Aban Offshore Ltd

(ABAN.BO / ABAN IN)

Rating	(from Neutral) **OUTPERFORM* [V]**
Price (07 Nov 08, Rs)	968.20
Target price (Rs)	(from 3,600.00) 1,261.00¹
Chg to TP (%)	30.2
Market cap. (Rs mn)	36,596.28 (US$ 770.61)
Enterprise value (Rs mn)	189,668
Number of shares (mn)	37.80
Free float (%)	37.60
52-week price range	5379.40 - 652.85

**Stock ratings are relative to the relevant country index.*
¹Target price is for 12 months.
[V] = Stock considered volatile (see Disclosure Appendix).

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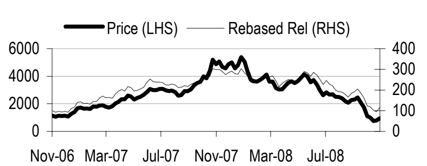
DECREASE TARGET PRICE

Leverage – from good to bad

- **Event:** The Aban offshore stock has fallen 80% since January and now trades at a discount to its peers compared to the premium then. We reduce our day rate estimates and cut FY09E and FY10E EPS by 43% and 13%, respectively. We reduce our target price to Rs1,261 from Rs3,600 and upgrade our rating to OUTPERFORM (from Neutral).
- **View:** A lack of funding and sharp falls in day rates are our main concerns, but at 2.7x FY10E earnings, the risks are more than in the price. While we estimate Aban's refinance requirements are front-ended, we do not anticipate lenders withdrawing funds – the lack of ability to repay and limited other funding options are the principal deterrents to lender apathy. Dilution is a concern, but only a large sale would make any dent on debt and is difficult in current market conditions. While interest spreads may rise, Aban's operations are unlikely to unwind for lack of funding. Slower demand (sustained low oil prices) and rising supply imply reduced jackup day rates. Even factoring in some softening, Aban's earnings should grow. We cut our 375'+ jackup day rate estimates from $200,000 to $153,000 per day from CY10 onwards. Aban should remain profitable for above $110,000 per day rates.
- **Catalyst:** Concerns around the large debt with Aban causes the current valuation discount. Deployment of new rigs will increase cash flow from operations; the announcement of newer contracts will assure a reduction of debt levels. Any consequent reduction in the valuation discount will be positive for the stock. A dramatic fall in day rates remains the principal risk for Aban.
- **Valuation:** Aban currently trades at 2.7x FY10E EPS, compared to 5.4x times for comparable stocks. Our new target price of Rs1,261 is 3.5x FY10E EPS and implies potential upside of 30%.

Share price performance



The price relative chart measures performance against the BOMBAY SE 30 SHARE SENSITIVE index which closed at 9734.22 on 06/11/08
On 06/11/08 the spot exchange rate was Rs47.64/US$1

Performance Over	1M	3M	12M
Absolute (%)	-26.2	-61.9	-80.9
Relative (%)	-13.3	-42.1	-63.1

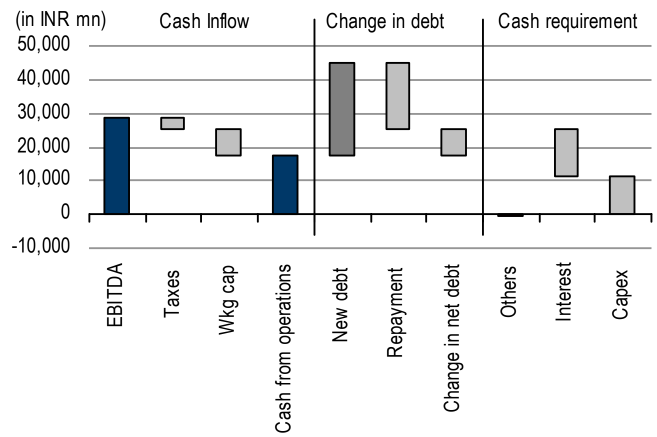
Financial and valuation metrics

Year	3/08A	3/09E	3/10E	3/11E
Revenue (Rs mn)	20,210.6	43,120.4	53,952.8	51,474.5
EBITDAX (Rs mn)	10,535.8	28,589.9	36,581.8	33,327.3
EBIT (Rs mn)	7,458.3	23,790.3	30,556.2	26,470.4
Net income (Rs mn)	1,229.9	7,132.1	13,615.4	10,081.0
EPS (CS adj., Rs)	32.54	188.69	360.21	266.71
Change from previous EPS (%)	n.a.	-42.9	-12.8	
Consensus EPS	n.a.	427.00	520.00	0
EPS growth (%)	n.a.	479.9	90.9	-26.0
P/E (x)	29.8	5.1	2.7	3.6
Dividend yield (%)	0.37	—	—	—
EV/EBIDAX (x)	16.7	1.9	1.3	1.6
P/B (x)	4.5	2.5	1.3	1.0
ROE (%)	4.6	49.0	48.8	26.6
Net debt/equity (%)	1,526.2	1,051.0	445.4	296.4

Source: Company data, Thomson Financial Datastream, Credit Suisse estimates.

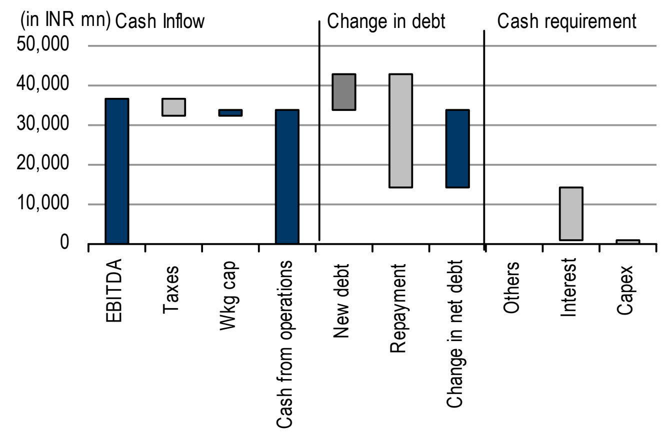
Focus charts

Figure 1: Large debt rollover requirement in FY09



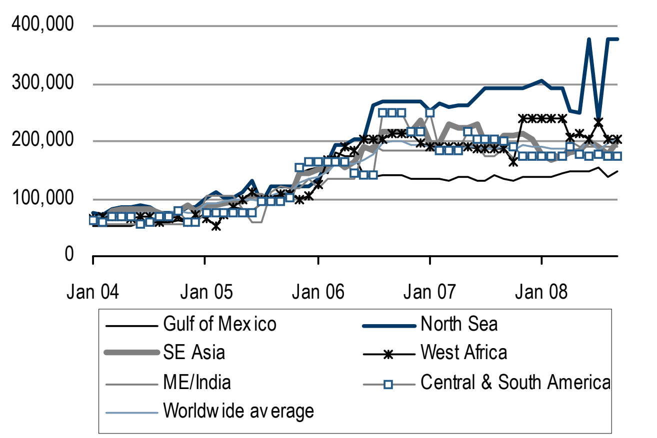
Source: Credit Suisse estimates

Figure 2: The pressure should reduce in FY10



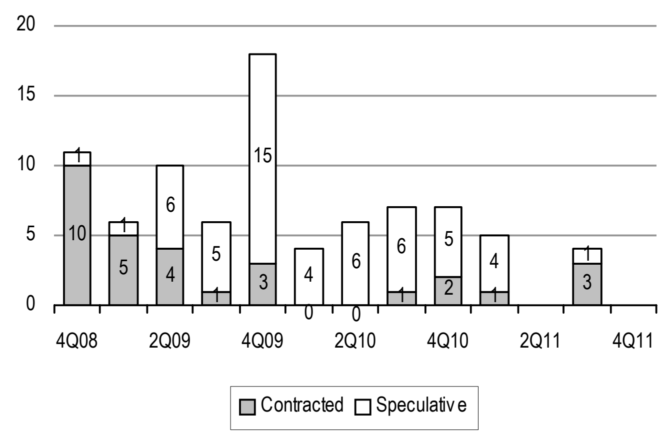
Source: Credit Suisse estimates

Figure 3: Jackup day rates have not fallen as yet



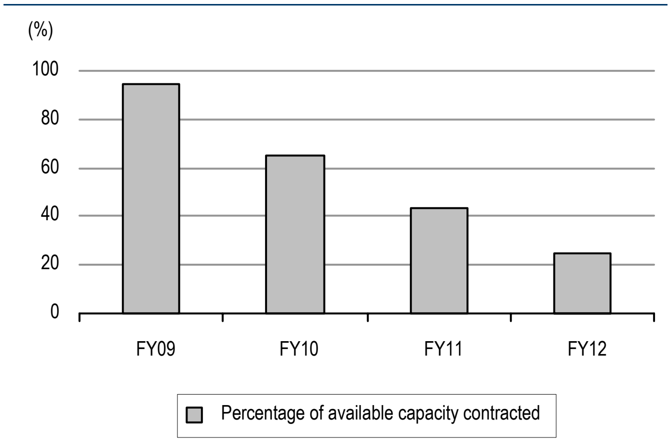
Source: ODS Petrodata, Credit Suisse estimates

Figure 4: Increasing supply of jackups will put pressure on rates



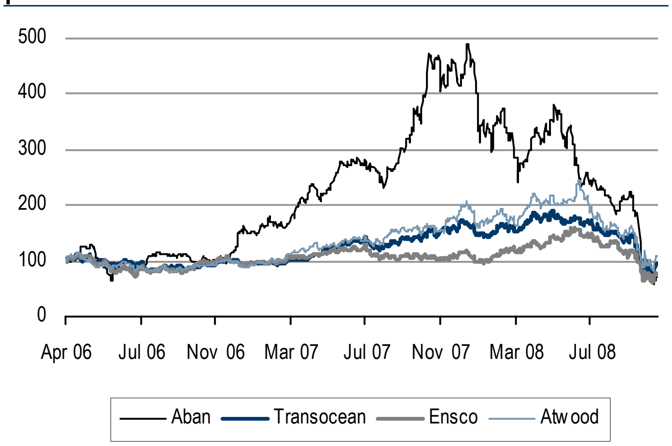
Source: ODS Petrodata, Credit Suisse estimates

Figure 5: Aban has a large portion of near-term capacity contracted



Source: Company data, Credit Suisse estimates

Figure 6: With the rapid fall, Aban's relative out-performance has eroded



Source: Bloomberg, Credit Suisse estimates

Leverage – from good to bad

The acquisition of Sinvest greatly increased Aban's scale of operations but left it with a mountain of debt. The large associated interest costs increased sensitivity of earnings to jackup day rate movements. In an up-cycle this was good; the high leverage was ignored. Now that the commodity cycle has turned, this debt has become a principal concern for the market. Aban's roll-over requirements are front-ended; while higher risk aversion implies higher debt spreads for the company, we do not anticipate a withdrawal of funding by Aban's lenders. We reduce day rate expectations and cut earnings by 43% and 13% for FY09 and FY10, respectively. From a premium to comparables earlier, Aban trades at a discount now. Deployment of new rigs and newer contracts that tie up revenue can improve valuations. We reduce our target price to Rs1,261 (3.5x FY10E EPS) from Rs3,600 and upgrade to an OUTPERFORM rating (from Neutral). Any large fall in day rates remains the principal risk to earnings and valuations.

Debt likely to be rolled over

Aban's FY08 consolidated debt to equity stood at 15 times. Post the global financial crisis and the turning of the commodity cycle, this debt has come under the spotlight; funding available with the company has become a concern. We estimate repayment of Aban's current debt is higher near term. With low operating cash flow and higher capex, FY09 debt rollover requirements are high – close to $580 mn, falling to about $240 mn in FY10.

Outside of the bonds in Norway, Indian banks comprise a majority of Aban's lenders. These may have a larger appetite for Indian corporate risk. Banks may also have incentive to continue the funding. With few other funding options available, a withdrawal of facilities would imply a fire sale of assets; which does not guarantee a recovery of principal. At current valuations, significant dilution would be needed to repay any meaningful amount of debt, which may be difficult in current market conditions. Other than a large fall in day rates, Aban should be able to forecast adequate debt cover; giving lenders little excuse for pulling the trigger. Adequate funding (albeit at higher spreads) should be available to Aban until their operations ramp up.

Other than a large fall in day rates, Aban should be able to forecast adequate debt cover; giving lenders little excuse for pulling the trigger

Jackup day rates – the bigger question

The fall in oil prices imply a reduction in demand for exploration services. This comes at a time when supply of jackups is increasing. Utilisation rates for jackups and day rates are likely to come under pressure. Consequently, we reduce day rate expectations for 375'+ jackups from the current $200,000 per day to $153,000 per day from CY10 onwards. We estimate Aban remains profitable for day rates above $110,000 per day.

Aban has most of available capacity for FY09 and FY10 contracted; tying up $3 bn in revenue. While this is not enough to service all debt (interest and principal), sensitivity to day rate movements is lower near term. Cash flows over the next two years will lower debt levels, increasing company ability to endure lower day rates.

Valuations look inexpensive

We cut FY09 and FY10 EPS by 43% and 13% to Rs189 and Rs360 respectively, and reduce our target price to Rs1,261 (30% potential upside, 3.5x FY10E EPS) from Rs3,600. Aban outperformed other offshore drillers on the way up – the recent correction has eroded that performance. High debt levels and associated high earnings sensitivities imply stock volatility. Reduction of debt and the announcement of new contracts should cause the volatility to reduce over time. At these levels though, the risks are skewed to the upside. We upgrade our rating to OUTPERFORM (from Neutral).

Aban outperformed other offshore drillers on the way up – the recent correction has eroded that performance

Financial summary

Figure 7: **Financial summary**

Year-end 31 Mar (Rs mn)	2006	2007	2008	2009E	2010E	2011E	2012E
USD/Rs rate	44.30	44.74	40.26	48.00	45.00	46.35	47.74
Profit and loss statement							
Revenue	4,902	7,187	20,211	43,120	53,953	51,474	52,384
Other income	148	881	1,070	788	627	569	564
Total income	5,049	8,068	21,280	43,908	54,580	52,044	52,949
Operating expenses	2,098	3,713	9,675	14,531	17,371	18,147	19,264
EBITDA	2,804	3,474	10,536	28,590	36,582	33,327	33,120
Depreciation	951	1,203	3,077	4,800	6,026	6,857	7,434
Goodwill amortised	63	63	63	-	-	-	-
EBIT	1,853	2,271	7,458	23,790	30,556	26,470	25,686
Interest	436	2,686	6,658	14,012	13,373	12,537	11,819
PBT	1,501	403	1,807	10,566	17,810	14,503	14,431
Tax	678	747	1,430	3,434	4,195	4,422	4,607
Minority interest	-	-	(0)	-	-	-	-
PAT	823	(140)	1,230	7,132	13,615	10,081	9,824
Balance sheet							
Net fixed assets	7,158	75,203	83,529	134,772	130,959	139,920	137,602
Investments	192	4,683	6,391	5,738	5,991	5,877	5,760
Current assets	1,505	19,190	14,090	18,071	16,334	15,860	16,076
Current liabilities	832	6,624	6,568	6,952	8,607	8,233	8,347
Total debt	11,098	108,525	130,434	157,158	126,428	114,598	102,422
Shareholders' funds	4,304	5,308	8,123	14,565	27,888	37,895	47,780
Minority interests	-	-	-	-	-	-	-
Gross invested capital	15,402	113,834	138,557	171,723	154,315	152,493	150,202
Capex	-	-	(22,619)	(11,495)	(1,000)	(1,000)	(1,000)
Cash flow statement							
Cash from operations				20,846	38,059	33,545	33,095
Tax				(3,434)	(4,195)	(4,422)	(4,607)
Cash from operating activities				17,412	33,864	29,123	28,488
Change in assets				(11,583)	(1,000)	(1,000)	(1,000)
Cash from investing				(11,583)	(1,000)	(1,000)	(1,000)
Change in debt				4,448	(21,170)	(15,746)	(15,929)
Interest				(14,012)	(13,373)	(12,537)	(11,819)
Cash from financing				(9,322)	(34,502)	(28,077)	(27,393)
Ratios							
Net debt	10,963	95,261	123,981	153,072	124,198	112,319	100,093
EPS	22	(4)	33	189	360	267	260
BVPS	114	140	215	385	738	1,003	1,264
P/E	44	(261.4)	29.76	5.13	2.69	3.63	3.73
EV/EBITDA	5.45			6.63	4.40	4.47	4.13
Interest cover	4.25	0.85	1.12	1.70	2.28	2.11	2.17
Net debt/equity	2.55	17.95	15.26	10.51	4.45	2.96	2.09
Dividend yield (%)	0	0	0	0	0	0	0
DPS	3	3	4	-	-	-	-
ROGIC (%)	14	3	7	15	21	19	18
ROE (%)	19	-3	15	49	49	27	21

Source: Company data, Credit Suisse estimates

Debt likely to be rolled over

The acquisition of Sinvest in 2006 was a significant event in Aban's history, increasing scale of operations but leaving the company with a mountain of debt. Large associated interest costs increase earnings sensitivity to changes in revenue (jackup day rates). In an up cycle, this large debt was ignored; higher rate expectations led to larger earnings estimates and rapid pay down of debt. Now that demand for all commodities (and associated services) is in question, the cycle is turning in reverse. Aban's debt has come under the spotlight. The company's liquidity position and ability to refinance debt has become a matter of concern.

We estimate Aban's need to refinance debt is front-ended driven by lower operating cash flow and higher capex near term. Aban may need to refinance close to US$580 mn in FY09 declining to US$240 mn in FY10. The increased global risk aversion implies Aban's debt spreads will increase. Without a significant collapse in day rates (and revenues) lenders though, may have little reason to withdraw funding.

Estimating a repayment schedule

The exact break-up of Aban's current debt and repayment schedule is unavailable, but based on disclosure in the annual report, at Sinvest and management comments; we estimate Aban's debt profile as in Figure 8.

Figure 8: **Aban has large debt repayment scheduled in FY09E and FY10E**

Debt repayment schedule			FY09E	FY10E	FY11E	FY12E	FY13E	FY14E	FY15E	FY16E
(Rs mn)										
Currency assumptions										
USD/NOK			6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00
USD/Rs			48.00	45.00	46.35	47.74	49.17	50.65	52.17	53.73
NOK/Rs			8.00	7.50	7.73	7.96	8.20	8.44	8.69	8.96
Aban India	**Outstanding amount**	**Currency**								
Loans	12,380	Rs	6,123	3,128	3,128					
FCCB (Yen)	2,184	Rs					2,184			
Aban Singapore										
Loans	1,931	USD	241	241	241	241	241	241	241	241
FCCB	149	USD						149		
Sinvest										
Bonds	250	NOK		250						
Bonds	750	NOK		750						
Bonds	400	NOK				400				
Bonds	140	USD	35	35	35	35				
Bonds	160	USD		53	53	53				
Bonds	280	USD		70	70	70	70			
Total repayment		**Rs**	**19,391**	**28,617**	**21,657**	**22,267**	**15,313**	**12,227**	**12,594**	**12,972**

Source: Company data, Credit Suisse estimates

Aban's liabilities are denominated in four currencies – Rs, USD, NOK and yen (for the FCCB). Dollar denominated debt constitutes the largest portion, and came with the acquisition of Sinvest. Most of the company's earnings are dollar denominated as well, matching the liability; reducing concern on currency fluctuation. Movements in the USD/NOK rate, have recently impacted Aban's reported earnings – we understand Aban is hedging this exposure to reduce the impact of future USD/NOK movement.

While the large USD debt amortises over eight years, the majority of loans are due over the next two to three years

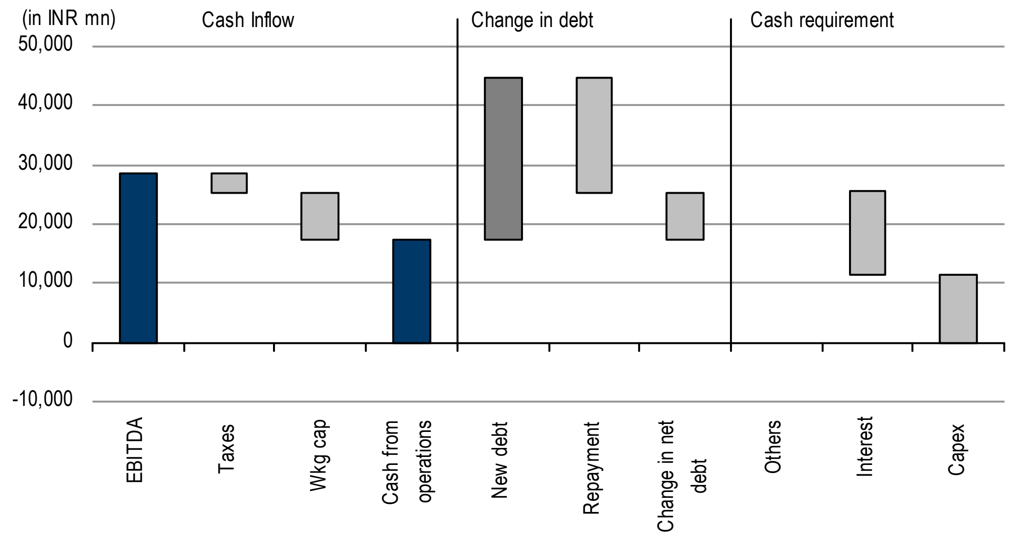
While the large USD debt at Aban Singapore amortises over eight years, a majority of loans are due over the next two-to-three years. This causes the repayment schedule to be front-ended; peaking in FY10. Note that these are not the total repayments likely to happen – debt that is refinanced now will also come due in later years.

Rollover requirements highest upfront

Aban's capex (payments for rigs under construction) continues in FY09. Cash flow from earnings is lower near term as several rigs are yet to commence operations. Interest costs are also high. Aban's scale of operations will continue to increase through FY09 as new rigs are delivered and deployed. This will increase working capital requirements near term. These, together with large repayment requirements imply that the company has to arrange for a large amount of new debt. We estimate FY09 new debt requirement at Rs28 bn ($587 mn). Of this, we understand the company has successfully refinanced some rupee loans on Aban's India balance sheet (about Rs6 bn due in FY09).

New debt requirement for FY09 is estimated at Rs28 bn (US$587 mn), of which, we understand the company has successfully refinanced rupee loans

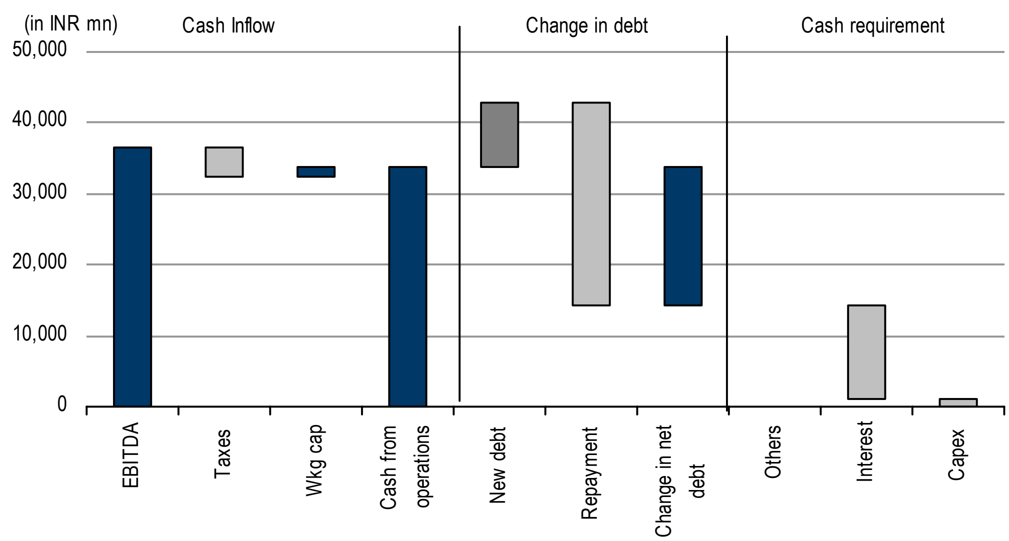
Figure 9: Large debt rollover requirement in FY09



Source: Credit Suisse estimates

The need to refinance debt should be reduced in FY10. Higher cash from operations and lower capex should allow business proceeds to meet some of the repayment requirements. We estimate about Rs10 bn ($240 mn) of new debt will have to be arranged for FY10.

Figure 10: Lower capex and higher EBITDA should reduce refinance requirement in FY10



Source: Credit Suisse estimates

More expensive, but debt should be available

The sharp increase in global risk aversion makes refinancing more difficult; especially for Aban with its high debt levels and relatively low interest cover. We believe while Aban may have to pay higher spreads for newer debt, money should be available to sustain the company until operating cash flows ramp up.

1) Outside of the bonds in Norway, Aban's lenders principally comprise Indian public and private sector banks. These have not suffered liquidity crunches as severe as some global banks and may have larger appetite for Indian corporate risk.

2) Even after building in moderate declines in day rates, we believe Aban can demonstrate adequate future debt cover to lenders. Unless day rates fall dramatically, there should be few triggers for lenders to ask for repayment instead of refinancing.

3) Large equity dilution is needed for any meaningful reduction in debt levels; which may be difficult in current market conditions. Given the lack of other funding opportunities, we believe lenders have little option but to rollover the debt. Repossessing and disposing assets is a difficult process and any fire-sale does not assure principal recovery. Banks are unlikely to resort to this route soon.

We model Aban's new debt at a spread of 5% over that of the older book. While the aggregate spread will be higher, the decline in LIBOR may help keep total interest costs in check.

Figure 11: **Falling LIBOR can lower the impact of increasing debt spreads**

Source: Bloomberg, Credit Suisse estimates

Figure 12: **Large dilution needed to repay any meaningful amount of debt**

Dilution	Reduction in FY08 debt (%)
10%	3
20%	7
30%	12
40%	18
50%	28
60%	41
70%	64
80%	110

Source: Credit Suisse estimates

Jackup day rates – the bigger question

While the market seems more worried about Aban's ability to rollover debt, jackup day rates are the larger determinant of company profitability. With the acquisition of Sinvest, most of Aban's exposure is to jackups that can drill in water depths of 300 feet or more. Global average day rates of jackups of this type increased three fold between 2004 and 2006 and have remained flat since. Lower oil prices imply reduced exploration capex and lower rig demand; increasing supply of jackups in addition will contribute to softening day rates. Consequently, we reduce day rate expectations for 375'+ jackups from the current $200,000 per day to $153,000 per day from CY10 onwards. We estimate Aban remains profitable for day rates above $110,000 per day.

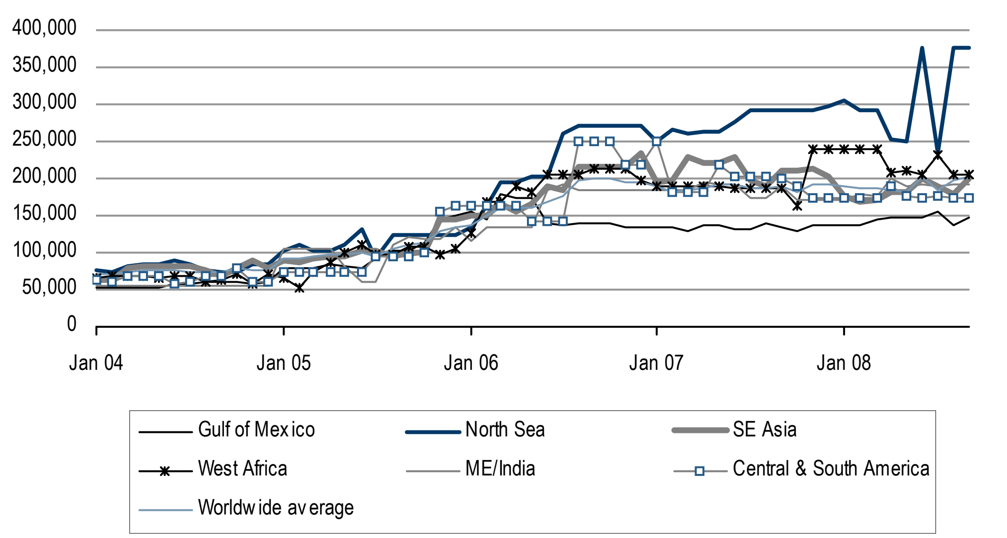
Aban is most exposed to 300 ft jackups – global day rates for which increased three fold from 2004 to 2006 and have remained flat since

Aban has most of available capacity for FY09 and FY10 contracted; tying up $3 bn in revenue. While this is not enough to service all debt (interest and principal), sensitivity to day rate movements is lower near term. Cash flows over the next two years will lower debt levels, increasing company ability to endure lower day rates.

Day rates have been flat, but there are signs of easing

Global average day rates for 300' plus jackups have been flat for the past two years after witnessing a steep rise since 2004. Increasing commodity prices and a tight rig market contributed to the strengthening. Demand for jackups in the Middle East and North-West Europe was particularly strong. Lower oil prices are likely to cause deferment of exploration expenditure (especially the marginal ones) and cause jackup demand to ease.

Figure 13: **Average day rates for 300'+ jackups have remained flat since mid 2006; only the North Sea region has seen some upside**



Source: ODS Petrodata, Credit Suisse estimates

Average utilisation rates for jackups also increased from the low 80% in 2002 to the mid-90% now. Jackups representing about 15% of the current capacity are expected to roll out over the next several quarters; increasing supply and hurting overall utilization rates. In an easing environment older, lower specification jackups will see reduced utilisations; some are likely to be retired. Even if demand remains at current levels, global jackup utilisation rates will then fall back to the low 80%. New build high specification rigs though can see above average utilisation rates on lower day rates.

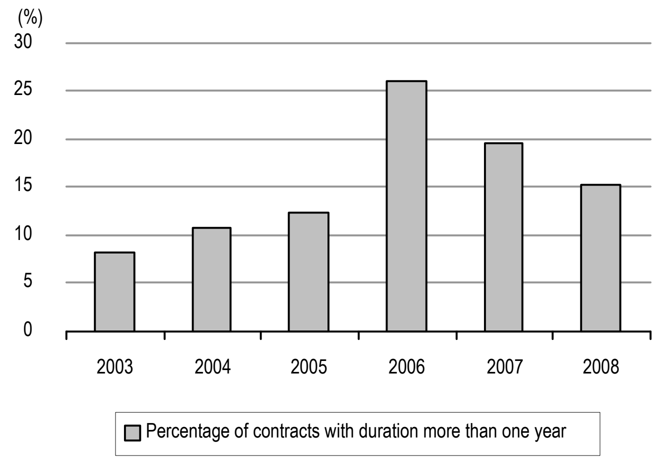
Even at current levels of demand, global jackup utilisation rates will fall back to the low 80% seen in 2002

While rates haven't eased yet, there are signs the market is turning looser

While jackup day rates have remained flat, analysis of contracts signed indicate the rigs market is turning looser. The proportion of contracts with duration more than a year peaked in 2006 and has been declining since – now at 15% from a high of 25%. This indicates increasing unwillingness on the part of exploration companies to commit to current high rig rates.

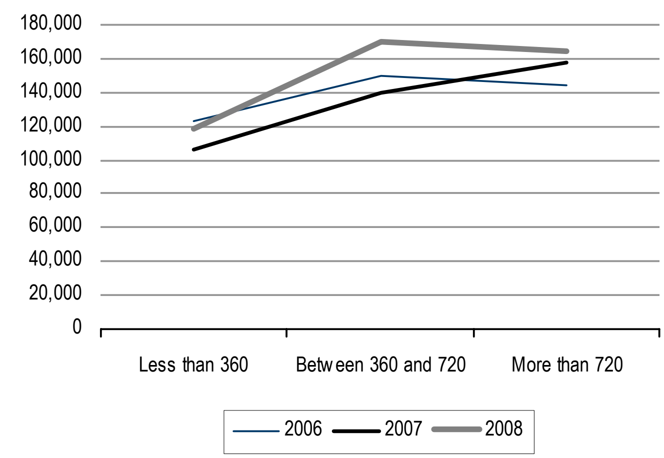
Proportion of contracts with duration >1 year has been declining since its peak in 2006– now at 15% from a high of 25%

Figure 14: **Rig users less willing to contract for longer term**



Source: ODS Petrodata, Credit Suisse estimates

Figure 15: **Rates for longer-term contracts are now lower**



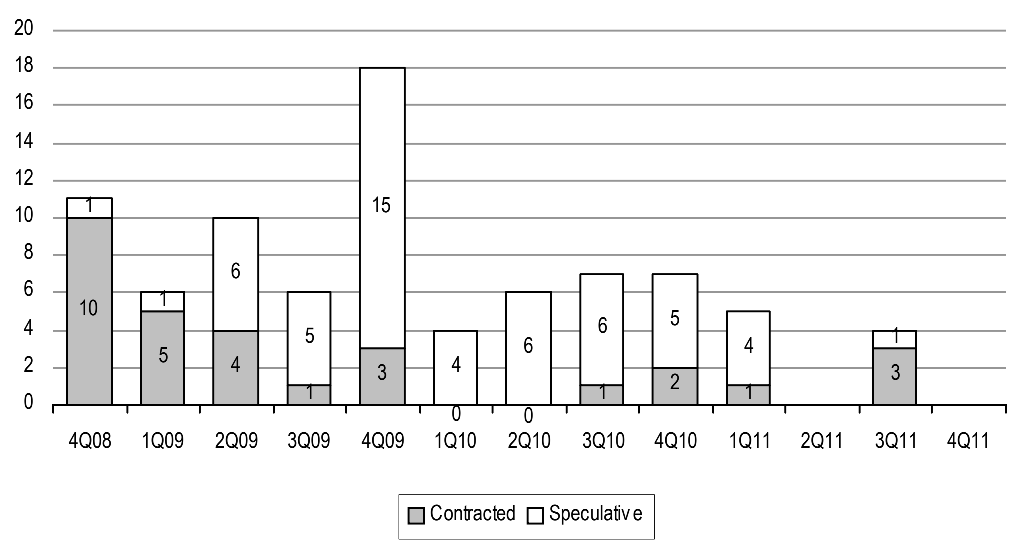
Source: ODS Petrodata, Credit Suisse estimates

In 2007, the average day rate for longer-term contracts was higher than that for the shorter variety. This has now turned – the average for contracts with duration of more than 720 days is less than that for those of duration between 360 and 720 days. The market was tight in 2007 – with buyers willing to pay a premium for volume. The 2008 reversal indicates rig companies are now willing to extend a discount for revenue assurance.

Supply of jackups to peak around 2H CY09

There is strong supply of new build jackups over the next few quarters, peaking around 2H CY09. Most of these jackups are un-contracted and will compete for available demand.

Figure 16: **Significant increase in jackup deliveries expected 2H CY09**



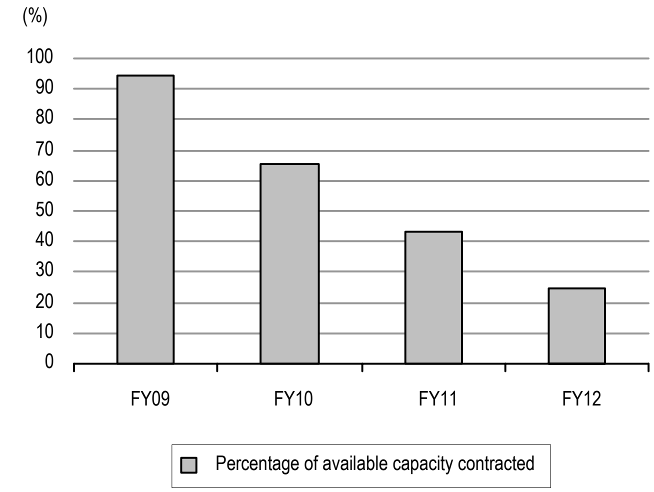
Source: ODS Petrodata, Credit Suisse estimates

Aban – existing contracts lower sensitivity to day rates near term

Most of Aban's rigs are currently contracted (three un-contracted at the time of this report) on long and short-term fixtures. As a result of these contracts, more than 90% of capacity in FY09 and nearly 65% capacity for FY10 has been locked in (capacity in terms of available rig days). These contracts represent about $3 bn in revenue for Aban.

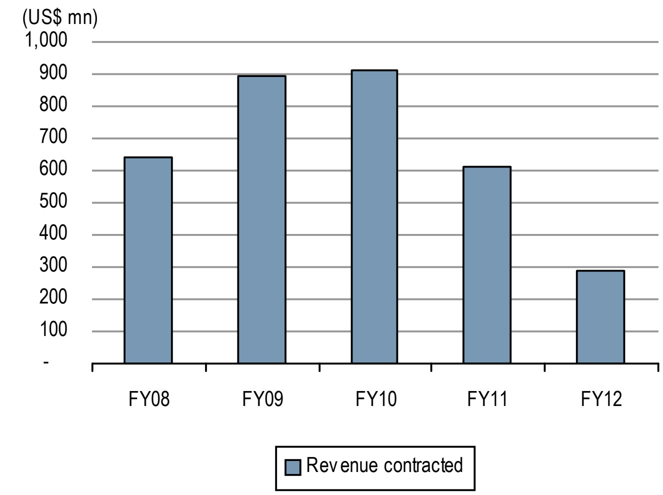
More than 90% of Aban's capacity in FY09 and nearly 65% capacity for FY10 are locked in

Figure 17: Aban has booked a large portion of near-term capacity, but susceptible to longer term day rate movements



Source: Company data, Credit Suisse estimates

Figure 18: Current contracts amount to about $3 bn in revenue



Source: Company data, Credit Suisse estimates

While day rate movements may have a low impact on near-term earnings due to the contracts signed, the company remains vulnerable in the medium to longer term. High interest payments imply earnings can disappear if jackup day rates (for the high spec variety) fall to US$110,000 per day in FY11.

Earnings can disappear on high interest costs if jackup day rates fall to US$110,000 per day in FY11

Figure 19: Near term sensitivity to day rate movements low

		CY2009	CY2010	CY2011
Base case				
375' jackup	USD/day	180,000	153,000	153,000
350' jackup	USD/day	170,000	143,000	143,000
EPS - base case	Rs/share	188	356	258
375' jackup rate sensitivity to EPS*		**FY2009 (%)**	**FY2010 (%)**	**FY2011 (%)**
110,000		-18	-47	-92
120,000		-15	-40	-79
130,000		-13	-34	-65
140,000		-10	-27	-52
150,000		-8	-20	-39
160,000		-5	-13	-26
170,000		-3	-7	-13
180,000		0	0	0
190,000		3	7	13
200,000		5	13	26
210,000		8	20	39
220,000		10	27	52
230,000		13	34	66
240,000		15	40	79

*with proportionate change in other rig rates as well

Source: Company data, Credit Suisse estimates

Summary of day rate assumptions

The table below lists the current contracts with Aban and our assumptions for newer contracts. With concerns on jackup day rates, we have reduced expectations of new contract rates. For 375'+ jackups, we forecast CY09 and CY10 rates at US$180,000 and US$153,000 per day respectively; from recent levels of US$200,000 per day. We reduce expectations for rigs with lower specifications accordingly.

Figure 20: **Aban rigs day rate assumptions**

	Current contract				Assumption beyond current contract	
Rig	**Contract with**	**Contract start**	**Contract end**	**Contact day rate** (USD per day)	**CY2009** (USD per day)	**CY2010 onwards**
Aban India						
Aban II	ONGC	Feb-07	May-10	82,191		63,000
Aban III	ONGC	Apr-08	Jan-11	156,600		133,000
Aban IV	ONGC	Dec-07	Dec-10	156,600		133,000
Aban V	ONGC	May-08	Jan-11	156,600		133,000
Aban VI	PEDCO	Jan-08	Dec-13	81,185		81,185
Frontier Ice	ONGC	Jan-09	Jan-12	150,000		150,000
Tahara	Hardy Oil	Aug-07	Aug-09	87,500	87,500	87,500
Aban Singapore						
Aban Abraham	Vanco	Sep-08	Jan-09	300,000		
Aban Abraham	Addax	Feb-09	Sep-10	410,000	450,000	
Aban VII			Dec-08		160,000	133,000
Aban VIII	Petropars	Jun-08	Jun-12	205,000		153,000
Deep Venture	Exxon	Jul-07	Jun-09	425,000		
Deep Venture	Maersk Oil Angola	Jul-09	Dec-10	495,000		495,000
Murmanskaya			Dec-08		170,000	-
Deep Driller 1	GSPC	Apr-07	Apr-09	194,000	180,000	153,000
Deep Driller 2	Chevron	Jul-08	Apr-09	188,000		
Deep Driller 2	Unknown	May-09	Nov-09	181,000	170,000	143,000
Deep Driller 3	Petronas	Oct-08	Sep-12	165,000		143,000
Deep Driller 4	RIL	Dec-07	Nov-09	220,000	180,000	153,000
Deep Driller 5	Husky Oil	Dec-08	May-09	215,000	170,000	143,000
Deep Driller 6			Dec-08		170,000	143,000
Deep Driller 7	Unknown - Offshore Thailand	Oct-08	Dec-08	200,000	180,000	153,000
Deep Driller 8	Unknown - Offshore India	Jul-09	Nov-09	200,000	180,000	153,000
Bulford Dolphin	Unknown - Offshore LatAm	Nov-08	Oct-13	310,000		310,000

Source: Company data, Credit Suisse estimates

Can contracts be cancelled?

With the fall in oil prices, there is concern that customers may cancel existing contracts to 'trade down'. Larger E&P companies are unlikely to do this; mindful of company reputation. We understand that most contracts build in penalties for cancellation and operate like take or pay contracts. This structure would deter companies from cancelling unless rig rates fell dramatically. The risk of large scale contract cancellation for Aban should be low.

Unless rig rates fell dramatically, the risk of large scale contract cancellations for Aban should be low

Valuations look inexpensive

Earnings-based valuations for Aban have moved from a large premium early this year to a discount now. The large debt increases earnings sensitivity to day-rate movements; the high proportion of rigs contracted reduces sensitivity in the near term. Global drillers are currently trading at a CY09 P/E of 5.4x. We use a lower FY10 P/E of 3.5x for Aban in light of the higher leverage. Our new target price of Rp1,261 implies potential upside of 30%. We upgrade the stock to an OUTPERFORM.

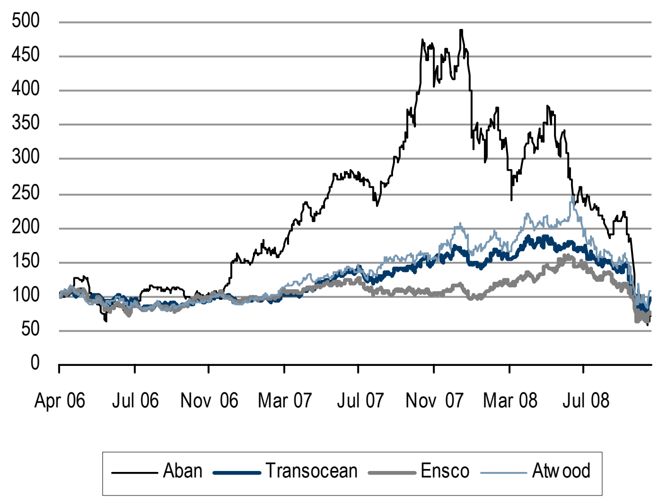
Without any potential upside to day rates and with the large debt, Aban is likely to continue to trade at a discount to peers. With the deployment of newer rigs and announcement of contracts, debt levels should reduce. The consequent lower volatility of earnings expectations should improve valuations for the stock.

Without any potential upside to day rates and with the large debt, Aban may continue to trade at a discount to peers

Any sharp near-term decline in jackup day rates remains the principal risk to earnings. The utilisation of jackups should fall, but the higher specifications of Aban's jackups should allow the company to do better than average on that count.

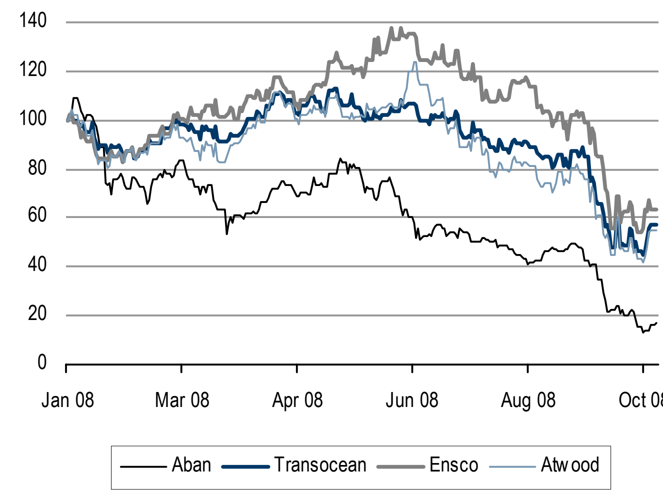
We reduce our utilisation estimates to 90% for FY09E onwards, reduce day-rate estimates, increase debt spreads for newer funding and update on recent contract announcements. Our FY09E EPS drops 43% to Rs189/share and FY10E EPS falls 13% to Rs.360/share.

Figure 21: **Aban rose faster than other drillers significantly since the acquisition of Sinvest …**



Source: Bloomberg, Credit Suisse estimates

Figure 22: **… but has fallen faster than others in the correction, reversing the relative outperformance**



Source: Bloomberg, Credit Suisse estimates

Figure 23: **Comparable valuations**

		Price		Price	Target	Mkt cap	P/E (x)		EV/EBITDA (x)	
Company	**Ticker**	**(l.c.)**	**Rating**	**(Rs)**	**(Rs)**	**(US$ mn)**	**2008E**	**2009E**	**2008E**	**2009E**
Atwood Oceanics	ATW	US$	NEUTRAL	26.3	34	1,706	7.62	5.26	6.30	4.57
Diamond Offshore	DO	US$	NEUTRAL	83.7	93	11,638	8.66	7.51	5.27	4.36
Ensco International	ESV	US$	NEUTRAL	37.1	43	5,252	4.57	5.05	3.02	2.86
Hercules Offshore	HERO	US$	NEUTRAL	7.0	11	617	7.77	7.03	4.68	3.65
Noble Corp	NE	US$	OUTPERFORM	30.5	42	8,216	5.43	4.36	4.08	2.96
Pride International	PDE	US$	NEUTRAL	17.7	26	3,073	4.86	4.97	2.92	2.85
Rowan Companies	RDC	US$	NEUTRAL	18.4	24	2,099	4.91	4.25	3.20	3.14
Transocean	RIG	US$	OUTPERFORM	77.9	108	25,019	5.64	5.17	5.56	4.62
Average							**6.18**	**5.45**	**4.38**	**3.62**
Aban Offshore	ABAN.BO	Rs	NEUTRAL	882.6	3,600	769	8.85	2.67	7.48	3.65

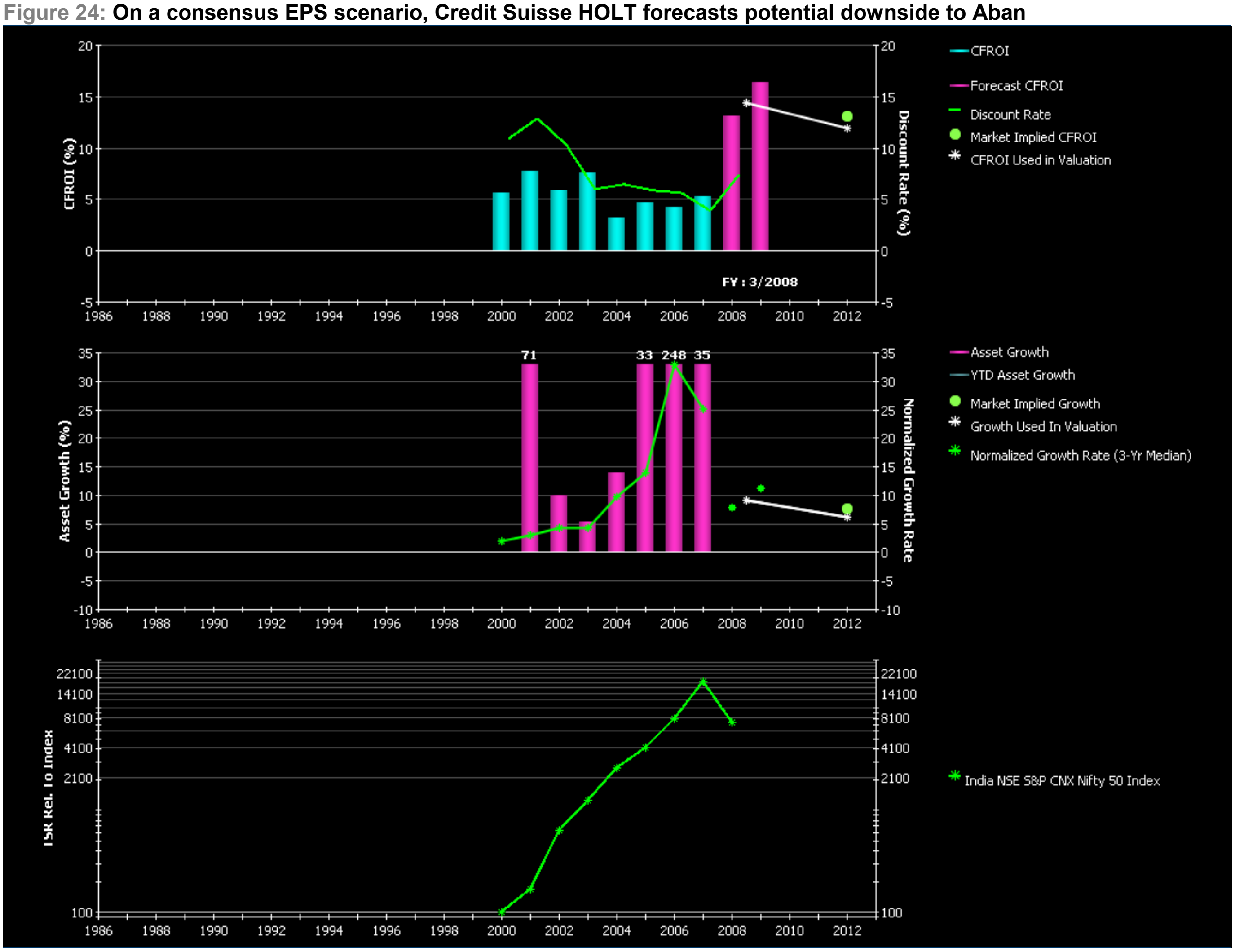
Source: Company data, Credit Suisse estimates

Aban on HOLT

Aban looks expensive on EV/EBITDA comparables. Using consensus EPS estimates, Credit Suisse HOLT™ also forecasts significant potential downside to Aban's share price (~45%). Due to its large debt, all EV-based valuation methodologies tend to imply low residual equity valuations for the firm.

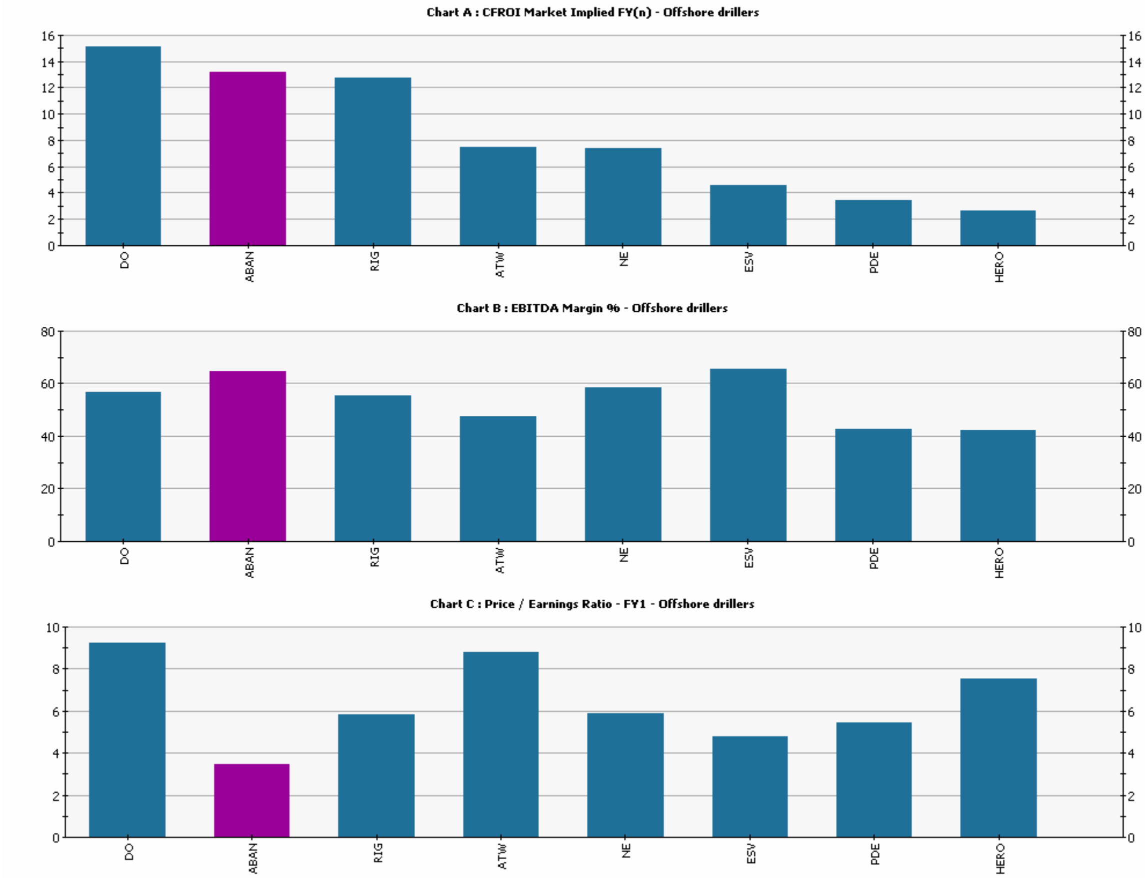
Credit Suisse HOLT values the enterprise maintaining the current capital structure and uses backward-looking asset growth estimates. Even on a default case, the market implied T+5 CFROI® is not too different from the default used by Credit Suisse HOLT (implying the large potential downside). This, again, highlights the large sensitivity of EV-based valuation methods to small changes in assumptions, due to the large amount of debt with Aban.

Figure 24: On a consensus EPS scenario, Credit Suisse HOLT forecasts potential downside to Aban



Source: Credit Suisse HOLT, Credit Suisse estimates

Figure 25: Aban looks stretched on EV valuations, inexpensive on earnings comparisons



Source: Credit Suisse HOLT, Credit Suisse estimates

Figure 26: Large sensitivity to a small change in assumptions

CFROI T+5

GROWTH T+5

	10%	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%
3%	-0.00	32.57	261.66	493.71	728.55	966.01	1205.94	1448.18	1692.60	1939.04	2187.39
4%	-0.00	93.00	333.96	578.03	825.05	1074.84	1327.24	1582.08	1839.22	2098.52	2359.82
5%	-0.00	157.92	411.52	668.41	928.40	1191.33	1457.00	1725.27	1995.97	2268.95	2544.06
6%	-0.00	227.71	494.78	765.32	1039.14	1316.06	1595.89	1878.46	2163.61	2451.18	2741.01
7%	25.19	302.76	584.19	869.28	1157.84	1449.67	1744.59	2042.42	2342.98	2646.09	2951.62
8%	90.84	383.50	680.24	980.85	1285.13	1592.87	1903.88	2217.98	2534.97	2854.67	3176.94
9%	161.64	470.40	783.47	1100.63	1421.68	1746.40	2074.58	2406.03	2740.55	3077.96	3418.08
10%	238.04	563.97	894.47	1229.29	1568.23	1911.06	2257.57	2607.54	2960.77	3317.08	3676.26

Less than 10%
Within 5%
More than 10%

Source: Credit Suisse HOLT, Credit Suisse estimates

Companies Mentioned *(Price as of 10 Nov 08)*
Aban Offshore Ltd (ABAN.BO, Rs968.20, OUTPERFORM [V], TP Rs1261.00)
Atwood Oceanics, Inc. (ATW, $25.39, NEUTRAL [V], TP $34.00)
Diamond Offshore (DO, $81.10, NEUTRAL, TP $93.00)
ENSCO International (ESV, $34.50, NEUTRAL, TP $43.00)
Hercules Offshore (HERO, $6.03, NEUTRAL, TP $11.00)
Noble Corporation (NE, $28.32, OUTPERFORM, TP $42.00)
Pride International Inc. (PDE, $17.38, NEUTRAL, TP $26.00)
Rowan Companies (RDC, $18.00, NEUTRAL, TP $24.00)
Transocean Inc. (RIG, $75.85, OUTPERFORM, TP $108.00)

Disclosure Appendix

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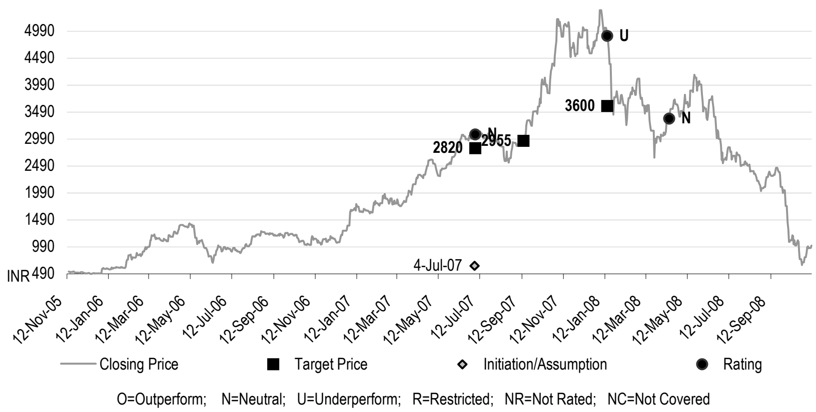
3-Year Price, Target Price and Rating Change History Chart for ABAN.BO

ABAN.BO Date	Closing Price (INR)	Target Price (INR)	Rating	Initiation/ Assumption
4-Jul-07	3,095.85			X
5-Jul-07	3,073.8	2820	N	
14-Sep-07	3,044.6	2955		
15-Jan-08	4,902.65	3600	U	
15-Apr-08	3,368.2		N	



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Price Target: (12 months) for (ABAN.BO)

Method: Our target price of Rs.1261 per share for ABAN.BO is based on 3.5x FY10E EPS of Rs.360; which is when all jackups are expected to contribute to earnings. The multiple we use is at a discount to global comparables in light of its higher leverage..

Risks: The primary risk to our target price of Rs.1261 for ABAN.BO is a decline in jackup day rates before all contracts that are up for negotiation in the next few quarters are signed. The high leverage with the company increases EPS sensitivity to changes in day rates. Delay in delivery of jackups will also affect the earnings of the company.

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