ARCM

ARCM's response to Premier Oil's proposed scheme of arrangement – ARCM opposes scheme

7 January 2020 - ARCM notes Premier Oil's announcement regarding the proposal for a scheme of arrangement to extend the debt maturity and approve certain acquisitions. As the Company's largest creditor, holding more than 15% across the Company's debt instruments with blocking positions in two of them, ARCM will take all steps to oppose the Company's proposal and will vigorously contest any attempt to implement such proposal via a scheme of arrangement.

ARCM is deeply concerned about Premier Oil's intention to pursue acquisitions as stated in its announcement, as they will only serve to increase risk for stakeholders. Premier Oil's balance sheet is already highly levered, and the Company is facing an impending May 2021 maturity of $2.55 billion of net debt as of the 2019 mid-year financials (comprising of $2.2 billion of "accounting net debt" and $371 million of letters of credit). Through its announcement this morning, whereby the Company is seeking an extension through a court supervised Scheme of Arrangement, it appears to be acknowledging that it cannot repay the outstanding debt in accordance with its terms.

ARCM believes that management's immediate priority should be on transactions that facilitate a significant deleveraging of the Company's highly levered balance sheet, so that it may meet the debt maturities that its creditors have already extended once in the 2017 restructuring - as opposed to pursuing acquisitions that expose the Company's balance sheet to significant incremental risks.

As such, ARCM will take all steps to oppose the Company's proposal and will vigorously contest any attempt to implement such proposal via a scheme of arrangement.

We are particularly concerned about the following developments:

1) Cost and quantum of debt and decommissioning liabilities

- Similar to the 2017 restructuring, the Company is once again offering a significant coupon increase of 1.6% to extend its debt maturities. This would increase the cost of debt to almost 9%. On top of this coupon increase, the Company is also going to have to pay amendment and prepayment fees of 1%.
- Even after the Zama sale, the Company will be left with around $2 billion of net debt ("accounting net debt" plus letters of credit) and this high cost debt will continue to pose risks to the balance sheet.
- The creditors have already granted a four-year debt maturity extension and the Company has been operating with a complex capital structure involving RCF, term loans, USPPs and retail notes with restrictive covenants. In our view, the prudent route forward is to address the fundamental problem of excessive leverage, simplify the balance sheet and eliminate the downside exposure to a weak commodity price environment.
- The Company already has $1.2 billion of decommissioning liabilities (as outlined on page 11 of its mid-year result announcement). Adding $600 million of decommissioning liabilities, to a total of $1.8 billion, by acquiring older assets further increases the risk profile of the Company. Buying short-term cash flows in exchange for long-term obligations could be very negative for all stakeholders in a weak commodity price environment.

2) Increasing the Company's exposure to the UK gas market and transitioning Premier to becoming a gas producer

- Based on our analysis, we believe that these acquisitions would likely transition Premier to becoming primarily a gas producer by 2021-2022 with significant exposure to the UK gas market.
- We are concerned about the supply/demand dynamics of the UK gas market and the potential impact on the Company's cash flow generation capacity. The UK and European gas markets are likely entering a multi-year period of excess supply due to strong regional gas production

and U.S. LNG and Russian imports. We note that the UK gas forward pricing for Calendar 2020 has declined more than -30% since the end of Q3 2019 to less than 35p/therm.

3) Inability to access the RBL lending market and exit of long-term creditors

- Since 2017, we have observed many of the Company's long-term creditors exit their positions, including large creditors over the last two weeks. With the Company's continued high-risk strategy, it continues to lose its core long-term lenders.
- In our view, one of the main reasons why the Company must delever now is its inability to access the traditional RBL market in any meaningful scale given its declining oil production profile and existing decommissioning liabilities of $1.2 billion.
- Going forward, the RBL capacity will be highly sensitive to U.K. gas prices. We are concerned that if the banks lower their baseline RBL estimates for U.K. gas prices, the Company will be constrained in its future ability to raise sustainable financing.

ARCM has articulated these concerns to the Company and has put forward an alternative proposal which would significantly reduce leverage and provide a stable balance sheet, from which the Company could then prudently pursue further acquisitions.

ARCM, and its financial advisers Moelis & Company, remain willing to openly discuss the issues summarized above, in addition to sensible alternative deleveraging options, with the Company, the Creditors (including those creditors who have purportedly already agreed to vote in favour of the Company's proposal) and other stakeholders.

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