Issuer Profiles:

KEP: Neutral (5)
KRIS: Unrated

Ticker:

KEPSP
KRISSP

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Keppel Corporation Ltd ("KEP") and KrisEnergy Ltd ("KRIS")

Our take on the situation:

- **KRIS has announced that the company will proceed with liquidation. On 31 March 2021, the company announced that five of its key development wells off the Cambodian coast appear less productive than initial forecast.**
- **Subsequently in April 2021, KRIS announced that the restructuring plan was no longer viable where the company was also not able to propose an alternative restructuring plan to its bank lender and KEP.**
- **This was despite the company completing a number of important restructuring steps in 1Q2021. The scheme though is no longer in effect. In a liquidation, priority of ranking will take precedence.**
- **Actual recoveries are highly uncertain given that bulk of KRIS assets are in exploration and evaluation assets as well as oil and gas properties which would need to be sold and monetized.**
- **We observe no active trading on the KRISSP' 22s and KRISSP '23s, with the KRISSP 0% '24s (a retail bond) priced at distressed levels of ~15 cents to the dollar, with a wide bid-ask spread. The KRISSP 0% '24s is a secured bond while the other two tranches are unsecured.**
- **With the weakest security package, we think actual recoveries on the KRISSP 0% '24s is likely to be significantly smaller (if any) compared to KEP's other secured exposures (the project financing loan, contract assets and RCF) as these will be paid first in a liquidation.**
- **KEP had written-down the KRISSP 0% '24s to SGD35.1mn as at 31 December 2020. Assuming KEP still hold 76.9% of these bonds, this reflects a write-down of SGD SGD72.2mn. A write-down of this secured bond by KEP while still subject to further assessment, points towards lack of recoveries for unsecured creditors.**
- **We expect minimal (if any) recoveries on the KRISSP' 22s and KRISSP '23s.**

OCBC Credit Research does not cover KRIS and has not covered KRIS historically. We have presented sections on KRIS on the back of investor interest. KEP is part of our official coverage. Please refer to our credit update dated 4 May 2021 and recent Asian Credit Daily publications for further information on KEP.

Background

- Kris Energy Ltd ("KRIS"), incorporated in the Cayman Islands, is an independent upstream company focusing on the production and development of oil and gas in Southeast Asia.
- Trading in the company's listed equity on the Singapore Stock Exchange has been suspended since 14 August 2019 and the company announced that it will proceed into liquidation on 4 June 2021.
- Listed in July 2013, KRIS is ~40%-owned by Keppel Corporation Ltd ("KEP") although KEP had fully written down the value of its equity stake in the company since end-2019.
- KEP still has other exposures in relation to KRIS, and these have not been fully written off as of writing.
- Previously in November 2016, as part of a broader financial restructuring, KRIS launched a CSE to exchange existing bonds (the KRISSP 6.25% '17s and KRISSP 5.75% '18s, issued in June and August 2014 respectively) into new senior unsecured notes (the KRISSP '22s and KRISSP '23s, with fixed coupon plus coupons linked to Brent prices) to alleviate short term liquidity pressures at the company. At that point, the company indicated that any potential defaults or cross defaults arising from the failure of its consent solicitation exercise could lead to KRIS losing its operatorships and petroleum licenses as a result of government confiscation. The CSE was approved by bondholders on 9 December 2016.

- As part of that earlier restructuring, shareholders of KRIS (including KEP) also subscribed to a preferential offering of zero-coupon bonds (the KRISSP 0% ‘24s with detachable warrants, issued in January 2017), raising ~SGD139.5mn for KRIS. The zero-coupon bonds are listed on the SGX in retail bond tranches. Per KRIS’ amended explanatory statement dated 27 November 2020, KEP holds ~76.9% of the KRISSP 0% ‘24s.

What has happened at KRIS since the first CSE?

- Since the first CSE, KRIS underwent board and management changes, with founding directors stepping down from executive roles at the company. Cost cutting measures remained in place and the company focused its attention on oil development and production in offshore Thailand and offshore Cambodia, relinquishing certain assets in other geographies.
- Led by the prolonged downturn in crude oil prices, KRIS’s assets had been impaired with book value of equity corroded; liquidity profile had come under pressure while the company’s ability to continue as a going concern was being questioned since April 2019.
- In August 2019, KRIS applied to the Singapore High Court to commence a court-supervised process to reorganise its liabilities and seek a moratorium against enforcement actions and legal proceedings by creditors against KRIS.
- In 2Q2020, KRIS suspended production at the Wassana oil-field in the Gulf of Thailand due to heightened uncertainties from the pandemic with depressed oil demand and prices.
- After a series of informal bondholder meetings, KRIS progressed with its restructuring which was to be implemented via four inter-conditional processes that required majority consent from each group of capital providers per a February 2021 update from the company. These four processes include:
  (1) Amendment of the revolving credit facility (“RCF”). The RCF is provided by a bank lender, though KEP is economically exposed to this RCF through a separate bilateral agreement with the bank lender. As of February 2021, the maturity date of the RCF was extended by six months to 30 June 2021 and was envisaged to be extended further if the restructuring is successfully completed.
  (2) Scheme of arrangement to convert unsecured creditor claims into equity. These include the KRISSP ‘22s and KRISSP ‘23s (aggregate principal outstanding of SGD330mn). The scheme was approved by unsecured creditors in January 2021 and sanctioned by the court in February 2021.
  (3) CSE to partially convert the senior secured zero-coupon bonds (45% of principal outstanding on the KRISSP 0% ‘24s) into equity and amend the terms of 55% of principal outstanding on the zero-coupon bonds. This was approved by the zero-coupon bondholders on 11 February 2021. The KRISSP 0% ’24s were issued in January 2017. KEP is a significant holder of these zero-coupon bonds. We assume KEP still holds ~76.9% of these zero-coupon bonds with a principal outstanding of SGD107.3mn. KEP’s carrying value of this investment was SGD74.3mn as at end-2019, though written-down to SGD35.1mn as at end-2020.
  (4) Extraordinary general meeting for shareholders to approve the issuance of new shares to fulfill the debt-to-equity swaps. The EGM had not been held prior to 31 March 2021 and is not expected to be held in light of subsequent developments.
- On 31 March 2021, KRIS announced that based on its preliminary analysis, five of its key development wells at the Aspara Mini Phase 1A development, off the Cambodian coast (“Aspara”) appear less productive than initial forecast and material uncertainty exists over KRIS’s ability to complete its current restructuring exercise and to continue as a going concern.
- In April 2021, KRIS announced that the restructuring plan was no longer viable with trading resumption likely to be rejected by the SGX. The company was also not able to propose an alternative restructuring plan to its bank lender and KEP.
- In 2020, KRIS took a total of USD105.8mn (~SGD139.6mn) in various impairment losses, provision of obsolete inventories and loss on commitments of exploration and evaluation assets (2019: USD89.2mn (~SGD117.7mn)).

What has happened at KRIS since announcing the liquidation?

- Subsequent to the liquidation announcement, the company has received a notice from the bank lender on the RCF. The bank lender has cancelled the total RCF commitments and declared that all loans are now payable on demand. The security agent on a loan extended by KEP's subsidiary to KRIS in relation to the Aspara project has also been notified of an event of default.

What is next for KrisEnergy unsecured bondholders?

Given that the second restructuring processes were inter-conditional and that certain of the implementation conditions has not been met, the scheme has no effect based on our interpretation of the disclosures. The debt-to-equity swaps have not taken place. Notwithstanding the possibility of movements post year-end, we think the end-2020 numbers can be used as a proxy for the capital structure, no financials as at 31 March 2021 for KRIS has been disclosed.

The bond issuer holds minimal assets with bulk of assets held at other KRIS entities. KRISSP '22s, KRISSP '23s and KRISSP 0% '24s are issued at the holding company level and subjugated to operating entities which hold the assets. Aside from structural subordination, bulk of KRIS' assets have been used as security to obtain financing, namely for the RCF, a project financing loan extended by KEP for the Aspara project and the KRISSP '23s and KRISSP 0% '24s.

We expect recoveries to be based on priority of ranking in KRIS's liquidation, with minimal recoveries (if any) to the unsecured creditors. KRISSP '22s and KRISSP '23s will only get the residual value, if any are still remaining post distribution to the secured creditors.

The RCF is secured by a comprehensive first ranking security package over the producing and development assets of the company. Kepinvest Singapore Pte. Ltd, ("Kepinvest"), a wholly-owned subsidiary of KEP, is a project financing lender to two wholly-owned indirect subsidiaries of KRIS for the development of Aspara. Kepinvest as lender holds a security package consisting of a share pledge over the shares of the KRIS borrowers and the assets of the borrowers, among others.

The KRISSP 0% '24s is a secured bond with a security interest over the shares and certain accounts of SJ Production Barge Ltd ("SJPB", a wholly-owned subsidiary of KRIS). However, Keppel Shipyard Limited (an indirect wholly-owned subsidiary of KEP) has first-ranking statutory mortgage over the sole asset owned by SJPB. The sole asset is a production barge, which was modified and upgraded by KEP's shipyard in 2019. This zero-coupon bond also has a junior ranking security interest over the assets secured under the RCF. In the event that the sole asset at SJPB does not cover Keppel Shipyard Limited's claims, the SJPB shares are unlikely to be of much value while the zero-coupon bonds only have the residual value after the RCF claimants has taken first bite of the assets.

Recovery values highly uncertain

KRIS' exploration and evaluation assets as well as oil and gas properties on a combined basis amounted to USD332.7mn (~SGD439.1mn) as at 31 December 2020. These represent ~69% of KRIS' total assets as at 31 December 2020. While some of these comprise of producing assets, it also includes earlier stage exploration licenses where maintenance of concession rights and extension of licenses depends on fulfillment of capex commitments and government authorities, among others. Actual recovery value from these assets are highly uncertain, especially in a distressed sale scenario and amidst a decarbonization backdrop which could limit the number of buyers.

As part of the earlier scheme of arrangement process, Crowe Horwath was engaged by KRIS to conduct an independent valuation on a liquidation analysis. Per Crowe Howarth's data, average estimated recovery rates for oil and gas assets from precedent corporate liquidation analysis in the upstream oil and gas sector was 33%-44%. Using 33% as recovery rate, the exploration and evaluation asset as well as oil and gas properties implies a recovery value of SGD144.9mn. This though is insufficient to cover the RCF of SGD247mn as at 31 December 2020 as well as the project financing loan for Aspara. This project financing loan facility is up to USD87mn (~SGD114.8mn) though as at 31 December 2020, KEP recognized only SGD77mn of project financing loan receivable. As a side note, 33% is higher compared to Crowe Horwath's liquidation analysis that also factors in the actual bids received by KRIS in 2019.

Other assets at KRIS includes other property, plant and equipment, inventories, trade and other receivables, prepayments, unrestricted cash and bank balances. Assuming an optimistic 100% recovery rates, these amount to USD129.4mn (~SGD170.8mn) in aggregate as at 31 December 2020.

Possibility of alternative plan

At the time of scheme of arrangement, the disclosures highlighted that KRIS and KEP have explored and discussed the possibility of an alternative plan. The alternative plan contemplates a "managed liquidation" where KRIS assets would be transferred into a new company controlled by the senior secured creditors, with the holders of the KRISSP 0% '24 and RCF bank lender releasing their claims in return for stakes in the new company. It is worth noting though that the KRIS board has no power to affect an alternative plan under a liquidation and this power rests with liquidators appointed by the Cayman Island courts. It remains to be seen if an alternative plan emerges.

What is the impact on KEP?

Since the debt moratorium at KRIS, we have been highlighting the possibility of KEP taking further impairments, with this risk escalating since KRIS' announcement on Aspara. A liquidation at KRIS and the amount of KEP's exposure is within our base case for KEP's issuer profile of Neutral (5). As such we are not changing our issuer profile of KEP on the back of the developments at KRIS.

Aside from owning a 40%-equity stake in KRIS, KEP is a project financing lender to KRIS and is also economically exposed to the KRIS RCF. KEP also holds other assets in relation to KRIS (eg: contract assets and its investments in the KRISSP 0% '24s bonds). While KEP has written-down the book value of the equity stake fully by end-2019 as well as the detachable warrants on the KRISSP 0% '24s, it has yet to fully write-down the other exposures as of writing. KEP's exposure on the RCF is an off-balance sheet item. We have no access to the detailed terms between KEP and the bank lender which was agreed under a bilateral agreement, though we expect KEP to "make-whole" the bank, should the recovery value from the underlying security be insufficient to cover the claims under the RCF.

On 8 June 2021, KEP updated that the carrying value of these exposures, including the RCF amount is ~SGD423.2mn as at 31 March 2021 although did not provide a breakdown of the items that make up the number. KEP further announced that it will recognise SGD318mn of losses in 1H2021 in respect of its exposures to KRIS, which factors estimated recoverable amounts of the various assets at KRIS and costs for realization of assets. KEP though did not specify its assumption on recoverable amounts.

Aside from the equity and detachable warrants (which we expect to have zero recovery in the liquidation), KEP had written down some of its exposure on the KRISSP 0% '24s. We assume that KEP's principal amount on this is SGD107.3mn and written-down by SGD72.2mn to SGD35.1mn by end-2020. This implies that excluding the equity stake and detachable warrants, KEP's exposure including the RCF was SGD495.4mn prior to the write-down.

Since KEP has guided a loss of SGD318mn for 1H2021, we assume that the recoverable amount estimated is between SGD105.2mn to SGD177.4mn. The upper end being the grossed-up exposure less the losses.

With the weakest security package, actual recoveries on the KRISSP 0% '24s is likely to be significantly smaller (if any) compared to KEP's other secured exposures (the project financing loan, contract assets and RCF) as these will be paid first in a liquidation. On a cash flow basis, our base case assumes KEP needs to "make-whole" and pay the RCF bank lender SGD247m. This is a conservative assumption as the bank lender may still be able to recoup from the security on the RCF.

Explanation of Issuer Profile Rating / Issuer Profile Score

Positive ("Pos") – The issuer's credit profile is either strong on an absolute basis, or expected to improve to a strong position over the next six months.

Neutral ("N") – The issuer's credit profile is fair on an absolute basis, or expected to improve / deteriorate to a fair level over the next six months.

Negative ("Neg") – The issuer's credit profile is either weaker or highly geared on an absolute basis, or expected to deteriorate to a weak or highly geared position over the next six months.

To better differentiate relative credit quality of the issuers under our coverage, we have further sub-divided our Issuer Profile Ratings into a 7 point Issuer Profile Score scale.

IPR	Positive		Neutral			Negative	
IPS	1	2	3	4	5	6	7

Please note that Bond Recommendations are dependent on a bond's price, underlying risk free rates and an implied credit spread that reflects the strength of the issuer's credit profile. Bond Recommendations may not be relied upon if one or more of these factors change.

Explanation of Bond Recommendation

Overweight ("OW") – The bond represents **better relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

Neutral ("N") – The represents **fair relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

Underweight ("UW") – The represents **weaker relative value** compared to other bonds from the same issuer, or bonds of other issuers with similar tenor and comparable risk profile.

Other

Suspension – We may suspend our issuer rating and bond level recommendation on specific issuers from time to time when OCBC is engaged in other business activities with the issuer. Examples of such activities include acting as a joint lead manager or book runner in a new issue or as an agent in a consent solicitation exercise. We will resume our coverage once these activities are completed.

Withdrawal ("WD") – We may withdraw our issuer rating and bond level recommendation on specific issuers from time to time when corporate actions are announced but the outcome of these actions are highly uncertain. We will resume our coverage once there is sufficient clarity in our view on the impact of the proposed action.

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