ISSUE NO 3
February 2014

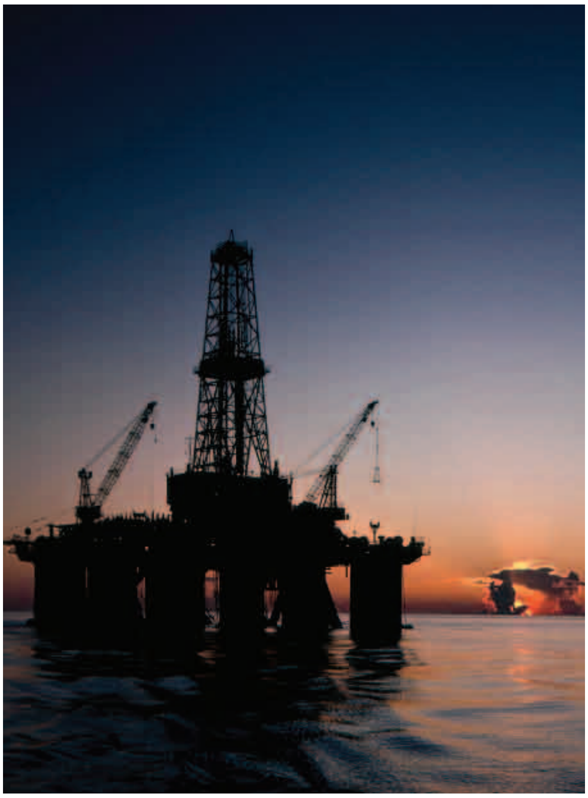
EPEUS

Industry Insights...

IN THIS ISSUE:

Welcome to the Epeus Quarterly Newsletter

As we approach the time of year when the major players in the Oil and Gas industry announce results for 2013, this issue of our quarterly insights looks back at 2013 and some of the key developments, assesses if the drilling rig market is becoming bifurcated, and looks at the importance of the application of lessons learned and transferring knowledge between projects.

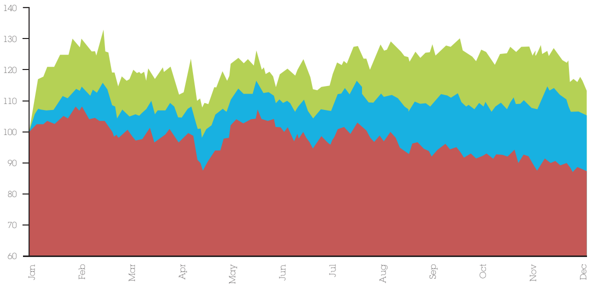


We start with a look at the financial performance of the major players in the upstream Oil and Gas Industry. The graphs below highlight that, although the major oil companies and drilling contractors have contrasting strategies and diversified portfolios of assets, their share prices are remarkably similar when compared on an indexed basis. They also highlight that as 2013 progressed both the highest and lowest share value within the Drilling Contractor group fell proportionally more than the average, and the end of year results may well see these drop further.

Perhaps the most interesting trend is that at some point in the year the share values of all but three of the Drilling Contractors were at the minimum level in the bundle on an indexed basis and these drops to the minimum usually coincided with quarterly results or announcements on major projects.

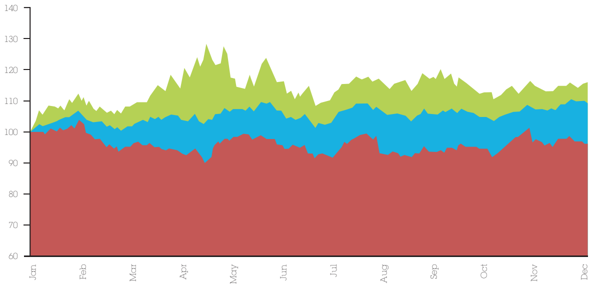
Indexed Share Prices of Major Drilling Contractors in 2013

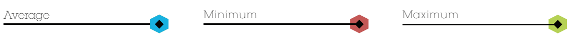
Source: Epeus Analysis, Oil Company Websites, FT.com



Indexed Share Prices of Major Oil Companies in 2013

Source: Epeus Analysis, Drilling Contractor Websites, FT.com





2013 Review

Our first Insight Newsletter of 2014 looks back initially at 2013 and the major developments in the industry we saw last year. It was a busy 12 months in a number of areas, not least in terms of new build rig construction. 69 Mobile Offshore Drilling Units were delivered, an increase over 2012 of almost 100%. In total US$23 billion of assets left shipyards around the world and more than half are already on contracts with Field Operators.

The trend of building Drillships and Jackups continues with 44 and 19 delivered respectively in the year. 2013 appears to be the first of three peak years, with 2014 and 2015 also seeing more than 60 MODUs due to be delivered.

A record number of orders were also placed in 2013, with 54 Jackups, 6 Semisubmersibles and 8 Drillships worth US$19 billion. The total CAPEX committed is down on 2012 levels of US$34 million. However, the mix of orders has changed from deepwater in 2012 (33 Drillships and 12 Semisubmersibles) to shallow water in 2013 (54 Jackups), meaning that the average CAPEX per rig is down from US$513 million in 2012 to US$281 million per rig in 2013.

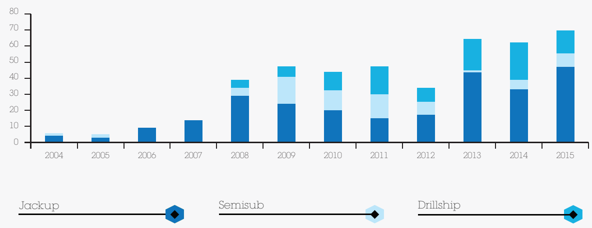
Across rig types, the average CAPEX cost per rig was down in 2013 for the first time in more than 5 years. This decrease could be explained by a number of factors, not least the 300% increase in orders of Jackups from China and Singapore and the number of Drillships that have been ordered as part of a bulk order.

Another interesting area of trends from 2013 is in the award of contracts to Drilling Rigs. In total 455 firm contracts were awarded in 2013, of which 284 were for a 2013 start date, a further 124 for a start date in 2014, and the remaining 47 to commence in 2015 or later. This differs a great deal depending on the type of Rig, with Drillships in particular

69 Mobile Offshore Drilling Units were delivered, an increase over 2012 of almost 100%

Total MODUs Delivered between 2004 and 2015 (Forecast)

Source: Epeus Analysis, RigLogix Database



Orders placed for MODUs in 2011 to 2013

		2011	2012	2013
Jackups	Orders	44	22	54
	Ave CAPEX	US$216m	US$212m	US$192m
Semisubmersibles	Orders	6	12	6
	Ave CAPEX	US$619m	US$645m	US$641m
Drillships	Orders	35	33	8
	Ave CAPEX	US$624m	US$665m	US$606m

Source: Epeus Analysis, RigLogix Database

showing more contracts awarded for 2014 and beyond (28) than for in 2013 (19). This is due in part to the number of contracts being awarded to Drillships still under construction but also the desire of Field Operators to secure rigs early for their deepwater projects.

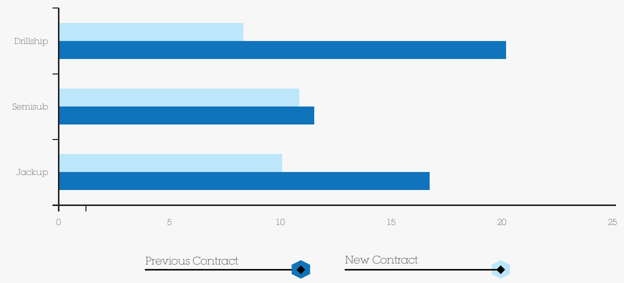
The average length of time between the award date and the start date was 11 months. For contracts commencing in 2013, however, the average length of time between the contract award and start date was just 3 months, which further reflects the short to medium term nature of the contracting market at present.

2013 saw an increase in the average length of contracts for all types of Mobile Offshore Drilling Units. Drillships in particular have seen contract lengths increase by 250%.

Finally, the drilling rig market continued to tighten in 2013 with utilisation rates remaining in the 80% range and significantly tighter for Drillships at almost 90%. Day Rates increased steadily through the year by around 10% across all types of MODU with Jackups and Drillships experiencing the biggest increases in percentage terms. Our forecasts indicate that Day Rates will continue to rise over the next 24 months across all regions in the next 3 years.

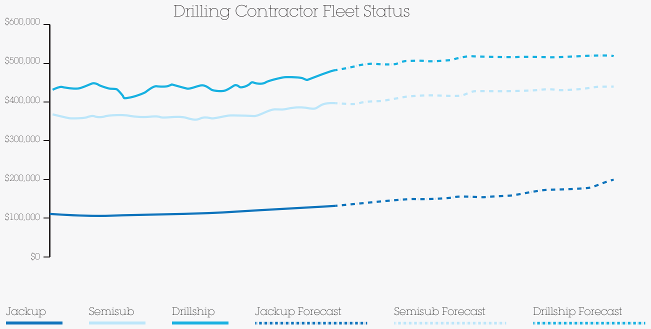
Comparison of New Contract Length to Previous Contract Length in months

Source: Epeus Analysis, RigLogix Database



Rig Day Rates between 2011 and 2016 by type

Source: Epeus Analysis, Rig Logix Database and Drilling Contractor Fleet Status



Industry Bifurcation

In 2003 more than 75% of the world's Mobile Offshore Drilling Units (MODUs) were owned and operated by just 6 organisations.

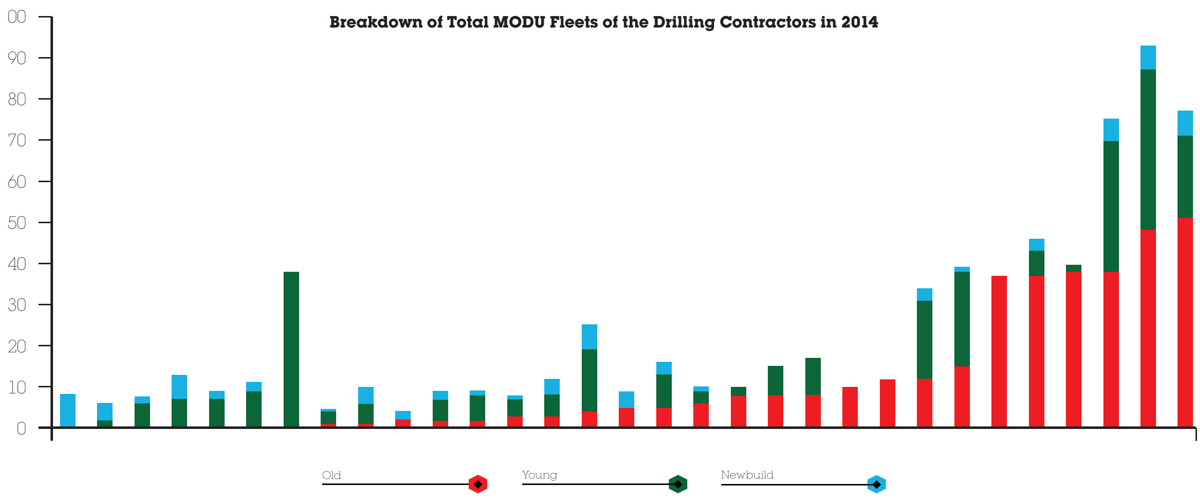
Ten years on, the major players still dominate the market with nearly two-thirds of the MODUs owned and operated by the top 6 organisations. The makeup of their fleets has changed, however, and a long period of consolidation, merger, acquisition and spin off activity has deeply affected the landscape. Previously the dominant players sought to develop large and diversified fleets of Jackups, Drillships and Semisubmersibles and combine newbuild, and young rigs with older rigs. The major players instead now target their fleets toward a specific market or requirement.

As the industry has gone through a fallow period of construction and entered another build boom, the major players have sought to offload their older rigs where they can and invest heavily in newbuild Jackups and Drillships. With Transocean offloading their older Jackup rigs into Shelf Drilling and Noble Drilling's announcement last year that they are looking at an option to spin off their older Rigs into a separate business, only Transocean, ENSCO and Diamond would be left among the dominant players with a fleet that combines old and new Rigs. The definite split between the drilling contractors with older fleets and those who have invested heavily in newer rigs leaves very little in between.

As the chart below shows only 2 or 3 drilling contractors have fleets of a reasonable size that combine older and newer rigs, it also shows the trend towards the smaller players focussing on newbuild and young rigs.

The reasons for this are obvious. Firstly the older rigs are approaching the point at which significant investment in life enhancement is required to keep them generating revenue. In addition older rigs simply don't generate the revenue that newer rigs do. For example on average an older Jackup rig will command a day rate that is only 52% of that of a newer rig, regardless of the region it is operating in or the client it is working for. Therefore a clear strategy to address this seems to be to either focus on newbuild and younger rigs or develop a fleet that has an older age profile but that is targeted on regions that clients that have a demand for this as Shelf Drilling are seeking to do with the Transocean Rigs acquired in late 2012.

Our next Insight Paper explores the bifurcation of the Drilling Rig industry in more detail and debates the future trends and implications further.



Lessons Learned

Everybody talks about it, not everyone does it. We pay more than lip service to the concept of learning lessons on the job.

Applying lessons and knowledge transfer is an important part of any project. However, too often it does not command the priority it needs, is left until the end of the project when the team has demobilised and is focussed elsewhere, or done in a way that confines it just to that project and the people involved. Although a project is a unique undertaking, projects in our industry are often repeatable and generic in nature with minor elements that make them unique. Therefore, lessons can and should be transferred between projects and even across organisations.

For a drilling contractor, completing Special Periodic Surveys (SPS) or rig modifications are repeatable projects with unique elements. For a Field Operator, planning and executing a development well or hiring a rig to execute that well is a repeatable project with unique elements.

Project phases are often referenced as a 'lifecycle'. Knowledge and lessons should be transferred from each phase of the project and from one project to another within an organisation. It's not just the lessons that are captured that are important but how that knowledge and those learnings are acted upon.

If left to the end of the project, then the capture, analysis and integration of lessons learned loses focus as the project team is often focussed on closing down administrative aspects or mobilizing onto the next project. Of course the team or the individuals take those lessons with them but the maturity of the organisation is not developing, high level lessons are not being transferred and other projects are not benefiting from them.

We recently worked with a client where we facilitated knowledge transfer not just through the move from Define and Plan into Execution within that project but onto another similar project about to enter the Define phase and into the other projects in that client that were in Select and Define.

Applied effectively, a robust approach to transferring knowledge and lessons learned between projects can make a big difference to the success of projects and the delivery of goals and business benefits. For more details on our approach to transferring knowledge and lessons learned on projects visit our website at **epeusconsulting.com/knowledge-transfer**

News in Brief

As in previous years clients have used our Advisory and project Risk Management services to feel more certain about their major projects and undertakings and in 2013 we also assisted a number of clients on their projects by providing specialist resources and teams.

In total we completed 20 assignments for 12 different clients including BP, Shell, Total, Ensco, Centrica, E.ON, Ince & Co and Clyde & Co. These assignments represent a combined total of more than $10 billion in capital expenditure for our clients.

The final quarter of the year saw some new faces join the Firm. Andrea Petrone joined in November 2013 to focus on Business Development. He has 12 years of experience in the oil and gas industry, having worked mainly for major drilling contractor, rig manufacturer and EPC companies around the world. Damien Harris also joined the Firm in November as an Associate and comes with a strong background in Project Management and Construction in the rail industry having worked for more than 13 years on major infrastructure projects.

For more details on any of the papers in this issue or for a copy of the full analysis please contact Richard Walker on:

+44 7894099604 or rwalker@epeusconsulting.com

or speak to your usual Epeus contact