

USA – Offshore Drillers

January 13, 2014

CAUTIOUS VIEW

HIGH RISK

TRADE BRIEF

Ultra Deepwater rigs UC*:

Company	# of Rigs	% of Total
Atwood	4	5.3%
Diamond Off	4	5.3%
ENSCO PLC	3	4.0%
Noble Corp	2	2.7%
Ocean Rig	4	5.3%
PacificDrilling	3	4.0%
Rowan Cos	4	5.3%
Seadrill Ltd.	11	14.7%
Transocean	7	9.3%
Vantage Drill	2	2.7%
Total	44	58.7%
Others	31	41.3%
Grand Total	75	100%

*UC = Under Construction. 12,000-ft.
Source: Company Data, HIS
Petrodata & ZGI Research

The Outlook

❖ Supply in the UDW segment is accelerating, which should start to exert downward pressure on day rates from 2016. In view of the high number of planned UDW (75 rigs) and a growing trend to continue to add will likely put pressure to day rates as UDW rigs come to market. We believe the balance between demand and supply factors has changed fundamentally which should lead to lower day rates.

The UDW Market...! Turbulence ahead – 2016!

- We believe that the supply for ultra deepwater (UDW 12,000-ft.) rigs will continue to be supported by strong demand from Brazil. However, with the majority of rigs slated for Brazil, **we are forecasting a soft market from 2016 with limited visibility as rigs come off contract.** This will be negatively impacted by the additional of 75 new UDW rigs (total 158) at a cost of \$49.2 billion in the global offshore market.
- **Survey:** We are providing a survey of 83 UDW rigs that are currently working with a contractual backlog of approximately \$46.1 billion.
- Based on our surveyed, we find that approximately \$24.5 billion of the total backlogs are due from 2014-2015, or approximately 53.0%. Our universe of offshore drillers (*Diamond Off. {DO}*, *Noble Corp. {NE}*, *Ocean Rig UDW {ORIG}*, *Pacific Drilling SA {PACD}*, *Seadrill Ltd {SDRL}*, *Transocean Ltd {RIG}* and *Vantage Drilling {VTG}*) have approximately \$16.8 billion or approximately 56.2% of the universe backlog of \$29.8 billion that is due from 2014-2015. **See Exhibit 1.**
- **Petrobras Brazil:** Given the significant percentage (28.9%) of UDW rigs that are contracted in Brazil by Petrobras with a backlog of approximately \$14.1 billion, we see significant risk in relying on Petrobras. The most recent trend in relying on Brazil represents a significant long-term risk for global deepwater managers, as it will likely result in a decline of rigs in this market in the event drilling is not successful. This of course, would also result in a decline in day rates. Further, meaningful cost-restructuring measures by Petrobras could prove to have negative affects for deepwater supply and day rates.
- **Day Rates:** According to our analysis, the *Ocean Rig Miklos* has the highest day rate at \$679k and the *Noble Duchess* has the lowest day rate at \$151k. The *Noble Duchess* has been working as a bareboat chartered since May 2012, thus the low day rate. Our analysis suggests that, companies with day rates of \$550k+ are at risk of seeing lower renewal rates than previously obtained. **See Exhibit 3.**
- By 2016, there will be approximately 158 ultra deepwater rigs in the market. We believe the balance between demand and supply factors will change fundamentally, leading to lower day rates. **We are very cautious on the group as a whole.**

Please refer to the disclaimer of this research at the end of document.

OSX: 277.48

S&P 500: 1,842.37

NASDAQ: 4,174.66

DOW: 16,437.05

Ultra Deepwater rigs UC*:

Company	# of Rigs	Est. Cost
Atwood	4	\$2.5
Diamond Off	4	2.6
ENSCO PLC	3	1.9
Noble Corp	2	1.2
Ocean Rig	4	2.6
PacificDrilling	3	1.9
Rowan Cos	4	3.0
Seadrill Ltd.	11	6.6
Transocean	7	5.2
Vantage Drill	2	1.2
Total	44	\$28.8
Others	31	20.5
Grand Total	75	\$49.2

*UC = Under Construction. 12,000-ft.
\$in Million
Source: Company Data, IHS
Petrodata & ZGI Research

Senior Equity Analyst



No Longer Sensitive to the Demand Factor...!

As supply potential grows, supply factors begin to dominate, leading to lower demand and lower day rates.

Over the course of the past couple of years, the trend in UDW rigs demand (limited supply) and higher day rates has been on an upward trend than on a downward trend, mostly driven by Brazil and the discovery of deeper offshore oilfields. With 75 UDW rigs that are currently under construction at a cost of \$49.2 billion, there could be an oversupply which will lead to a structural change in the UDW market in full in 2016-2017. In 3-4 years, there will be approximately 158 UDW rigs which will add pressure when valuing the market day rates. Our research suggests that **this will become an Operator/Client market; not an Offshore Drillers market.**

The future trend is clear with over half of the total backlog of approximately \$24.4 billion is due from now through 2015.

This is approximately 52.9% of the total backlog.

Exhibit 1. The Drillers Universe Working UDW Backlog 2014 – Thereafter

Company	No. of Rigs	% of Rigs	2014	2015	2016	2017	Thereafter	Total
Diamond Offshore	1	1.2%	\$119	\$123	-	-	-	\$241
ENSCO PLC	7	8.4%	1,210	1,171	714	195	32	3,323
Noble Corp.	9	10.8%	1,285	1,232	1,121	670	1,889	6,196
Ocean Rig UDW	5	6.0%	948	732	290	-	-	1,971
Pacific Drilling S.A.	5	6.0%	980	766	384	66	-	2,195
Seadrill Ltd	6	7.2%	928	884	884	845	1,246	4,788
Transocean Ltd.	19	22.9%	2,967	2,159	1,292	937	1,462	8,817
Vantage Drilling	3	3.6%	637	590	209	209	613	2,256
Universe	55	66.3%	\$9,074	\$7,656	\$4,894	\$2,923	\$5,241	\$29,788
Others	28	33.7%	4,100	3,556	3,199	2,532	2,883	16,271
Total	83	100.0%	\$13,174	\$11,212	\$8,093	\$5,456	\$8,124	\$46,060

Source: \$ in Million. Company data, HIS Petrodata & Zephyrin Group, Inc. (ZGI) research estimates

Exhibit 2. Operators UDW Expenses Commitment 2014–Thereafter

Company	No. of Rigs	% of Rigs	2014	2015	2016	2017	Thereafter	Total
BP	6	7.2%	\$1,105	\$957	782	573	645	\$4,062
Chevron	7	8.4%	1,227	1,178	814	674	1,191	5,085
ENI	3	3.6%	605	441	244	-	-	1,289
ExxonMobil	2	2.4%	432	406	204	-	-	1,042
Petrobras	24	28.9%	3,428	3,036	2,308	1,916	3,378	14,068
Shell	5	6.0%	866	896	896	776	1,939	5,373
Statoil	1	1.2%	212	219	73	-	-	504
Universe	48	57.8%	\$7,875	\$7,133	\$5,321	\$3,940	\$7,154	\$31,423
Others	35	42.2%	5,299	4,079	2,773	1,516	971	14,637
Grand Total	83	100.0%	\$13,174	\$11,212	\$8,093	\$5,456	\$8,124	\$46,060

Source: \$ in Million. Company data, HIS Petrodata & Zephyrin Group, Inc. (ZGI) research estimates

Exhibit 3. The Drillers Universe UDW Highest/Lowest/Average Dayrate

Company	No. of Rigs	Highest Dayrate	Highest Rig Name	Lowest Dayrate	Lowest Rig Name	Average Dayrate
Diamond Offshore	1	\$336.1	Ocean Clipper	\$336.1	Ocean Clipper	\$336.1
ENSCO PLC	7	607.0	ENSCO DS-7	358.0	ENSCO DS-1	489.9
Noble Corp.	9	618.0	Noble Bob Douglas	151.0	Noble Duchess	404.4
Ocean Rig UDW	5	679.0	Ocean Rig Mylos	417.0	Ocean Rig Corcovado	537.2
Pacific Drilling S.A.	5	660.0	Pacific Khamsin	499.0	Pacific Scirocco	555.2
Seadrill Ltd	6	653.1	West Polaris	565.0	West Capella	599.7
Transocean Ltd.	19	674.0	Deepwater Pathfinder	412.0	GSF Explorer	552.5
Vantage Drilling	3	641.0	Tungsten Explorer	572.0	Titanium Explorer	601.2
Universe	55	\$608.5		\$413.8		\$509.5
Others	28	643.8		282.4		500.3
Total	83	\$679.0		\$151.0		\$491.1

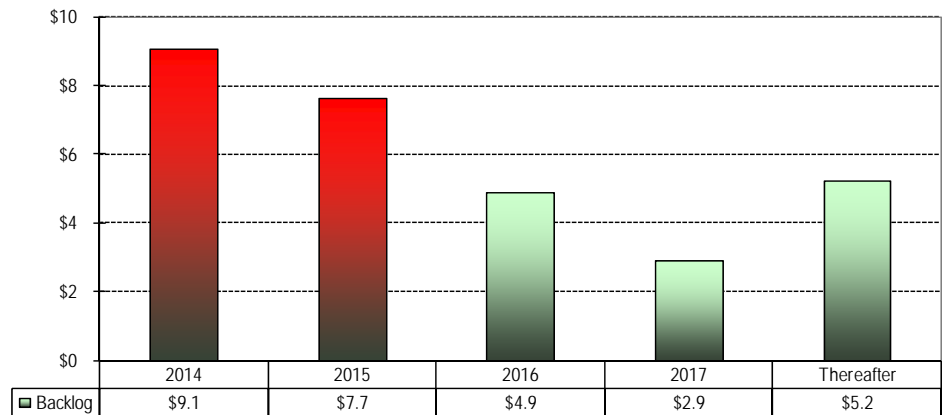
Source: Company data, HIS Petrodata and The Zephyrin Group, Inc. (ZGI) research estimates

Members of our universe hold both the highest and lowest day rates in the UDW segment.



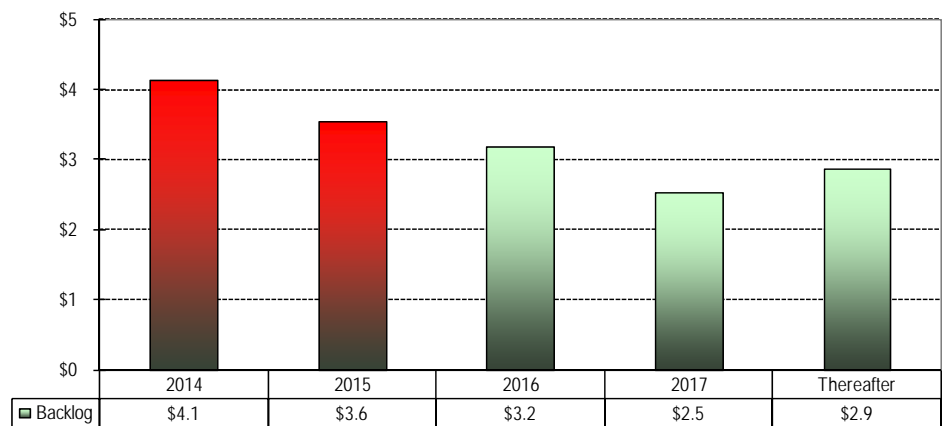
Exhibit 4. Offshore Universe Working UDW Backlog 2014 – Thereafter

After excessively high backlog growth in 2014-2015, backlog will slow sharply in 2016, continuing thereafter.



Source: Company data, HIS Petrodata and The Zephyrin Group, Inc. (ZGI) research estimates

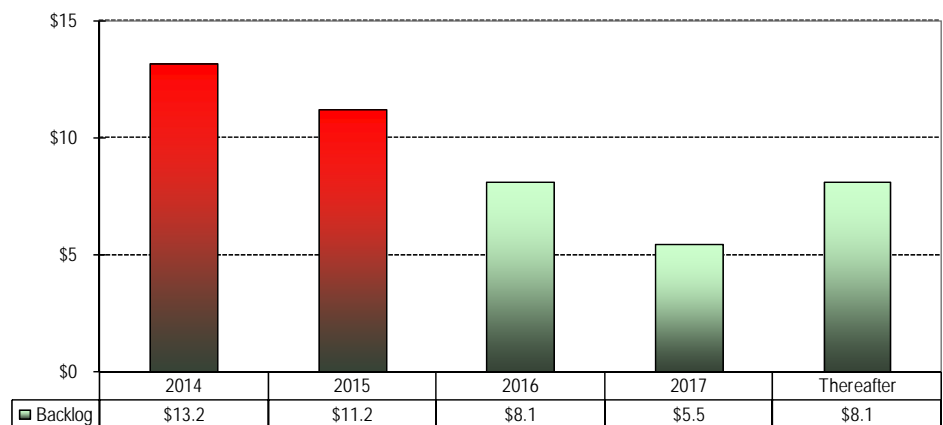
Exhibit 5. Other Working UDW Companies Backlog 2014 – Thereafter



Source: Company data, HIS Petrodata and Zephyrin Group, Inc. (ZGI) research estimates

Exhibit 6. Total Working UDW Backlog 2014 – Thereafter

More than half of the backlog is due by 2015.



Source: Company data, HIS Petrodata and Zephyrin Group, Inc. (ZGI) research estimates



Companies mentioned *As of January 10, 2014

Name	Ticker	Price*	Objective	Rating
Diamond Offshore	DO	\$55.91	●	SELL High Risk
ENSCO PLC	ESV	56.94	●	SELL Medium Risk
Noble Corp.	NE	36.51	●	SELL High Risk
Ocean Rig UDW	ORIG	19.02	●	SELL High Risk
Pacific Drilling S.A.	PACD	11.02	●	HOLD High Risk
Seadrill Ltd.	SDRL	40.74	●	SELL High Risk
Transocean Ltd.	RIG	48.53	●	SELL High Risk
Vantage Drilling	VTG	1.92	●	HOLD Speculative Risk

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Risk Rating: LOW RISK (LR) — Return of 0-10%; MEDIUM RISK (MR) — Return of 0-20%; HIGH RISK (HR) — Return of 0-30% and SPECULATIVE RISK (SR) — Return of 0-50%. **Distribution of Rating:** Buy = 0 (0.0%); Hold = 3 (30.0%); Underperform/Sell = 7 (70.0%)

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