

### **Awilco goes to Keppel – is the rig market back to normal?**

Awilco Drilling's announcement of a \$65 Mn private placement to fund an order for a new harsh environment midwater semi-submersible drilling rig came as a surprise for many market observers, including MSI. After digesting the news however, the order does make sense, or at least a lot more than some of the other asset purchases (on the face of it, the West Rigel deal which Breakwater and Hayfin piled into looks far more aggressive).

Firstly, from a corporate perspective the deal makes sense. Awilco currently owns two elderly rigs, one of which is cold-stacked and will need a significant cash outlay to bring back to the market. In the medium-term, Awilco need a fleet replacement program in order to continue to exist, in part since their prudent management did not overinvest during the market peak. The terms of the contract – with a 10%/10%/80% structure for yard payments and ability to push the delivery back by an additional 12 months from the 2021 delivery date – are certainly favourable to Awilco, and the price also looks competitive (\$455 Mn 'ready to drill' cost, against \$505 Mn equivalent for the Stena MidMAX). Furthermore, with MSI's rig model estimating newbuilding prices will be 18% higher by 2021, taking what amounts to a 10% option on a rig for 2021 delivery now seems a sound idea.

In other words, we think this is a good move for Awilco. Some industry commentators have suggested that this will fire the starting gun for new orders for rigs targeted at the Norwegian sector; we fear that the desperation of Singaporean yards may lead to new orders but we are less than convinced these would be a good idea.



The class of midwater harsh environment floaters to which the Awilco newbuilding rig belongs are heavily focussed on the NW European market, with some incremental demand from Canada. The failure of recent exploration efforts at Flemish Pass in Canada, together with the challenging geology of new exploration work in the UK North Sea, means that the core market for the recent rig orders really boils down to Norway.

In Norway, on the face of it activity is picking up, with an uptick in both rig tenders and wells drilled, whilst dayrates have also picked up strongly – the Deepsea Stavanger's contract rate equates to \$288 k/day . However, we would be cautious about a significant newbuilding campaign centred on Norway. The increase in wells drilled was entirely down to wells associated with production rather than exploration, and whilst of course mega-projects such as Johan Castberg will generate significant near-term demand, the outlook post-2021 is very unclear; Statoil's Arne Sigve Nyland acknowledged as

much, stating that from 2022 onwards there were no major projects planned and that new blocks would need to be allocated.

There are two challenges to the bullish view of the Norwegian outlook; geology and geography. Geographically, significant portions of the Barents and the northern reaches of the Norwegian Sea lie in areas which are either off-limits for offshore drilling – such as the Lofoten Islands – or in areas where drilling would be highly controversial such as offshore Bear Island.

Secondly, with some notable exceptions the geology of the Barents has been less strong than hoped, with the 2017 drilling campaigns for Lundin and particularly Statoil underperforming initial expectations. The recent scandal over the efforts to exaggerate Goliat's profitability to the Norwegian parliament shows the sensitivity of the Barents Sea to all sides of this debate, and a successful 2018 campaign would do much to convince sceptics such as MSI. However, for the time being MSI would recommend ignoring the siren calls of desperate shipyards and avoid overinvesting in the harsh environment semi-submersible fleet.