

Star Energy Geothermal (Wayang Windu) Ltd: Losing Steam

Wednesday, May 09, 2012

Trade recommendation

At current indications of 109.30/110.10, the STAREN'15s have a mid-YTW of 5.65%. With high gearing and weak credit metrics, we consider this to be rich in the Indonesian HY universe. Despite trading above the call price of 105.75, we ascribe a low probability to a call, given its need for cash to fund Unit 3 capex and the consequent inability to generate significant free cashflows. Underweight.

Key credit considerations

- **Good operating performance:** Operating performance in 2011 was strong, with availability factors of 100% and 99.9% for Units 1 and 2 respectively and corresponding net capacity factors of 95.8% and 97.1%. Actual power production was 1,878GWh, down 2.3% y/y and 0.6% below target, due to curtailment of steam supply to accommodate drilling rig operations.
- **Award of EPC contract for Unit 3 likely to be after 1st January 2013:** STAREN opined that the result of its drilling program has performed below expectations. The 10 completed wells and current drilling of well No.11 is only sufficient to add an additional 96kg/s of steam (equivalent to 49MW), bringing total steam supply to 485kg/s. Given that 450kg/s of steam is needed for Units 1 and 2 and another 100kg/s steam buffer is required (i.e. 550kg/s total), the incremental steam generated thus far will go towards the buffer and not used for Unit 3. Further steam studies will be conducted and concluded by June 2013 at the earliest. As such, the pending award of the EPC contract for construction of Unit 3 is unlikely to be awarded before 1st January 2013, pending completion of the steam study.
- **Capex outlays will remain moderate in the near-term:** With the uncertainty of tapping existing steam reserves for Unit 3, budgeted capex for 2012 is limited to further drilling, consulting and pre-operating expenses, totaling US\$41.7mn. Cumulative spending thus far for drilling and pre-operating expenses for Unit 3 (including 2012 budgeted amount) is US\$113.3mn (41% of initial estimated project cost of US\$277mn for 127MW expansion). Cost overruns is an elevated possibility should it wish to embark on the whole 127MW expansion, with limited deleveraging headroom, given that FY2011 FOCF/gross debt was an anaemic 0.7%.
- **Likelihood of tariff increase is uncertain:** Management opined that new geothermal capacity in West Java is getting tariffs of US\$0.097/kWh (STAREN's 2011 tariff was US\$0.0632) and that it is trying to negotiate with PLN to obtain a similar tariff. Though the likelihood of a tariff adjustment is uncertain, STAREN indicated that it will not move ahead with Unit 3 construction until it has achieved a tariff increase and/or secured a feed-in tariff from the Indonesian government.

Underweight

S&P: Not rated
 Moody's: B2 Outlook: Stable
 Fitch: B+ Outlook: Stable

Ticker: STAREN

Treasury Advisory

Corporate FX & Structured Products

Tel: 6349-1888 / 1881

Fixed Income & Structured Products

Tel: 6349-1810

Interest Rate Derivatives

Tel: 6349-1899

Investments & Structured Products

Tel: 6349-1886

Jerry Gwee, CFA, CAIA

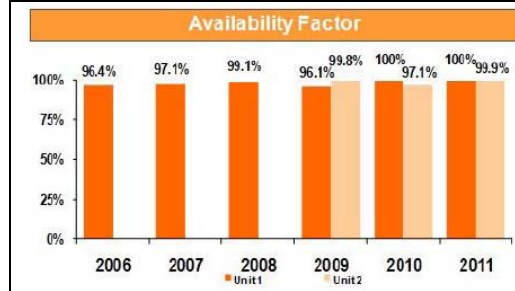
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- **Weak leverage metrics:** Net debt was almost flat to FY2010 levels at US\$184.5mn, with net debt/EBITDA of 2x. Net debt/net capitalization is still an elevated 82.2% (down 4pp y/y) while EBITDA/gross interest is a weak 1.8x and FOCF/gross debt of 0.7%.
- **Tight operating cashflows will likely require refinancing of bullet maturity in 2015:** Under the bond indenture, should STAREN fail to proceed with an EPC contract by 1st January 2013, the bond will be subjected to 4 semi-annual principal amortizations of US\$12.5mn each, starting from 12th February 2013. With cash balance of US\$165.5mn at end-FY2011, expected CFO of US\$40mn – 60mn p.a. and minimum capex outlays of c.US\$42mn in 2012 (likely a similar amount in 2013 as well since steam study will only be completed by June 2013 at the earliest), we expect STAREN to meet total scheduled debt repayments of US\$50mn till August 2014. Notwithstanding this, the inability to generate significant free cashflows portends a material refinancing risk for the bullet bond maturity in 2015.

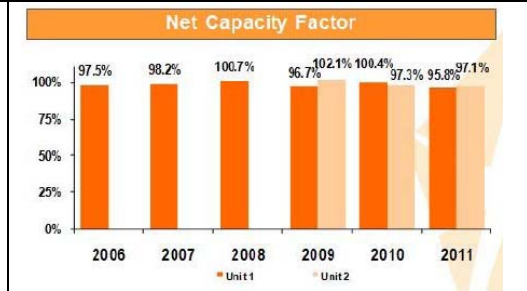
Appendix A

Chart 1: Availability factor



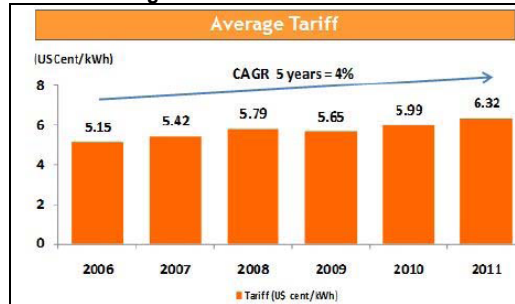
Source: Company

Chart 2: Net capacity factor



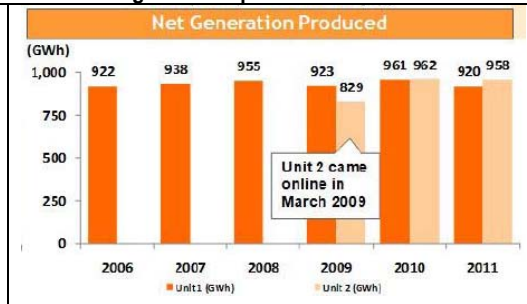
Source: Company

Chart 3: Average tariff



Source: Company

Chart 4: Net generation produced



Source: Company

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