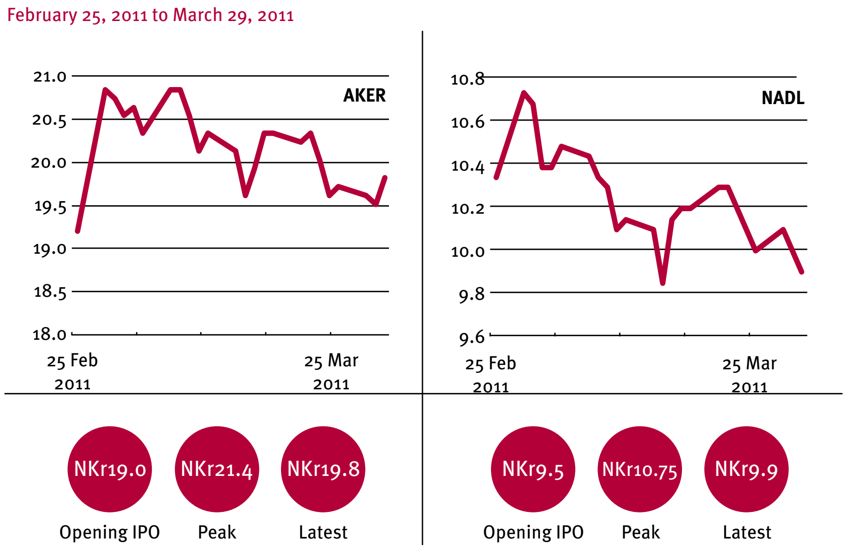
Investor appetite for drilling rig exposure prompts spin-offs

With demand for shares still strong, the offshore sector looks likely to see a variety of fresh public offerings

Barry Parker — New York

AKER DRILLING AND NORTH ATLANTIC DRILLING
February 25, 2011 to March 29, 2011



Source: Argo Securities

PERFORMANCE of recent drilling initial public offerings has been flat to slightly positive.

Anders Bergland, from the RS Platou Markets oil services research team, told Lloyd's List that Aker Drilling was issued at NKr19 ($3.41) per share. As of Thursday March 30 it was trading at NKr19.8 — up more than 2.5% from its IPO price after trading up as high as NKr21.4.

Mr Bergland added that North Atlantic Drilling was issued at NKr9.5 after an adjustment for foreign exchange. He said that the shares peaked at NKr10.75. Their price at close of trading on Wednesday was NKr9.9.

Janne Kvernland, oil services analyst at Argo Securities, said: "I think we need to see higher ultra-deepwater rates before we see a run in the share price." She added: "Other triggers are new contracts or consolidation news in the sector, for instance."

Mr Bergland emphasised: "The investor appetite for rig exposure appears to be very strong, and we do not rule out that there is still more to come within the offshore segment."

Egle Domataite, offshore team leader at Terra Markets, said: "I am aware that there are plans to list Pacific Drilling, a company with six new ultra-deepwater drillships, five of them yet to be delivered."

Mr Bergland and a colleague at RS Platou Markets, Herman Hildan, issued a "Buy" recommendation on Sevan Marine, which will maintain its existing floating production, storage and offloading vessels business (including a unit to be deployed at Goliat) while owning 20% of a planned spin-off of its ultra-deepwater drilling assets as Sevan Drilling.

In their report, they estimated an all-in cost of $570m (figuring in a return on the equity component, in addition to the announced $525m), for each of two newbuilding rigs which they characterised as "...a 5% discount to the alternative". The analysts argue for a valuation of the Sevan Driller and Sevan Brasil at $650m each and said that they expected other counterparties besides Petrobras to consider the benefits of the cylindrical hulls.

The objective of spin-offs, ultimately, is to increase shareholder value in the initial entity. In this exercise, the sale to investors of new Sevan Drilling shares is coupled with the sale of shares owned by Sevan Marine. It is this "sell-down" of owned shares that brings in cash. The RS Platou analyst team expects the sell-down to be worth approximately $160m-$170m. Sevan Marine's financial balance sheet would be further enhanced by a holding of 20% interest in Sevan Drilling (reckoned to be worth approximately $129m after the dust settles). In their report, the Platou team thoroughly dissected Sevan's highly complicated debt structure, and estimated debt tied to the Sevan Marine FPSO business to have been some $930m at the end of last year.

Ms Domataite, from Terra Markets, captured the big picture view of the Sevan transaction, explaining to Lloyds List: "Sevan is underpriced, in my view, on both an absolute basis and relative to its peers. The business split could unlock some value on the company, as both entities (FPSO and Drilling) would have a specific focus area and become easier takeover targets."

She also commented that the cycle of listings, and then consolidation, would benefit underpriced companies most, "and I see Sevan as such".

When asked about the potential for similar deals, Janne Kvernland, from Argo Securities, said: "I would say that Transocean and Maersk are the only players with a fleet big enough to make it sensible with a spin-off like this at the moment." She added: "I do not think that it is very likely in the short term."

Ms Kvernland talked about other types of spin-offs, mentioning "region-wise" spin-offs, for example, in Brazil.

She also talked about "asset-based" spin-offs, noting that: "Transocean, for instance, considers to spin off older parts of its fleet. I think we may see more of that, too."

In the same vein, she described situations in which the spin-off a jack-up fleet could create a totally new company. ■

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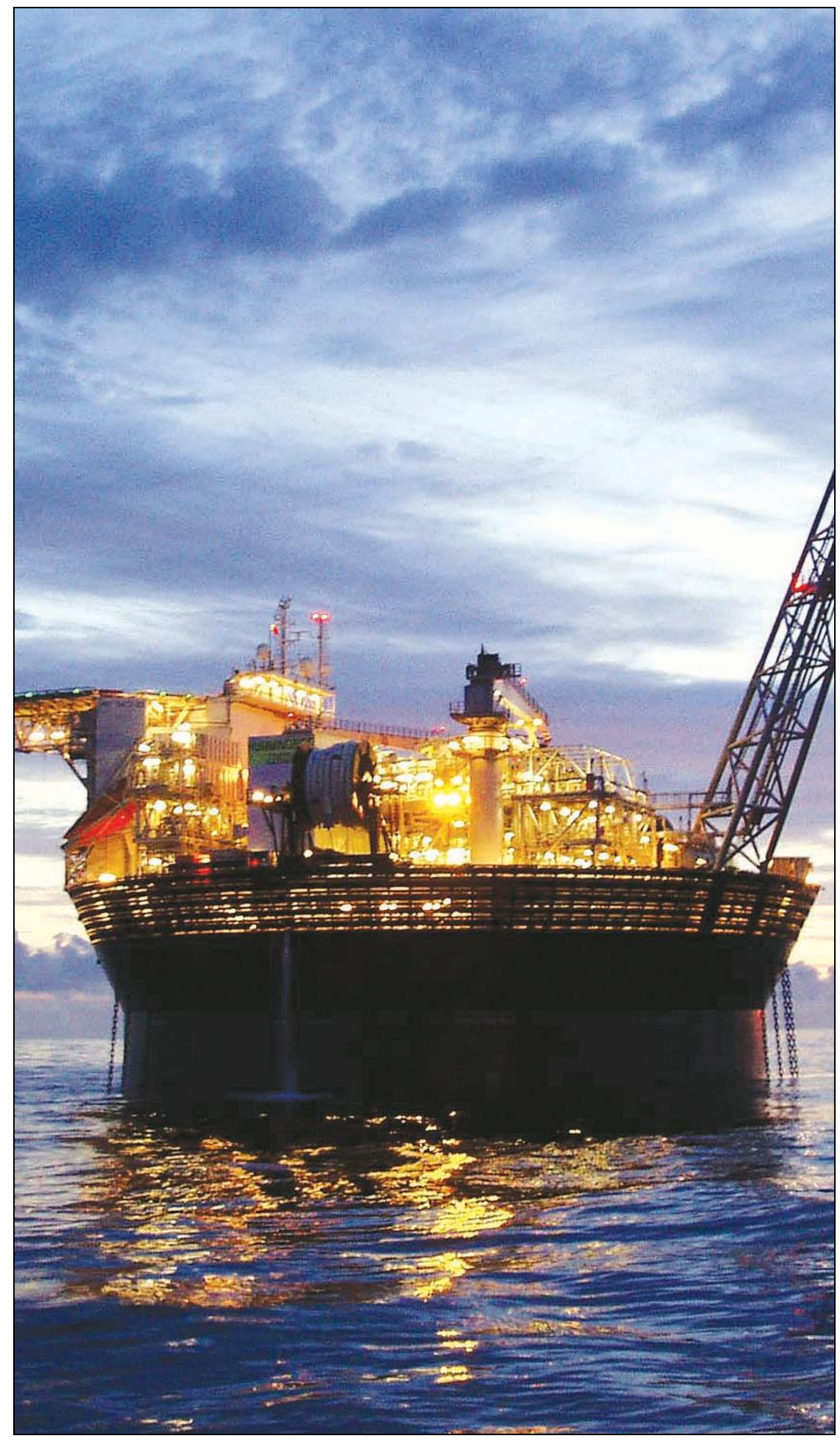

One of Sevan's cylindrical drilling units, the Sevan Hummingbird: Sevan Marine plans a spin-off of its ultra-deepwater drilling assets, but will keep a stake in them and also retain its FPSO business.

> *"Sevan is underpriced, in my view, on both an absolute basis and relative to its peers. The business split could unlock some value on the company"*
> ***Egle Domataite, offshore team leader at Terra Markets***

Seven reveals April drilling IPO to raise up to $350m

EQUIPMENT owners are mustering financial resources to support outsized capital expenditure programmes for harsh environments or ultra-deepwater.

In Aker's case, cash flows from the harsh environment semi-submersibles provide the platform as the company gears up for worldwide ultra-deep growth.

Aker Drilling has placed orders with Daewoo Shipbuilding and Marine Engineering for two ultra-deepwater drillships, expected to cost around $600m each, for delivery in late 2013. Options, to be declared during the course of this year, would provide for construction of two additional drillships, to be delivered in 2014 and 2015, if exercised.

In conjunction with its February initial public offering, Aker Drilling raised NKr1.5bn ($268.1m) in an offering of unsecured high-yield bonds maturing in February 2016, a time when Aker Drilling cash flows could be substantial. Simultaneously, a new NKr900m banking facility was agreed, refinancing an existing NKr600m bank credit. After the dust settled on the Sources and Uses of Funds statements, Aker Drilling is able to fund its requisite 25% deposits on the two firm DSME drillships (which, unlike the semi-submersibles, are not suitable for harsh environments).

Sevan Marine, best known for its cylindrical drilling units and FPSOs, will keep its three existing production units and three newbuildings, including one to be deployed by Eni at the Goliat field, while the drilling units will be joining the spin-off club. Last week, it announced a likely public share offering in April that will create a new company, Sevan Drilling, for its ultradeepwater drilling assets.

Sevan Marine (the present owner) already has one ultra-deepwater round rig, Sevan Driller, on a six-year charter to Petrobras, at $402,000 per day. A second unit is scheduled to deliver in the second quarter of 2012, to begin a charter to the Brazilian oil giant at a number working back to $442,000 per day. The second unit, to be named Sevan Brasil, will also be drilling with a six-year duration.

At the same time that Sevan Marine revealed the IPO intentions, it also announced a Letter of Intent for building two new cyclindrical drilling rigs at the Cosco Nantong yard, which the company said were priced at $525m each with deliveries in the last quarter of 2014 and third quarter of 2015. As is customary, options were granted for an additional two units. These newbuildings (and optional units, if declared) will also go into the new company.

The IPO, expected to be $350m, will see new Sevan Drilling shares issued to investors, followed by a further sell-down of Sevan Drilling shares owned by Sevan Marine. Cash inflows from share sales will fund downpayments on the two new units.

The newfound cash will allow Sevan Marine, now with a strengthened balance sheet, to raise additional debt finance to support its floating production, storage and offloading vessel construction programme. Fitting a pattern, such refinancing is closely tied to spinoffs.

As it announced the IPO, Sevan Marine already drew down $480m of fresh finance, tied to Sevan Driller, which will be used to pay off existing first and second mortgage bank debt, and to pay off holders of a NKr1bn bond that was issued in late 2006. ■

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Total drilling plans to boost Barents Sea exploration

TOTAL has announced that it will be drilling for gas at the Norvag gas field, about 200 miles above Hammerfest, in partnership with Det Norske Oljeselskap and others, *writes Barry Parker*.

The well will be the first within a concession awarded in the Norwegian Petroleum Directorate's 20th licensing round, one of nine in the Barents Sea.

The region has not been without its challenges; in recent months, Statoil, employing the Transocean Polar Pioneer hit a dry well at a Barents field, while Eni had also come up dry drilling in the Lunde field, about 30 miles west of the better known Goliat field.

In the Norwegian Sea, Shell plugged a well last December after failing to strike oil at Dalnuten, while employing the Aker Barents. That advanced semi-submersible rig was subsequently remobilised by Det Norske, which has the unit at $520,000 per day until 2012, to drill at the nearby Dovregubben well, which also came up dry.

The rig will now be moving on to drill at the Gullris prospect, operated by BG with Det Norske having a 20% stake. Gullris shares a geological trend with the Gro field where Shell has made significant oil finds.

The northern reaches of the Norwegian Sea and the adjacent Barents Sea are again on the radar of drilling analysts and their peers who pay close attention to corporate finance. Harsh environment drilling, along with ultra-deepwater drilling, is closely intertwined with moves into new financial environments.

Bankers and investors have not been put off by the occasional dry well. The West Phoenix, an advanced semi-submersible which is two years into a three-year contract to Total at a dayrate of $530,000, is one of six rigs that has moved into the newly formed North Atlantic Drilling, valued at $1.7bn in mid February after its spin-off from Seadrill. Following an oversubscribed private placement for $425m, Seadrill retains a 75% stake.

To complete the picture, Aker Exploration, which had been employing the Aker Barents on charter since the autumn of 2009, merged with the much larger Det Norske in late 2009. Almost simultaneously with Seadrill's spin-off, Aker Drilling, owner of the rig (along with the sister Aker Spitzbergen) successfully raised $635m equivalent in a largely institutional initial public offering, valuing the company at slightly above $1bn. Parent company Aker retains a stake of approximately 43%, post IPO.

There will be more demand for drilling in harsher areas, with the results of the Norwegian Petroleum Directorate's 21st licensing round to be announced shortly. The licensing area includes 51 blocks in the Barents Sea, exceeding the 43 in the Norwegian Sea. ■

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