’s common stock and 0.1 million restricted stock units were excluded from the diluted weighted average common shares outstanding for both the three and six months ended June 30, 2016, respectively, because their effects were anti-dilutive. Additionally, 0.9 million restricted shares, which are participating securities, were excluded from the calculations above for both the three and six months ended June 30, 2016, respectively, as the security holders do not have the obligation to share in the losses of the Company.

A total of 2.5 million options to purchase shares of the Company’s common stock and 0.1 million restricted stock units were excluded from the diluted weighted average common shares outstanding for both the three and six months ended June 30, 2015, respectively, and zero and 1.5 million preferred shares were excluded from the calculations above for both the three and six months ended June 30, 2015, respectively, because their effects were anti-dilutive. Additionally, 0.7 million restricted shares, which are participating securities, were excluded from the calculations above for both the three and six months ended June 30, 2015, respectively, as the security holders do not have the obligation to share in the losses of the Company.

Recent Accounting Pronouncements

Revenue from Contracts with Customers. In May 2014, the Financial Accounting Standards Board ("FASB") issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), which specifies how and when to recognize revenue. In addition, this standard requires expanded disclosures surrounding revenue recognition and is intended to improve, and converge with international standards, the financial reporting requirements for revenue from contracts with customers. This ASU will become effective for fiscal years beginning after December 15, 2017 with early adoption permitted for periods beginning after

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Matador Resources Company and Subsidiaries
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED - CONTINUED

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

December 15, 2016. Entities can transition to the standard either retrospectively to each period presented or as a cumulative-effect adjustment as of the date of adoption. The Company is currently evaluating the impact, if any, of the adoption of this ASU on its consolidated financial statements.

Leases. In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), which requires the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous U.S. GAAP. This ASU will become effective for fiscal years beginning after December 15, 2018 with early adoption permitted. Entities are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. The modified retrospective approach includes a number of optional practical expedients that entities may elect to apply. These practical expedients relate to the identification and classification of leases that commenced before the effective date, initial direct costs for leases that commenced before the effective date and the ability to use hindsight in evaluating lessee options to extend or terminate a lease or to purchase the underlying asset. The Company is currently evaluating the impact of the adoption of this ASU on its consolidated financial statements.

NOTE 3 - EQUITY

On March 11, 2016, the Company completed a public offering of 7,500,000 shares of its common stock. After deducting offering costs totaling approximately $0.8 million, the Company received net proceeds of approximately $141.5 million, which are being used for general corporate purposes, including to fund a portion of the Company's current and future capital expenditures.

NOTE 4 - ASSET RETIREMENT OBLIGATIONS

The following table summarizes the changes in the Company's asset retirement obligations for the six months ended June 30, 2016 (in thousands).

Beginning asset retirement obligations	$15,420
Liabilities incurred during period	1,044
Liabilities settled during period	(119)
Revisions in estimated cash flows	1,662
Accretion expense	552
Ending asset retirement obligations	18,559
Less: current asset retirement obligations[1]	(61)
Long-term asset retirement obligations	$18,498

(1) Included in accrued liabilities in the Company's interim unaudited condensed consolidated balance sheet at June 30, 2016.

NOTE 5 - DEBT

At June 30, 2016 and August 3, 2016, the Company had $400 million of outstanding 6.875% senior notes due 2023 (the "Notes"), no borrowings outstanding under the Company's revolving credit agreement (the "Credit Agreement") and approximately $0.6 million and $0.8 million in outstanding letters of credit issued pursuant to the Credit Agreement, respectively.

The borrowing base under the Credit Agreement is determined semi-annually as of May 1 and November 1 by the lenders based primarily on the estimated value of the Company's proved oil and natural gas reserves at December 31 and June 30 of each year, respecti