2020 Atwood Oceanics 6.5% Senior Notes
Headquarters: Texas, USA
Industry/Sector: Oil & Gas Drilling

Proposal:
Buy 2020 Atwood Oceanics 6.5% Senior Notes at 51 or lower.

Reason of Brief:
The market is inefficiently pricing the 2020 Atwood notes despite these receiving full recovery in multiple scenarios. This brief will explain why you will benefit from the proposal even if the company were to undergo a reorganization or liquidation. Under a liquidation scenario the notes would receive a 95.29 recovery even with a 20% haircut applied. Under a going-concern valuation based on EBITDA multiples, bondholders would receive full recovery, even with the haircut applied.

Company Background:
Atwood Oceanics Inc. (NYSE: ATW) is a global offshore drilling contractor engaged in the drilling and completion of exploratory and developmental oil and gas wells. The company currently owns a diversified fleet of 11 mobile offshore drilling units located in the United States Gulf of Mexico, the Mediterranean Sea, offshore West Africa, offshore Southeast Asia and offshore Australia.

Atwood's various types of drilling rigs are Ultra Deepwater Drillships, Semisubmersible Rigs, Semisubmersible Tender Assist Rigs and Jackup Drilling Rigs. The mobile offshore drilling units and related equipment comprising their offshore rig fleet operate in a single, global market for contract drilling services and are often redeployed globally due to changing demands of customers, which consist largely of major integrated oil and natural gas companies and independent oil and natural gas companies.

Company’s Current Standing:
A. The current price of ATW notes has been pounded by rapidly falling oil prices.

Reasons of Negative Pressure:
1. Oversupply of both oil and natural gas.
2. Absence of subsidiary guarantees
3. Subordination to substantial amount of priority claim debt
4. Increasing idle rig count
5. Credit downgrades by the major rating agencies
6. Forced selling
The possibility of bankruptcy
Amendments to agreements due to industry conditions

**B. Maintenance covenants on the credit agreement stand as follows:**
1. Debt/EBITDA < 4.50 (Until December 2017) | < 4 (After December 2017)
2. Senior Secured Debt/EBITDA < 3
3. Interest Expense Coverage > 1.75

As of the first quarter of 2016, Atwood Oceanic is in satisfaction of its covenants. Debt/EBITDA stands at 2.28, Senior Secured Debt/EBITDA stands at 1.53 and Interest Expense Coverage stands at 13.84.

Obligations under the revolver are secured by first preferred mortgages on eight of the drilling units, as well as liens on the equity interests of the subsidiaries that own, directly or indirectly, the aforementioned drilling units.

Covenants, particularly the leverage covenant, could be challenged in late 2017 as more rigs are either idled or roll into contracts at current market rates. However, the company has communicated that the leading banks signal flexibility regarding covenant modification.

For liquidity the company has $115.7M in cash, $199M in free cash flow, $587M available under the revolver as well as substantial alternate liquidity in that four of its drillships and one of its jackups are not pledged to bank lenders. Amendments to production agreements also allowed the company to defer $200M that would have been due in the first two quarters of this year to be due upon delivery of the rigs. This results in increased liquidity and a reduction in near term debt.

<table>
<thead>
<tr>
<th>Liquidity Ratios</th>
<th>Company</th>
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<tbody>
<tr>
<td>Operating Cash Flow/Debt</td>
<td>39%</td>
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<tr>
<td>Debt/Adjusted EBITDA</td>
<td>2.28</td>
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<tr>
<td>Senior Secured Debt/EBITDA</td>
<td>1.53</td>
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<tr>
<td>Adjusted EBITDA/Interest</td>
<td>13.84</td>
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<tr>
<td>Adjusted EBITDA – Capex / Interest</td>
<td>5.39</td>
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<tr>
<td>Quick Ratio</td>
<td>3.44</td>
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<tr>
<td>Current Ratio</td>
<td>4.46</td>
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<tr>
<td>Debt/Equity</td>
<td>0.54</td>
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<tr>
<td>Cash &amp; Cash Equivalents</td>
<td>$115.7 million</td>
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<tr>
<td>Revolver</td>
<td>$587 million</td>
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</table>
**Analysis:**

The following two scenarios assume the worst. The first being a reorganization and the second being a liquidation.

**Scenario 1:** Under a going-concern valuation utilizing comparable company EBITDA multiples, the notes would receive full recovery. The comparables chosen are Ensco (ESV), Seadrill (SDRL) and GulfMark Offshore (GLF). Even if a 50% haircut were to be applied for other reorganization-related expenses and other unforeseen factors, the notes still receive full recovery.

**Scenario 2:** Under a liquidation scenario the notes receive full recovery. Were a 20% haircut be applied due to unforeseen priority expenses, the notes would still receive a 95.29% recovery. Applying an extreme haircut of 50% the notes receive a 57.92% recovery.

Important to note for investors willing to take more risk, the equity would be worth $11.10 under the going-concern valuation with the 20% haircut applied. Even with a 40% haircut, the equity would still be worth $8.32, which is within the trading range we have seen these days.

**Conclusion:**

Seeing as how there is more than enough asset coverage for the secured debt under every scenario, it is possible that if a technical default were to occur, the creditors would be willing to renegotiate terms instead of forcing a bankruptcy. Either way, whether the company undergoes an out-of-court reorganization or a formal Chapter 11 procedure, the 2020 Atwood Oceanics 6.5% senior notes are a bargain at the moment, and even under a liquidation scenario they offer great potential returns.