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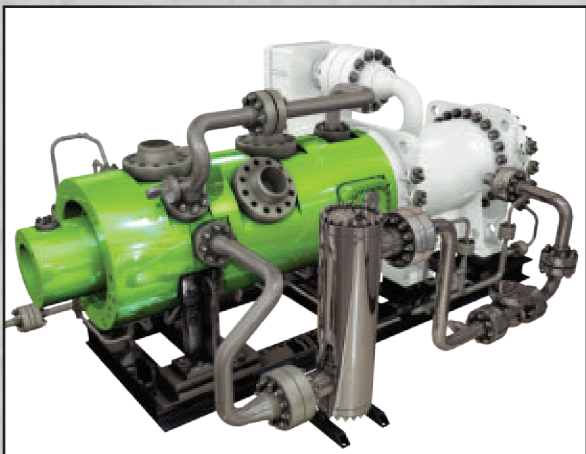

U.S. Compression Industry Poised For Growth In 2012

2011 Year In Review

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U.S. COMPRESSION INDUSTRY POISED FOR GROWTH IN 2012

James Barr says new shale plays are boosting demand for motor-driven and H_2S capable packages

By Patrick Crow

James R. Barr is sales and marketing manager at J-W Power Co. and the immediate past chairman of the Gas Compressor Association.

Editor's Note: *James R. Barr, sales and marketing manager for J-W Power Co., predicts the compression industry will grow in 2012 despite relatively low prices for natural gas. He said newer shale plays are increasing requests for electric motor-driven packages and units designed for hydrogen sulfide gas.*

J-W Power is one of the largest privately held gas compression companies in the United States. A service company subsidiary of J-W Energy Co., it specializes in gas compression rental, sales and service as well as high-pressure air injection, compressed natural gas (CNG) fueling compressors, storage spheres and ancillary equipment.

Barr was recently interviewed by COMPRESSORTech^{Two}.

What kind of a year has 2011 been for J-W Power Co.?

Given the continuing stressful economic environment of 2011, I would rate 2011 an A minus in terms of execution of our business plan, and the marketplace a C minus in terms of the opportunities to deploy our fleet equipment at rates that are profitable.

Equipment sales were our bright spot, and the strength of that market was both welcome and somewhat surprising to all of us since natural gas prices were so low.

Small segments of the rental market have exhibited a lot of strength and, with equipment in very short supply, the rental rates are strong and have allowed us to continue to invest capital in new equipment for the rental fleet — although not at our normal levels.

One area of disappointment has been the continued increase in the cost of major components which, to some degree, has depressed the volume of new rental unit fabrication in our industry segment. At the end of the day, we have to produce a rate of return on our equipment. It becomes more difficult in this type of environment and depresses investment.

What's the outlook for 2012?

Next year looks to be very similar to 2011. With all the new gas coming onstream, and a lot still behind the pipe, I don't look for a substantial movement in gas prices for the next year or two. The political environment may change in 2012 but not nearly enough to impact the industry.

We need for Americans to get back to work to increase demand and bring on additional consumption requirements.

Natural gas is still a favored fuel by most consumers, but politically, the government subsidies are going toward high-electricity-cost solutions such as wind and solar, and not to natural gas — the appropriate bridge fuel for the future. J-W Power would like to see much more political focus on natural gas for transportation fuel and for electricity generation demands.

Around the world, nations that compete with us economically are much more advanced in their efforts to use natural gas to offset their oil imports.

How did 2011 compare with previous years?

As with most companies, we pulled back our capital investments for fleet growth early in the recession. We focused more on new markets for our products and increased our efforts with product sales.

Since early 2006, one of our operational focus issues has been compliance with the new U.S. Environmental Protection Agency (EPA) regulations for reciprocating internal combustion engines.

We have developed internal electronic solutions that place the data at our fingertips and that allow us to both serve our customers and provide equipment solutions to help them with their compliance issues.

I would like to claim that we are ahead of the game, but there seems to be something new every month and we have to add a feature or a service to remain in compliance. In this economy, these have been difficult pills to swallow. It's not always possible for us to recoup a reasonable portion of the increased costs.

Our customer base continues to be very supportive of our efforts to maintain our high level of service in conjunction with our efforts to control our costs. We have made investments in robotics in our fabrication facility, placed CNG-fueled vehicles in our service groups and introduced some innovative engineering solutions to reduce our expendable costs on our packages in the field — all without sacrificing mechanical availability, package quality or safety of operation.

What was the largest challenge facing your company this year? What about next year?

We were fortunate to have stable operations in place to handle both the expansion of our Marcellus Shale and Eagle Ford Shale regions, but on the service side, training and retaining personnel has been a continuing challenge.

Training of personnel for the new engine and control technologies is always a challenge, as well as implementation of better cost controls and inventory strategies to remain profitable.

For 2012, our biggest challenge is to continue our current efforts and also prepare for the tougher National Emissions Standards for Hazardous Air Pollutants. This will be a huge undertaking for our industry and for J-W Power, although we have performed a lot of preparatory work leading up to implementation of the emissions requirements.

Were there any other noteworthy events related to your company or its primary markets in 2011?

We have continued our expansion with three new facilities in the northeastern United States, the latest of which will open in late 2011 at Muncy Creek, Pennsylvania, U.S.A., to better service the growth of Marcellus Shale gas production.

We also have invested in our current facilities for better tooling, inventory control and increased capability on our third-party service efforts.

One of my focus areas has been to strengthen our supplier relationships and work closely with our manufacturing group to give it consistent direction on the needs of the marketplace. With less new equipment being built for the rental fleet, it has been both challenging and exciting to come up with strategies to deploy our idle equipment and encourage more package sales.

We were very excited to close some sales in international markets that we had targeted for development in 2011 and look forward to more opportunities overseas.

What products or services will J-W Power Co. focus on in 2012?

I joke with our engineering group that "If it ain't broke, don't fix it," but they're always trying to add more features.

Our service offering may change slightly in 2012, but our focus still will be to offer constant improvements and innovations to our product offerings. We try to be nimble and react quickly to market changes with new strategies.

New package sales to supplement our rental fleet fabrication will be an ongoing focus. We will build on our previous successes in international markets and CNG equipment fabrication as well as continue to expand our service offerings for customer-owned units.

I think our knowledge of emissions equipment and regulations will be a key component of our success in 2012, leading into 2013.

Do you have any particular problems regarding the cost and availability of raw materials or spare parts?

We are seeing increases in the cost of specialty steel for vessels and skids as well as increasing lead times. Major components, such as engines, compressors and coolers, continue to increase in cost on a regular basis. Lately, the lead times have accelerated for the most popular models.

In visits with our suppliers, they also are seeing shortages, cost increases and longer lead times on the components supplied to them.

Regarding the compression industry as a whole, how did 2011 compare with recent years?

This year was better than 2010. Business in our industry stabilized and more capital investment was made than in 2009.

Noteworthy events were mostly on the regulatory side and concerned greenhouse gas emissions as well as the ratcheting up of other regulations. Of particular concern was the public reaction to hydraulic fracturing technology and how it has affected the ability of our customers to obtain permits to continue their development efforts.

The BP oil spill in the Gulf of Mexico last year, in conjunction with other specific pipeline events and the tsunami in Japan, has given critics more ammunition against the energy business as a whole.

Cooler heads must prevail in government to explain our energy dilemma to the public and move toward reasonable strategies to reduce our reliance on foreign oil.

What are your thoughts on market conditions for 2012?

I am an eternal optimist and a practicing realist. I see signs that compression businesses will improve in 2012, even with natural gas prices in the US$3 to US$4 per Mcf range. I am concerned about the volumes of gas that are subject to hedging strategies and how the expiration of those hedges will impact capital investments in the pure gas play areas.

Also of concern is our economy and its ability to rebound and create demand growth for natural gas. Oil prices are projected to remain at or above our current levels, which bodes well

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for the compression of gas produced in association with oil. Development of oil assets will be strong as the major companies continue to balance their energy portfolios.

What was the most surprising/ unusual development in the gas compression industry in 2010?

It was not really surprising, but we have seen a significant number of requests for electric motor-driven equipment for both sales and rental. With the development of the oil shale plays, rich, high BTU gas is a component of the wellhead stream. Most modern engines will not tolerate the rich fuel, and we foresee increased demand for electric motor-driven packages as well as fuel gas conditioning skids for the larger sites.

Another surprise has been the presence of varying amounts of hydrogen sulfide in gas from the Eagle Ford Shale in South Texas, U.S.A. We should also see an increase in the demand for H_2S trim and National Association of Corrosion Engineers specifications for custom builds, as well as significantly higher rental rates for units placed into H_2S rental service.

How do you see evolving government energy policy decisions affecting the gas machinery business in the next 12 months or longer?

We are concerned about the direction of federal energy policy in several areas. Legislators continue to postpone energy policy decisions and take a broad-brush approach to the issues. We are also concerned about the EPA's policies and instability in their decision-making process.

The atmosphere of "What next?" is downright scary for our industry. With local governments, we often see a lack of sound logic behind their regulatory requirements in areas such as noise reduction requirements for compression sites.

What major technological advances have you seen in the industry in recent years?

I think advances in engine technology have been amazing. The speed at which manufacturers have brought products to market in conjunction with the development of the diesel engines to meet the required emissions timelines was surprising.

On the business side of the compression industry, do you see any particular trends that are different from those of the recent past?

We generally have seen fewer acquisitions and consolidations by compression companies, although the appetite for investment by venture capital has been evident. It appears that most companies are working within their cash flow and their fleet expansion has slowed in recent years.

What is the compression industry's biggest challenge in meeting its customer needs?

The challenge never seems to change: We must provide quality equipment that operates 105% of the time at 105% of capacity. We must maintain it to provide compliance with regulatory requirements. And it needs to be in stock for delivery tomorrow at a price below our cost to fabricate.

Obviously, I'm kidding, although there's a lot of truth behind what I say.

I think that in this environment of reduced investment, the challenge for compression companies is to reassure customers that their future needs will be met and work as partners with the industry.

If those needs change, customers also want the flexibility to change direction in advance of equipment procurement. That must be done without endangering the commercial and financial needs of the compression company as well as the producers.