

December 31<sup>st</sup>, 2016

*Island Drilling Company ASA*

# 4<sup>th</sup> Quarter Financial Report



**ISLAND DRILLING**

## **Operations**

The rig concluded operations on well 6407/10-4 Lorry March 11<sup>th</sup>. This well was the last well under the Lundin Drilling contract, and the rig was subsequently sailed to Hanøytangen where it is now placed in temporary lay-up.

The main focus in Q4/16 has been to continue planned work for the temporary lay-up including extensive maintenance activities on the machinery and equipment, including electrical systems. The objective being to make sure that all of the equipment is well preserved and ready for a quick start up should the company win contracts for additional off-shore work.

In addition there is class maintenance work in progress, and thus most of the rig is being re-classed and ready for long term assignment. As a consequence of the Lundin award (see below) work started late December 2016 in order to mobilize the rig.

## **Market update**

The negative trend observed in the rig market throughout 2015 – with rigs being committed at very low day rates – continued and was further aggravated in 2016.

However, in December 2016 the Company was awarded a new contract with Lundin Norway, for one well plus two options, with agreed commencement date 15 February – 15 March. The contract was, in general terms, based on the previous Lundin contract. The well is located in a known area, the Edvard Grieg field, and the rig started drilling on February 27<sup>th</sup>, 2017.

To date, the number of rigs being laid-up and/or scrapped is still not sufficient to stabilize the utilization and thus the market rates. This has had a significant negative impact on the day rates, and very few new fixtures are reported in the market.

## **Financial update**

As stated in the Q3/16 Financial Report, the company is in breach of financial covenants. The breaches have not been cured, and no waivers have been received – to the contrary the Company has received “Reservation of rights” – letters from both DnB as agent for the senior loans and Nordic Trustee as trustee for the Bond loan.

The Company paid interest and instalments on the senior loans provided by Eksportkreditt Norge ASA, DnB and Sparebanken Søre Sunnmøre Q1/16, but informed the bondholders through a notice to Nordic Trustee early April that interest on the Bond Loans falling due in April 2016 would not be paid. Consequently, the Company is in default in relation to the Bond Loan. The interest on the senior loans was not paid in September 2016.

Due to the significant impairment of the rig Q4/15, the Working Capital (WC) as well as the Equity (and Value Adjusted Equity (VAE)) was negative at year end (requirements are  $WC > 0$ ,  $VAE > 30\%$ ). This situation continues. As at year end 2016 a brokers valuation confirming the book value of the rig has been received. Un updated assessment of the parameters in DCF valuation model has also been carried through – and the conditions set forth in the DCF model is considered still valid.

However, as the cash position as of 31.12.16 was USD 20,2 million, down from USD 26,1 million 30.09.16, and the discussions with the Company's secured creditors are continuing, IDC is still insufficient, but not ill-liquid and thus the condition for continued operations is still considered valid. As stated in previous quarterly reports and the 2015 Annual Report, the Board of Directors have appointed Clackson's Platou Securities as financial advisors to the company, and initiated discussions with the banks and financial institutions involved in the financing of the rig. Formal discussions with the bond holders will commence shortly.

Operating revenues in Q4/16 amounted to USD 0 million. (Q4/15 USD 43,0 million), while EBITDA in Q4/16 amounted to minus USD 2,9 million (Q4/15 USD 27,7 million). Net Financials amounted to USD 7,8 million. (Q4/15 USD 8,3 million) and the Pre-tax profit Q4/16 thus amounted to minus USD 15,6 million (Q4/15 minus USD 358,8 following an impairment of the rig of USD 370,1 million)

Total fixed assets as of 31 December 2016 amount to USD 239,1 million. Current assets total USD 26,8 million, of which bank deposits amount to USD 20,2 million. As a consequence of the continuing breach of certain financial covenants, the long term senior loans as well as the bond loan and the long term loan from related parties are still classified as short term. Current liabilities as of 31 December 2016 thus amount to USD 425,2 million, including the long-term senior- and bond debt as well as the related parties' loan.

The cash flow from operating activities for the fourth quarter 2016 was negative with USD 5,5 million (Q4/15 USD 5,3 million), while the cash flow from investments was 0,4 million. Cash flow from financing activities Q4/16 was zero as well. This resulted in a net cash flow of minus USD 5,9 million in Q4/16 (Q4/15 USD 5,0 million), decreasing the cash and cash equivalents from USD 26,1 million at 30 September 2016 to USD 20,2 million at 31 December 2016. (USD 21,8 million at 31 December 2015).

The Q4/16 accounts are not audited.

### **Going Concern**

'Island Innovator' was still in "warm stacked" mode at Hanøytangen at the end of Q4/16. However, following an award of a 1 well contract (plus options) with Lundin Norway AS the rig left Hanøytangen on February 24<sup>th</sup>, and commenced drilling on February 27<sup>th</sup>, 2017. Market opportunities are still followed closely to obtain further work. A restructuring of the Company's balance sheet is still deemed necessary to enable the Company to come through the current market challenges, and the Company has initiated discussions with its finance providers in this respect. While these discussions are ongoing, the Company has decided to halt all payments of interest and amortization to all of its finance providers.

The "Going Concern"-assumption is thus based on the Company working with its finance providers to reach a sustainable solution for the Company. Consequently, the Q4/16 accounts reflect a situation where the Company is not liquidated and no forced sale of the rig is carried through.

While the Company remains confident that such sustainable solution will be reached with the relevant stakeholders, there can be no assurance or guarantee that such final solution will be reached.

During the discussions with the finance providers, the Company will continue to operate normally in all other respect. The liquidity of the Company remains stable, but strained, for the period to come in anticipation of a sustainable solution with the finance providers.

Agreement as to a refinancing and restructuring of the Company to provide such a sustainable solution has in principle been reached with the senior secured lenders. This agreement is, however, subject to certain conditions to be fulfilled, amongst others that agreement is also reached with the bond holders in the Second Lien Callable Bond Issue 2013/2018 in the amount of USD 140 million (ISIN NO00167418.7). Thus, March 15<sup>th</sup>, 2017 the Company called for an Extraordinary General Meeting and a Bondholders Meeting to approve the proposed refinancing and restructuring. The outcome of of these meetings is not know as of today. For further details of the proposed solution please see the “Summons to Bondholders’ Meeting” posted on the Company’s web-site.



### Profit & Loss Account

Amounts in USD 1,000s

|                               | YTD Q4 2016    | Q4 2016        | Q3 2016        | Q2 2016        | Q1 2016       | 2015            |
|-------------------------------|----------------|----------------|----------------|----------------|---------------|-----------------|
| Revenues                      | 33 689         | 0              | 3              | 9              | 33 677        | 169 342         |
| Operating expenses            | 20 484         | 2 943          | 2 238          | 2 480          | 12 824        | 64 031          |
| <b>EBITDA</b>                 | <b>13 205</b>  | <b>-2 943</b>  | <b>-2 234</b>  | <b>-2 471</b>  | <b>20 853</b> | <b>105 310</b>  |
| Depreciation and amortisation | 19 498         | 4 877          | 4 875          | 4 874          | 4 871         | 32 492          |
| Impairment                    | 0              | 0              | 0              | 0              | 0             | 370 103         |
| <b>EBIT</b>                   | <b>-6 292</b>  | <b>-7 820</b>  | <b>-7 109</b>  | <b>-7 344</b>  | <b>15 982</b> | <b>-297 284</b> |
| Net financial items           | -27 328        | -7 828         | -6 741         | -7 547         | -5 212        | -45 245         |
| <b>Net pre-tax profit</b>     | <b>-33 621</b> | <b>-15 649</b> | <b>-13 850</b> | <b>-14 891</b> | <b>10 770</b> | <b>-342 529</b> |
| Taxes                         | 0              | 0              | 0              | 0              | 0             | 0               |
| <b>Net result after taxes</b> | <b>-33 621</b> | <b>-15 649</b> | <b>-13 850</b> | <b>-14 891</b> | <b>10 770</b> | <b>-342 529</b> |
| <i>EBITDA%</i>                | 39 %           | N/A            | N/A            | N/A            | 62 %          | 62 %            |

### Balance sheet

Amounts in USD 1,000s

|                                     | 31-12-16        | 30-09-16        | 30-06-16        | 31-03-16        | 31-12-15        |
|-------------------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| <b>Assets</b>                       |                 |                 |                 |                 |                 |
| <i>Fixed assets</i>                 |                 |                 |                 |                 |                 |
| Total intangible assets             | 0               | 0               | 0               | 0               | 0               |
| Rig, machinery and equipment        | 239 064         | 243 567         | 248 394         | 253 139         | 258 010         |
| <b>Total Fixed Assets</b>           | <b>239 064</b>  | <b>243 567</b>  | <b>248 394</b>  | <b>253 139</b>  | <b>258 010</b>  |
| <i>Current Assets</i>               |                 |                 |                 |                 |                 |
| Total receivables                   | 6 610           | 6 672           | 6 730           | 25 635          | 36 818          |
| Cash and cash equivalents           | 20 212          | 26 109          | 28 789          | 20 062          | 21 751          |
| <b>Total Current Assets</b>         | <b>26 822</b>   | <b>32 781</b>   | <b>35 519</b>   | <b>45 697</b>   | <b>58 569</b>   |
| <b>Total Assets</b>                 | <b>265 886</b>  | <b>276 348</b>  | <b>283 913</b>  | <b>298 836</b>  | <b>316 579</b>  |
| <b>Equity and Liabilities</b>       |                 |                 |                 |                 |                 |
| Paid-in equity                      | 137 751         | 137 751         | 137 751         | 137 751         | 137 751         |
| Retained earnings                   | -297 032        | -281 383        | -267 533        | -252 642        | -263 411        |
| <b>Total Equity</b>                 | <b>-159 281</b> | <b>-143 632</b> | <b>-129 782</b> | <b>-114 891</b> | <b>-125 660</b> |
| Bonds                               | 0               | 0               | 0               | 0               | 0               |
| Long term loans                     | 0               | 0               | 0               | 0               | 0               |
| Current liabilities                 | 425 167         | 419 980         | 413 695         | 413 727         | 442 239         |
| <b>Total Liabilities</b>            | <b>425 167</b>  | <b>419 980</b>  | <b>413 695</b>  | <b>413 727</b>  | <b>442 239</b>  |
| <b>Total Equity and Liabilities</b> | <b>265 886</b>  | <b>276 348</b>  | <b>283 913</b>  | <b>298 836</b>  | <b>316 579</b>  |

### Cash flow statement

Amounts in USD 1,000s

|   | YTD Q4 2016 | Q4 2016 | Q3 2016 | Q2 2016 | Q1 2016 | 2015    |
|---|-------------|---------|---------|---------|---------|---------|
| Cash flow from operating activities     | 19 601      | -5 522  | -2 632  | 8 856   | 18 900  | 48 968  |
| Cash flow from investment activities    | -552        | -375    | -48     | -128    | -1      | -5 590  |
| Cash flow from financing activities     | -20 588     | 0       | 0       | 0       | -20 588 | -50 452 |
| Net cash flow in the period             | -1 539      | -5 897  | -2 680  | 8 728   | -1 689  | -7 074  |
| Cash and cash equiv. at start of period | 21 751      | 26 109  | 28 789  | 20 062  | 21 751  | 28 826  |
| Cash and cash equiv. at end of period   | 20 212      | 20 212  | 26 109  | 28 789  | 20 062  | 21 751  |

## Contact us

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