Asia Credit Research

OCBC Bank

Ezra Holdings Limited: Credit Update

Tuesday, 19 April 2016

Kitchen Sink Quarter

- **Provisions and impairments overwhelm**: EZRA reported 2QFY2016 results for the quarter ending February 2016. It is the first offshore marine issuer under our coverage to report (partial) 1Q2016 results. The numbers look grim, driven by the challenging environment pressuring performance, as well as impairments and provisions that EZRA had taken during the quarter. It should be noted that a number of EZRA's peers in the offshore marine space have taken impairments and provisions during the quarter ending December 2015. Given EZRA's atypical financial quarters, it is not surprising that management considered the weak environment and took some impairments / provisions as well.

- **Diving into the numbers**: For 2QFY2016, EZRA reported USD111.2mn in total revenue, a decline of 13.9% y/y (note that since November 2015[1], EZRA has deconsolidated its EMAS AMC subsea division post the announcement of the JV). The slump in revenue was largely driven by the OSV division (mainly EMAS Offshore), with EMAS Offshore seeing a 50% fall y/y to just USD30.5mn for the quarter. There was both pressure on utilization (~51%, with management indicating that the 1st half of the fiscal year tends to be softer due to the winter season) as well as on charter rates. The market for PSVs was particularly weak. The shipbuilding division (mainly Triyards), managed to sustain its performance despite the difficult environment. Triyards revenue was up 15.4% y/y to USD70.5mn, driven by revenue recognized on work done on four liftboats, two MPSVs and three chemical tankers. As for the subsea division (EMAS AMC, now treated as discontinued operations, not reported under total revenue), revenue generated was USD108.4mn, a decline of 37.3% y/y. Subsea performance was attributed to both the winter season, as well as challenging conditions for deepwater projects.

- **Earnings took a beating**: EZRA generated a gross loss of USD0.2mn for the period. This was largely driven by its OSV division, with EMAS offshore generating USD15.4mn in gross loss for the quarter, overwhelming the USD14.8mn in gross profit generated by Triyards. During the quarter, EZRA's administrative expenses surged from USD17.1mn (1Q2015) to USD97.6mn (1Q2016) due to USD48.6mn in allowance for doubtful debts (on some long outstanding receivables) as well as USD18.9mn for bad debt written off. During the quarter, EZRA also incurred USD115.5mn in other expenses. This includes USD18.1mn of losses incurred from the disposal of fixed assets (ie: vessel sales), about USD60.5mn in impairments taken on fixed assets (mainly EZRA's PSV fleet, done at the EMAS Offshore level), as well as USD38.3mn in impairment losses on JVs (held at the EMAS Offshore level, these two JVs, EMAS Victoria Bhd and SJR Marine Ltd are mainly ship owning and leasing JVs focused on Malaysia). Impairment losses generated at associate Perisai Petroleum (23% owned) also impacted EZRA's bottom line (USD32.1mn impact). Of the USD251.8mn in pre-tax losses generated by EZRA, about USD166.3mn were driven by impairments and provisions.

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[1] OCBC Asia Credit - Ezra Credit Update (12 Nov 2015)

- **Orderbook**: As of end-2QFY2016, EZRA had USD513mn in shipbuilding orders, USD400mn in orders at EMAS Offshore and ~USD400mn in subsea orders. FPSO contract backlog (USD360mn worth) was excluded due to EZRA's intent to divest part of the business). Looking forward, management was cautiously optimistic in rebuilding its subsea orderbook, and is in the final stages for certain large tenders.

- **Cash burn was elevated**: During the quarter, EZRA generated negative USD54.5mn in operating cash burn (given the slight gross loss generated during the quarter). Capex was also higher than expected at USD76.1mn. Management indicated that this was largely due to a vessel purchase done at the EMAS Offshore level. As such, FCF was negative USD130.6mn for the quarter. The cash gap was met in part by USD59.6mn in net borrowings, USD24.3mn from its cash balance as well as USD18.2mn in vessel sales. It should be noted that EMAS Offshore (the OSV division) still has USD91.7mn in committed capex outstanding (as of end-2QFY2016).

- **Credit profile deteriorated sharply**: The increase in borrowings and use of cash has driven net gearing sharply higher, from 81% (end-1QFY2016) to 110% (end-2QFY2016). Cash / current borrowings was weak at just 0.3x. It is worth noting that Ezra has already redeemed its SGD95mn in bonds maturing on 21/03/16. This was refinanced by a SGD100mn term loan that was secured against Ezra's shareholdings in EMAS Offshore and Triyards, and will be reflected in the 3QFY2016 results. Interest coverage for 1HFY2016 was poor at -2.9x given the negative EBITDA generated from the provisions / impairments taken. The recently completed second round of consent solicitation[2] meant that EZRA has some flexibility over its interest coverage covenant till August 2017. Note that the minimum consolidated total equity of USD600mn covenant still applies (total equity stands at USD1044.1mn as of end-2QFY2016).

- **Bitter medicine mostly taken**: EZRA results remain very much in transition due to the Chiyoda JV as well as the impairments and provisions taken during the quarter. As such, we can expect 2HFY2016 to be more representative of EZRA's performance going forward. As mentioned previously[3], the Chiyoda JV is strategically beneficial to EZRA, and the transaction consideration (USD150mn) paid by Chiyoda will be helpful in injecting fresh liquidity into EZRA. Management has indicated that the transaction consideration remains as stated in the MOU filed previously. It should be noted as well that EZRA has announced that it has accepted a non-binding LOI for 78.4% of PV Keez (book value of USD77.2mn as of end-FY2015), which holds the FPSO Lewek EMAS. The liquidity generated from the divestment will also be helpful in shoring up EZRA's balance sheet.

- **Conclusion**: 2QFY2016 results have reflected continued challenges in the offshore marine environment. Though we believe the Chiyoda JV successfully closing to be a huge credit positive for EZRA, EZRA's subsea division as well as OSV division continue to face headwinds, which would in turn prevent any meaningful near-term improvements to EZRA's credit profile. As such, we will continue to hold EZRA's **Issuer Profile at Negative.** As for the sole bond outstanding, the EZRASP'18s, we continue to be **Overweight**, given the attractive risk-to-reward. The bond is now trading at an offer of 85c, or 13.7% YTM (spread of over 1200bps over swaps) for a bond maturing in two years. With the Chiyoda JV / equity infusion a certainty, and potentially more liquidity from the FPSO sale, we believe that there are enough positive catalysts that have occurred to warrant a positive re-rating to the bond.

[2] OCBC Asia Credit - Ezra Credit Update (24 Mar 2016)
[3] OCBC Asia Credit - Ezra Credit Update (5 Apr 2016)

Ezra Holdings Ltd

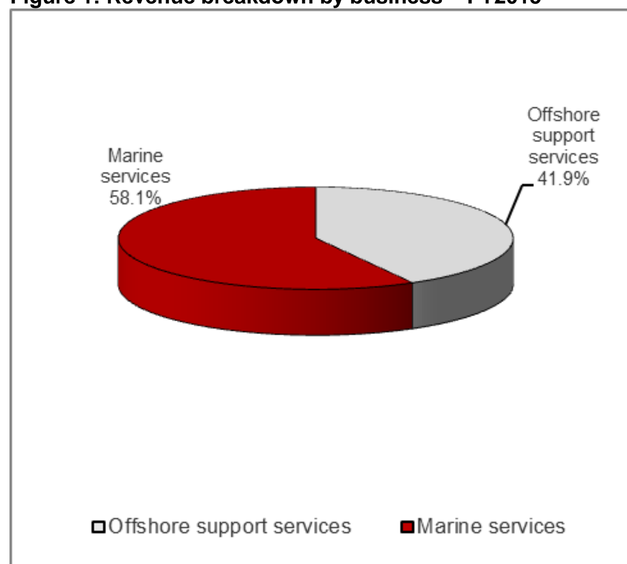
Table 1: Summary financials

Year ended 31st August	FY2014	FY2015	1H2016
Income statement (US$ mn)		restated	restated
Revenue	1,488.4	543.8	263.4
EBITDA	141.8	76.3	-62.8
EBIT	69.6	7.0	-98.8
Gross interest expense	51.3	52.3	21.5
Profit Before Tax	74.7	79.1	-332.3
Net profit	45.3	43.7	-305.3
Balance Sheet (USD'mn)			
Cash and bank deposits	178.9	417.8	150.0
Total assets	3,363.0	4,177.3	3,486.9
Gross debt	1,551.9	1,470.2	1,293.8
Net debt	1,373.0	1,052.3	1,143.8
Shareholders' equity	1,185.8	1,365.3	1,044.1
Total capitalization	2,737.7	2,835.5	2,337.9
Net capitalization	2,558.8	2,417.6	2,188.0
Cash Flow (USD'mn)			
Funds from operations (FFO)	117.4	113.0	-269.3
CFO	140.1	142.5	-42.0
Capex	327.4	320.5	85.8
Acquisitions	0.0	-25.2	0.0
Disposals	8.5	30.3	18.2
Dividend	5.4	0.0	0.0
Free Cash Flow (FCF)	-187.3	-178.0	-127.8
FCF adjusted	-184.1	-122.5	-109.6
Key Ratios			
EBITDA margin (%)	9.5	14.0	-23.8
Net margin (%)	3.0	8.0	-115.9
Gross debt to EBITDA (x)	10.9	19.3	-10.3
Net debt to EBITDA (x)	9.7	13.8	-9.1
Gross Debt to Equity (x)	1.31	1.08	1.24
Net Debt to Equity (x)	1.16	0.77	1.10
Gross debt/total capitalisation (%)	56.7	51.8	55.3
Net debt/net capitalisation (%)	53.7	43.5	52.3
Cash/current borrowings (x)	0.4	0.6	0.3
EBITDA/Total Interest (x)	2.8	1.5	-2.9

Source: Company, OCBC estimates

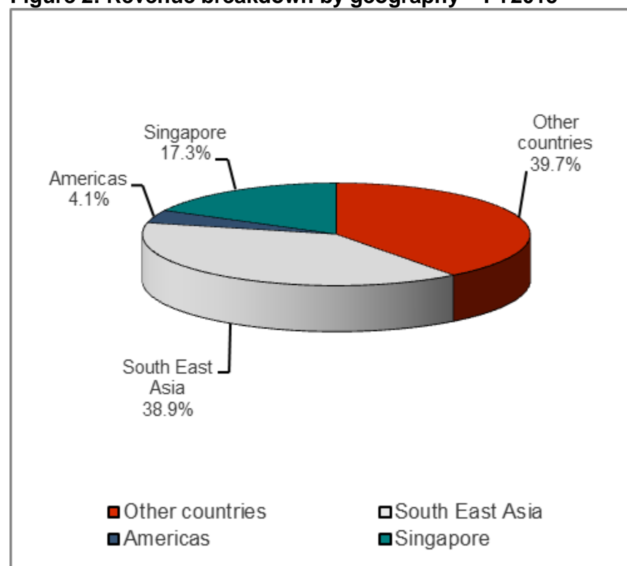
**Adjusted FCF = FCF –Acquisitions – Dividends + Disposals*

Figure 1: Revenue breakdown by business – FY2015



Source: Company

Figure 2: Revenue breakdown by geography – FY2015



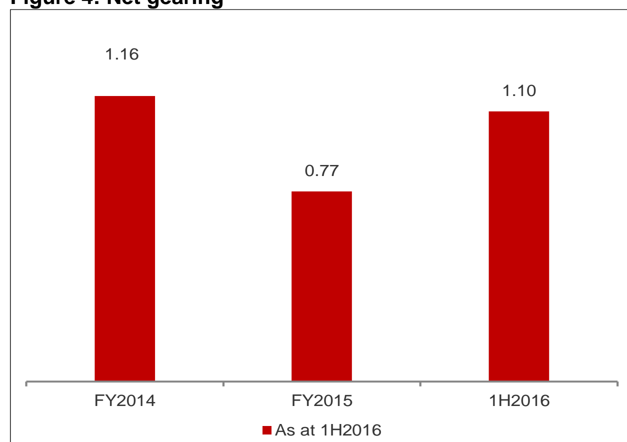
Source: Company

Figure 3: Debt Maturity Profile

Amounts in (USD'mn)	As at 31/12/2015	% of debt
Amount repayable in one year or less, or on demand		
Secured	243.1	18.8%
Unsecured	323.6	25.0%
	566.7	**43.8%**
Amount repayable after a year		
Secured	467.3	36.1%
Unsecured	259.8	20.1%
	727.1	**56.2%**
Total	**1293.8**	**100.0%**

Source: Company

Figure 4: Net gearing



Source: Company, OCBC estimates

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