CASH FLOW MODELLING CASE ASSIGNMENT

I. Situation

May 2006: Ocean Rig is trying to acquire Eastern Drilling at a price tag of NOK 2.7b (NOK 135/share, 20m shares) or USD415m (exchange rate USD/NOK 6.5). The offer from Ocean Rig is subject to at least 50% acceptance (if not obtained, the offer will fall away). If it obtains the 50% threshold, Ocean Rig is obliged to provide a mandatory offer for 100% of the shares. Hence, Ocean Rig has to formulate a finance plan predicated on it becoming the 100% owner of Eastern Drilling.

Ocean Rig has recently issued bonds in the amount of USD250m and has asked if we are able to step up with the remaining USD165m.

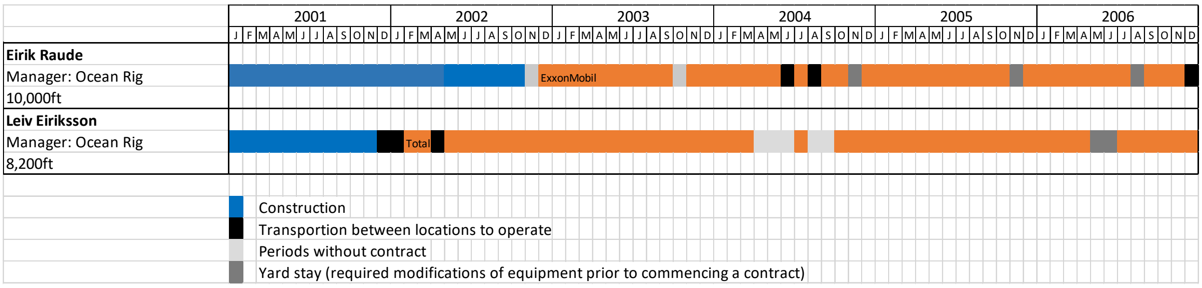
We are already the Lead Arranger of a USD430m loan to Ocean Rig, which was concluded in June 2005 and syndicated to a number of other banks. Our share of the loan after syndication is USD130m.

We are also the Lead Arranger of a USD300m loan to Eastern Drilling, of which we have a USD100m share of after syndication.

II. Ocean Rig details

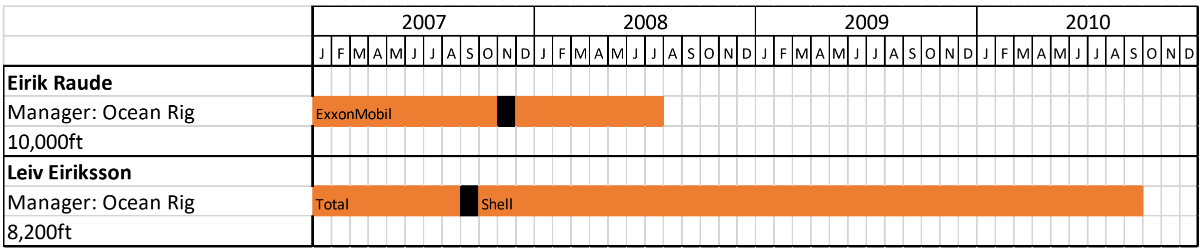
Ocean Rig has two modern rigs in operation, one on contract for Total in West Africa ("Leiv Eiriksson") and one on contract with ExxonMobil in the North Sea and Canada ("Eirik Raude").

The contract situation from 2001 to end 2006 is as follows:



From the delivery of the rigs from the construction yard in the beginning and end 2002 respectively, the rigs have operated on multiple contracts (orange blocks). The blue blocks indicate construction, the black blocks indicate transportation between locations to operate, the light grey blocks indicate periods without contracts and the dark grey blocks indicate a yard stay (required modifications of the equipment prior to commencing on a contract).

Going forward, the fixed contract situation is as follows:



The charter rates on the current contracts are USD405,000/day for Eirik Raude and USD380,000/day for Leiv Eiriksson. When Leiv Eiriksson goes on contract with Shell from 3Q2007, it will receive a rate of USD465,000/day.

Ocean Rig's loans have the following terms and conditions:

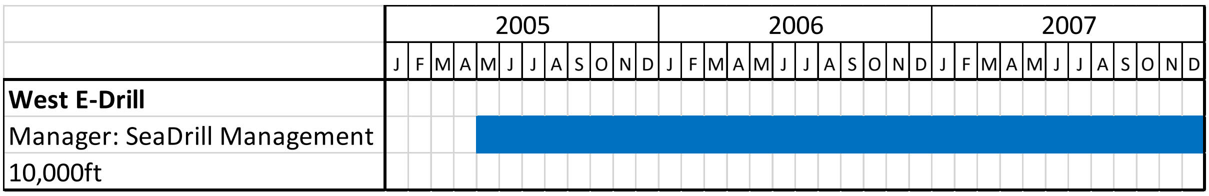
Facility	Loan Disbursement Date	Final Repayment Date (Maturity)	Repayment Profile	Interest Rate (Libor = 5%)
USD430m Bank Loan	15 June 2005	15 June 2010	Over 10 years	L+1.25% p.a.
USD150m Bond Loan	15 June 2005	15 June 2010	100% at Maturity	L+3.5% p.a.
USD250m Bond Loan	15 May 2005	15 June 2012	100% at Maturity	L+3.5% p.a.

The cost of operating each of the rigs would be around USD125,000/day/rig. Admin costs would be approximately USD5m/year in total.

The book value of each rig is USD550m, which corresponds to the rig broker's market value assessment. The company holds USD25m as free and available cash in addition to the funds raised in connection with the latest USD250m bond issue, which corresponds to the minimum cash requirement set out in the Loan Agreement with us as lenders.

III. <u>Eastern Drilling details</u>

Eastern Drilling has ordered one rig on speculation, which is currently under construction in Korea at Samsung Heavy Industries. The agreed construction price with the yard is USD465m, but all-in construction cost is assumed to be USD550m (Total Capex). The rig is financed with USD250m equity and USD300m debt.



There is currently no contract secured after the delivery at year end 2007, but Eastern Drilling is very optimistic that it will be secured prior to delivery given the strong market conditions.

Eastern Drilling has an option for a second rig at the same terms but has yet to decide if it would exercise this.

Eastern Drilling's loan has the following terms and conditions:

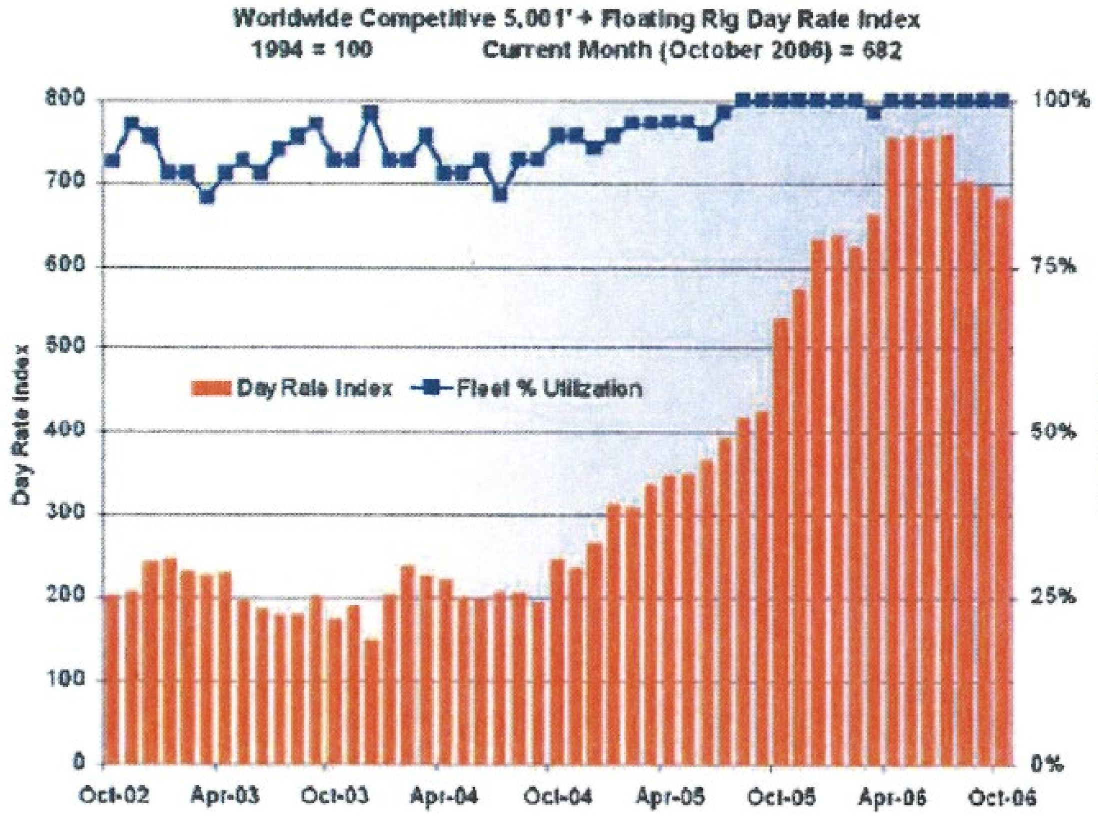
Facility	Loan Disbursement Date	Final Repayment Date (Maturity)	Repayment Profile	Interest Rate (Libor = 5%)
USD300m Bank Loan	50%: 31 Dec 2006 50%: 31 Dec 2007	15 June 2013	Over 15 years	L+1.5% p.a.

The cost of operating the rig would be around USD125,000/day. Admin costs would be approximately USD5m/year. The company is required to hold a minimum cash of USD15m from delivery of the rig (included in the Total Capex requirement).

IV. **Market Outlook**

After 5 years of low drilling activity, the market conditions have improved significantly from beginning of 2005. The market rate for a new, modern rig would today be between USD450,000 - 500,000/day for a fixed period between 3 to 5 years (up from USD150,000 – 200,000/day at much shorter contract tenors).

The figure below illustrates the strong improvement that has been experienced in the drilling rig market:



In addition to the strong increase in day rates for modern rigs, it is worth noticing that the fleet utilisation has been fairly high also in the period of much weaker day rates (i.e. the modern rigs will have work but must take a beating on the rates while older rigs will suffer both in terms of utilisation and rates).

Since the oil demand is high due to the growth rate in China and India and OPEC is producing at maximum capacity, the oil price is high. This in turn results in increased activity to find and produce more oil offshore among the oil companies, which leads to increased demand for drilling rigs. The general perception is that this situation will last for a number of years going forward but this is uncertain. It is likely that Ocean Rig will get 3 to 5-year contracts at expiry of their existing contracts and Eastern Drilling a 3 to 5-year contract from delivery at today's market rates, but the market conditions thereafter would be more uncertain from a lender's perspective.

V. **Assignment**

You are asked to make a cash flow model for the next 5 years on a quarterly basis for the purpose of assessing the potential to accommodate Ocean Rig's request to finance the acquisition of Eastern Drilling (100%) with additional bank debt of USD165m. You will join a weekly transaction assessment meeting for senior personnel on Monday next week to present your analysis.

Since you are presenting your cash flow to a larger audience, the model should be easy to follow (tip: structure and layout). The model should be flexible to allow the toggling of assumptions in order to run sensitivity analysis during the meeting if requested by any of the persons present.

The most important purpose of the model is of course to assess whether or not the overall debt can be serviced cash flow wise, but since the company would like to be allowed to pay 50% of the company's net profit as dividends, you would need to produce a Profit & Loss statement. As there would also be a minimum 30% equity ratio requirement, you would also have to produce a Balance Sheet statement for the forecast period.

The forecasted scenario should be presented in one graph which you believe illustrates the case in a simple and easily understandable manner so that a fruitful discussion, and potentially a decision, can take place.

You may assume that the two companies will be consolidated at the time of completing Ocean Rig's acquisition of Eastern Drilling (by mid 2006). Otherwise, make assumptions based on the information contained herein and such other that you feel is relevant (if lacking or unclear).

Good luck!