QGOG Constellation SA Oil & Gas

4Q17 Credit Update 25 May 2018 Brazil

SUMMARY - CAPITAL STRUCTURE									
Instrument	Currency	Coupon (%)	Maturity	Original amount (USD m)	Amount outstanding (USD m)	Price	Yield (%)	Z-spread (bps)	Rating: M/S&P/F
2018 Senior Secured Bond (1)	USD	5.25%	July 2018	700	87.7	86.63	98.70		Caa1 / NR / CCC
2019 Senior Unsecured Bond (2)	USD	6.25%	November 2019	700	95.6	68	36.47		NR / D / C
2024 Senior Secured Bond (2)	USD	9%+ 0.5% PIK	November 2024	604.6	591.4	42.38	16.55	1,405	NR / D / C
Bradesco Working Capital	USD	Libor+ 6.8%	July 2018	250	153.0				
Project Finance Loans	USD	L+ 2%-2.75%	2018 - 2020		727.5				
Total Debt					1,655.2				

Source: Debtwire, company filings, Thomson Reuters as of 24 May 2018.

(1) Issuer: QGOG Atlantic / Alaskan Rigs Ltd
(2) Issuer: QGOG Constellation SA

QGOG FACES REVENUE AND LIQUIDITY CONSTRAINTS, POSTPONES DEBT OBLIGATIONS

QGOG NEGOTIATES WITH CREDITORS, SKIPS BOND SERVICE

QGOG Constellation SA started conversations with the project finance lenders for the Amaralina, Laguna and Brava Star rigs following completion of the July 2017 bond exchange, Debtwire has reported. The lenders include ING, Citibank and BNP Paribas. The company has been seeking an extension for the balloon payments, and asked bank lenders for a two-year grace period. During this time, QGOG would try to sign new contracts to enhance cash flows and liquidity.

On 26 April 2018, QGOG extended for three months a USD 75m amortization installment related to its working capital lines under the Bradesco facilities. As a result of the extension, the next amortization payment with Bradesco, totaling USD 153m, is scheduled for 25 July 2018. The company is seeking to negotiate an additional extension of these working capital lines.

QGOG has also proposed a two-year grace period for Bradesco loans followed by quarterly payments until 2024. Bradesco is inclined to accept a debt extension of only as far as 2023 prior to amortization of the senior notes due 2024, as lenders also want the grace period to include payments to bondholders. The banks were unlikely to accept a refinancing into a new loan with little interest if QGOG continues to pay bond coupons while maintaining a low cash balance, Debtwire noted.

On 7 May 2018, QGOG announced that it would utilize the 30-day grace period and defer payments due 9 May of an approximate USD 27m cash interest payment on its USD 591m of 9.5% senior notes due 2024, and an approximate USD 3m cash interest payment on its USD 96m of 6.25% senior notes due 2019.

QGOG made the decision to use the 30-day grace period to advance the ongoing discussions with certain lenders and a group of bondholders representing a material amount of the 2024 notes. It met on 15 May with bondholders, Bradesco and syndicate banks to review potential terms for a restructuring proposal. Holders of the 2019 notes could also take part in restructuring discussions.

Holders of QGOG's 2024 notes were planning to demand a capital injection of approximately USD 100m and an increase in the PIK portion of their interest payment, Debtwire reported. Bondholders had already requested an equity injection during the negotiations for the July 2017 bond exchange offer that the company rejected.

The restructuring negotiations also face challenges regarding the sharing of collateral amongst bondholders and banks. Holders of the senior secured 2024 bonds are not apt to sharing collateral with project finance lenders. There is a greater inclination for holders to share collateral with Bradesco, which may share the collateral that serves QGOG's 2024 bonds under the 2024 bond indenture.

QGOG had a cash balance of USD 269m at 4Q17 and short-term debt totaling USD 656m. Short-term debt consisted mainly of (i) USD 88m for the senior secured Atlantic/Alaskan rigs bonds maturing July 2018; (ii) USD 153m in working capital loans with Bradesco maturing July 2018; (iii) USD 177m of Amaralina Star project finance debt maturing September 2018; and (iv) USD 187m of Laguna Star project finance debt maturing November 2018.

LATIN AMERICA CREDIT RESEARCH

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RECENT *DEBTWIRE* COVERAGE

QGOG Constellation presents cash sweep proposal to creditors (22-May-18)
QGOG to meet with creditors in New York (14-May-18)
QGOG Constellation downgraded to 'C' - Fitch (11-May-18)
QGOG coupon delay pressures creditors; 2019 holders likely to join conversations (10-May-18)
QGOG Constellation to use the 30-day grace period for 2019, 2024 bond coupon payments (07-May-18)

REVENUES TO TUMBLE IN 2018 ON CONTRACT EXPIRATIONS

Estimated 2018 revenues of USD 557m would represent a decline of 41% (USD 389m) from actual revenues of USD 946m for full-year 2017. Average uptime for the ultra-deep water (UDW) fleet was 91% for full-year 2017. Contracts with Petrobras expired in 1Q18 for the UDW Gold Star (February) and Lone Star (March) rigs (See Table 1).

Projected 2H18 revenues of USD 165m represent a substantial decline from projected revenues for 1H18 totaling USD 392m (See Table 2). In addition to the expiration of the Gold Star and Lone Star rig contracts during 1Q18, QGOG has contracts with Petrobras expiring in 2H18 for the Midwater rig of Atlantic Star (July), and the UDW rigs of Brava Star (August), Amaralina Star (September) and Laguna Star (November).

Petrobras has not renewed contracts for the Alpha Star rig, which expired in July 2017, or for the Gold Star and Lone Star rigs. Day rates for the UDW contracts expiring during 2018 ranged from USD 393,543 for Lone Star to USD 565,170 for Brava Star. Day rates of potential contract renewals for these rigs could be substantially lower, as Petrobras recently hired a rig from Sete Brazil for a day rate of USD 229,000.

In January 2018, QGOG commenced work on a new three-year contract for the Deepwater Olinda Star rig with Oil and Natural Gas Corporation (ONGC), an Indian state-owned oil and gas exploration and production company, for operations within an offshore area in India. The day rate with ONGC for Olinda Star is approximately USD 118,000. The company's backlog for the years 2019 and 2020 only includes annual revenues of USD 43m, associated with operations for Olinda Star. QGOG is maintaining the Alpha Star, Gold Star and Lone Star vessels stacked in the state of Rio de Janeiro.

TABLE 1 - CONTRACT AND BANK FINANCING STATUS FOR DEEP WATER RIGS (USD M) - AS OF 31 DECEMBER 2017

	% Interest	Contract Expiration Date	Dayrate (USD/Day)	Water Depth (ft)	Bank Financing (Lead Arrangers)	Security For	Maturity	Outstanding 31 Dec 2017
Ultra-Deep Water								
Alpha Star	100%	July 2017	-	9.000	Citibank, Santander		July 2017	Repaid July 2017
Lone Star	100%	March 2018	393,543	7.900		2024 Bond		
Gold Star	100%	February 2018	477,556	9,000	ING	2024 Bond	Dec. 2017	Prepaid March 2017
Amaralina Star	55%	September 2018	422,360	10,000	BNP, Citi, ING	Project Finance	Sept. 2018	176.8
Laguna Star	55%	November 2018	422,360	10,000	BNP, Citi, ING	Project Finance	Nov. 2018	187.0
Brava Star	100%	August 2018	565,170	12,000	BNP, Citi, ING, DNB	Project Finance	Sep. 2020	363.7
Deep Water								
Olinda Star	100%	January 2021	118,000	3,600		2024 Bond		
Midwater								
Atlantic Star	100%	July 2018	293,678	2,000	Senior Secured Bond	2018 Bond	July 2018	87.7
Alaskan Star	Sold for Scrap Value	November 2016	-	1,700	Senior Secured Bond		July 2018	

Source: Debtwire, company Filings.

TABLE 2 - ESTIMATED 2017/2018 REVENUES FOR DEEP WATER RIGS (USD m) - ASSUMES 100% UPTIME

	Contract Expiration Date	Estimated Revenues First Half 2017	Estimated Revenues Second Half 2017	Estimated Revenues First Half 2018	Estimated Revenues Second Half 2018
Alpha Star	July 2017	77.9	13.0	-	-
Lone Star	March 2018	71.7	71.7	35.4	-
Gold Star	February 2018	87.1	87.1	28.7	-
Amaralina Star	September 2018	76.3	76.3	76.0	38.0
Laguna Star	November 2018	76.3	76.3	76.0	63.4
Brava Star	August 2018	104.0	104.0	101.7	33.9
Olinda Star	January 2021	-	-	21.2	21.2
Atlantic Star	July 2018	52.4	52.4	52.9	8.8
Total Estimated Revenues		**545.7**	**480.8**	**391.9**	**165.3**

Source: Debtwire, company Filings.

ALPHA, ALASKAN EXPIRATIONS IMPACT 4Q17 REVENUES, ADJUSTED EBITDA

QGOG consolidated revenues of USD 219.9m for 4Q17 represented a decline of 15.3% (USD 39.8m) from USD 259.7m in 4Q16. Revenues from ultra-deep water rigs declined 10.7% (USD 23.3m) to USD 194.5m for 4Q17 from USD 217.8m for 4Q16. The main reason for the decline was the expiration of the Alpha Star contract in July 2017, which had been operating at a day rate of close to USD 433,000. Another reason for the decline was lower average uptime for the ultra-deep water fleet of 93% for 4Q17, as compared to 95% for 4Q16.

Revenues from midwater rigs declined 32.9% (USD 12.4m) to USD 25.3m for 4Q17 from USD 37.7m for 4Q16. The principal reason was the expiration of the Alaskan Star contract in November 2016, which had been operating at a day rate of close to USD 302,000. The average uptime of the midwater fleet of 97% during 4Q17 was slightly lower than 98% in 4Q16.

Contract drilling expenses increased 6.8% (USD 4.9m) to USD 77m for 4Q17 from USD 72.1m for 4Q16. The main reason for the increase was expenses of USD 3.4m for materials required to prepare the Olinda drilling rig for the contract with ONGC. Other operating expenses increased USD 136.6m to USD 156.9m for 4Q17 from USD 20.3m for 4Q16. Other expenses in 4Q17 consisted mainly of non-cash charges totaling USD 155.7m, including impairment charges for the Olinda Star, Lone Star and Alpha Star rigs totaling USD 110.6m. The company recorded an operating loss of USD 75.4m for 4Q17 as compared to operating profit of USD 99.8m for 4Q16.

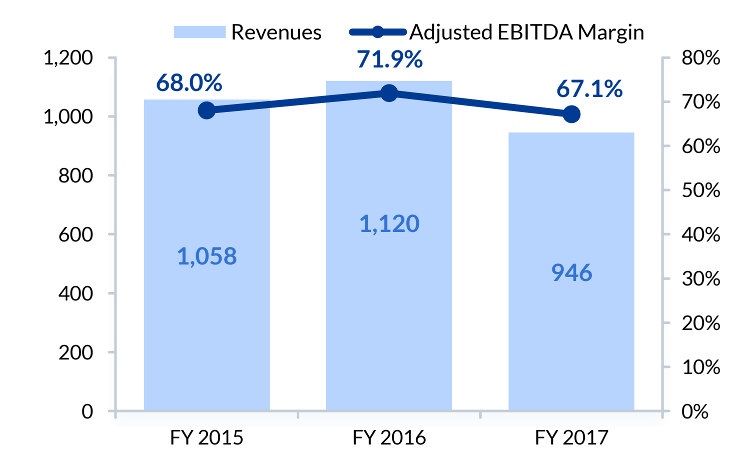
The decline in operating income led to a fall in EBITDA to a negative USD 12.8m for 4Q17 from USD 160.5m for 4Q16. EBITDA adjusted for non-cash charges declined 21% (USD 38.4m) to USD 142.9m for 4Q17 from USD 181.3m for 4Q16. The adjusted EBITDA margin declined to 65% for 4Q17 from 69.8% for 4Q16.

There was a decline in free cash flow of USD 41m to USD 99.5m for 4Q17 from USD 140.5m for 4Q16, the principal cause of which was the fall in adjusted EBITDA of USD 38.4m.

Total debt declined to USD 1.66bn at 4Q17 from USD 1.73bn at 3Q17. A decline in outstanding balance of the Amaralina Star, Laguna Star and Brava Star project finance loans to USD 728m at 4Q17 from USD 773m at 3Q17 reflected debt amortization.

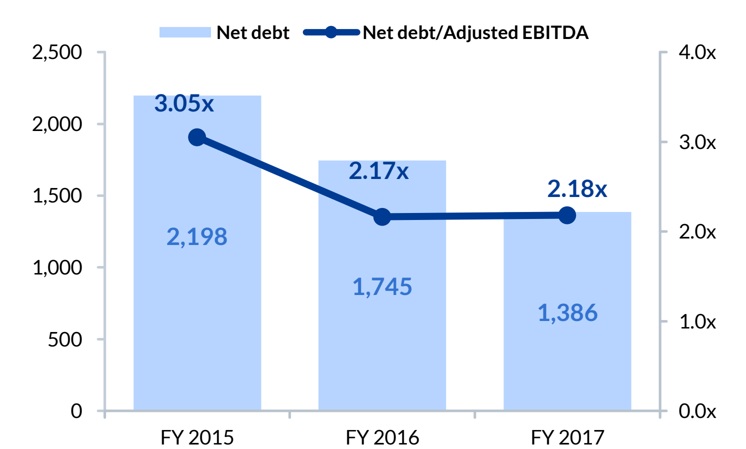
Adjusted EBITDA of USD 635m for FY2017 represented a decline of 21% (USD 171m) from USD 806m for the year FY2016 (See Figure 1 for FY2017 and FY2016 EBITDA margin). QGOG's net debt to adjusted EBITDA ratio of 2.2x (See Figure 2) for FY2017 was comparable to FY2016, and lower than 2024 bond indenture for incurrence of additional debt of 3.75x. Lower adjusted EBITDA led to a decline in the adjusted EBITDA-to-net financial expense ratio to 5.4x for FY2017 as compared to 6.8x for FY2016. Continuing declines in revenues and EBITDA caused by expiring contracts will lead to deterioration in net debt-to-EBITDA ratios for subsequent quarters.

FIGURE 1: HISTORICAL EBITDA MARGIN (USD m)



Source: Debtwire, company filings

FIGURE 2: HISTORICAL LEVERAGE (NET DEBT TO EBITDA-USD m)



Source: Debtwire, company filings

TABLE 3 — CONSOLIDATED FINANCIAL SUMMARY (USD M)	FY15	FY16	FY17	4Q16	4Q17
Ultra-deep water revenues	747.4	902.7	830.8	217.8	194.5
Midwater revenues	193.6	187.9	103.4	37.7	25.3
Deep water / onshore / other revenues	116.7	29.2	11.6	4.2	0.1
Total Net Operating Revenues	**1,057.7**	**1,119.8**	**945.8**	**259.7**	**219.9**
EBITDA	656.5	524.8	479.1	160.5	(12.8)
Non-cash adjustments	63.1	280.7	155.7	20.8	155.7
Adjusted EBITDA	**719.6**	**805.5**	**634.8**	**181.3**	**142.9**
Adjusted EBITDA margin	68.0%	71.9%	67.1%	69.8%	65%
Net financial expense	(108.1)	(118.7)	(117.2)	(27.1)	(28.8)
Total debt	2,621.4	2,195.7	1,655.2	2,195.7	1,655.2
Cash and equivalents	423.4	450.3	268.8	450.3	268.8
Total debt to adjusted EBITDA	3.6	2.7	2.6		
Net debt to EBITDA	3.3	3.3	2.9		
Net debt to Adjusted EBITDA	**3.1**	**2.2**	**2.2**		
Adjusted EBITDA to net financial expense	6.7	6.8	5.4		
Principal Components of Cash Flow Statement:					
Operating cash flow	507.5	890.9	666.7	111.9	246.2
Increase (Decrease in short-term investments)	172.1	(136.2)	(100.4)	67.4	(114.6)
Acquisition of PP&E	(540.2)	(86.2)	(80.2)	(23.4)	(29.9)
Dividends paid	(66.0)	(94.4)	0	0	0
Interest paid on loans and financing	(104.3)	(104.3)	(104.3)	(36.3)	(30.7)
Net proceeds (repayment(from financing	173.9	(435.3)	(532.5)	(140.9)	(75.6)
Free Cash Flow Computation:					
Adjusted EBITDA		805.5	634.8	181.3	142.9
Working Capital Changes		31.0	29.4	22.2	18.4
Acquisition of PP&E		(86.2)	(80.2)	(23.4)	(29.9)
Interest Paid		(104.3)	(104.3)	(36.3)	(30.7)
Dividends Paid		(94.4)	0	0	0
Taxes Paid		(25.7)	(11.1)	(3.3)	(1.2)
Free Cash Flow		**525.9**	**468.6**	**140.5**	**99.5**

Source: Company Filings, Debtwire.