Category Strategy Template

A Worldwide Insight into Offshore Jack-up Rigs

June 2017
Offshore jack-up rigs are an essential feature of the oil and gas industry. Typically used in water depths between 25m to 150m, jack-up rigs are floated onto the drill site before retractable legs are lowered to the sea floor, raising the hull out of the water. Once in position jack-up rigs are capable of drilling to depths of up to 9000+m.

**LIFE CYCLE USAGE**

**Exploration**
- Are hydrocarbons present?
- Drilling 1 or 2 Wildcat Wells
- Low volume drilling
- Gather Information

**Appraisal**
- How much hydrocarbon is present?
- Understand reservoir characteristics
- Low volume drilling

**Development**
- Drill wells to produce hydrocarbons
- Higher volume drilling
- Access production zone of well
- Drill injection wells

**Production**
- Maintain production levels
- Higher volume drilling
- In-field drilling (more injectors and producers)
- Workover wells

**JACK-UP TYPES**

- **Standard**
  - Typically older in age
  - Water depth less than 110m
  - Low automation

- **Premium**
  - Water depths greater than 110m
  - Greater automation
  - Higher hook load capacity

- **High Specification**
  - Often designed for Harsh Environment
  - High level of automation
  - Water depths of up to 120+m
  - High hook load capacity

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MARKET SUMMARY
The offshore jack-up rig market is highly cyclical. Utilization and rates are quick to react to oil price and over the past 2-3 years prices have been driven to record lows. With oil prices stabilizing around US$50 per barrel the short to mid term is likely to remain challenging for rig owners as investment levels remain restrained. Looking further ahead any growth in investment will likely see higher specification jack-ups contracted first leaving a large surplus of standard specifications rigs (unlikely to work again) and a continuation of pressure on day rates.

DEMAND remains low
- Oil prices have moved between 12 year lows of $26 to mid $50’s during 2016 and early 2017. This has left many projects uneconomical.
- Both national and international oil companies have drastically cut capital spending programs and continue to maintain such levels in light of the low & volatile price environment.
- During the oil recovery jack-ups are likely to respond first given the lower risk and investment in shallow waters.
- Tendering is highly competitive on pricing and commercial and legal terms.
- No increase in demand expected without a robust rise in oil prices.

SUPPLY remains high
- Supply hugely outweighs demand
- Since the downturn rig owners have retired 30+ jack-ups, 90+ jack-ups older than 30 years are cold-stacked and approximately 60+ of a similar age and specification have contracts expiring in 2017. Many of these will likely be retired given the cost to maintain and recertify.
- Approximately 70 new build jack-ups are planned for delivery in 2017 and a further 30-40 planned in future years. Most remain un-contracted and will likely face further cancellations
- Newer rigs most likely to be the first to see demand during recovery
## The Market Dynamic cont.

**OFFSHORE JACK-UP RIGS**

### ACTIVITY HEAT MAP

<table>
<thead>
<tr>
<th>Location</th>
<th>2012 Rig Count</th>
<th>Current Rig Count</th>
<th>Change (+/-)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mexico</td>
<td>36</td>
<td>24</td>
<td>-33%</td>
</tr>
<tr>
<td>GoM</td>
<td>36</td>
<td>6</td>
<td>-83%</td>
</tr>
<tr>
<td>W. Africa</td>
<td>25</td>
<td>8</td>
<td>-68%</td>
</tr>
<tr>
<td>North Sea</td>
<td>42</td>
<td>28</td>
<td>-33%</td>
</tr>
<tr>
<td>Middle East</td>
<td>110</td>
<td>110</td>
<td>0%</td>
</tr>
<tr>
<td>India</td>
<td>29</td>
<td>36</td>
<td>+24%</td>
</tr>
<tr>
<td>S.E. Asia</td>
<td>58</td>
<td>26</td>
<td>-55%</td>
</tr>
</tbody>
</table>
PORTER’S FIVE FORCES

THREAT OF NEW ENTRY
- High capital requirements
- Saturated market currently

INDUSTRY RIVALRY
- Low market growth
- High fixed cost
- Low switching costs
- Low rig utilization

THREAT OF SUBSTITUTION
- No other economical means to drill wells
- Alternative workover options

SUPPLIER BARGAINING POWER
- Low differentiation
- Multiple suppliers
- Low demand
- Low switching cost

BUYER BARGAINING POWER
- Few buyers and low demand
- Market intelligence on rig rates widespread
- High total cost

SUMMARY OF BUYER POWER

LOW

STRONG
Buyer Bargaining Power
Supplier Bargaining Power
Industry Rivalry

WEAK

BALANCED
Threat of Substitution
Threat of New Entry
Portfolio Placement
OFFSHORE JACK-UP RIGS

KRALJIC MATRIX

Supplier Risk is LOW

<table>
<thead>
<tr>
<th>Importance &amp; Profit Impact</th>
<th>Leverage</th>
<th>Strategic</th>
<th>Routine</th>
<th>Bottleneck</th>
</tr>
</thead>
<tbody>
<tr>
<td>Supplier Risk is LOW</td>
<td>Number of Suppliers</td>
<td>♻️</td>
<td>Multiple suppliers available in the market</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Availability</td>
<td>♻️</td>
<td>Rig utilization low and many alternatives available</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Market Demand</td>
<td>♻️</td>
<td>Capital investment low due to oil price. Low demand for rigs</td>
<td></td>
</tr>
</tbody>
</table>

Importance and Profit Impact is HIGH

<table>
<thead>
<tr>
<th>Importance</th>
<th>Procurement Cost</th>
<th>Critical resource to E&amp;P companies and essential to revenue generation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Importance</td>
<td>Procurement Cost</td>
<td>Typically a high percentage of CAPEX and OPEX budgets</td>
</tr>
</tbody>
</table>
Cost and Price Trends
 OFFSHORE JACK-UP RIGS

TYPICAL HIGH-SPEC BREAKEVEN
High-Spec Breakeven
US$ 80-100k/day

- Overhead: 6%
- Interest: 16%
- Depreciation: 20%
- Operating Costs (crewing, tools, equipment, maintenance, radios, etc): 58%

CURRENT PRICE TREND

<table>
<thead>
<tr>
<th>Rates</th>
<th>High Specification</th>
<th>Premium</th>
<th>Standard</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low Rate (US$/day)</td>
<td>95,000</td>
<td>75,000</td>
<td>40,000</td>
</tr>
<tr>
<td>High Rate (US$/day)</td>
<td>225,000</td>
<td>185,000</td>
<td>95,000</td>
</tr>
<tr>
<td>Target Rate (US$/day)</td>
<td>95,000 to 135,000</td>
<td>75,000 to 100,000</td>
<td>40,000 to 65,000</td>
</tr>
</tbody>
</table>

Price Pressure: 🔻 🔻 🔻
## Market Summary
OFFSHORE JACK-UP RIGS

### Overview

<table>
<thead>
<tr>
<th>Category</th>
<th>Supplier</th>
<th>Buyer</th>
<th>Category Positioning</th>
</tr>
</thead>
<tbody>
<tr>
<td>Offshore Jack-Up Rig</td>
<td><img src="#" alt="Blue Circle" /></td>
<td><img src="#" alt="White Circle" /></td>
<td><img src="#" alt="Yellow Square" /></td>
</tr>
<tr>
<td></td>
<td><img src="#" alt="Arrow Down" /></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Market supply</td>
<td>Market Demand</td>
<td>Power</td>
</tr>
<tr>
<td></td>
<td>Price Pressure</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Category**
- Offshore Jack-Up Rig

**Supplier**
- Market supply: ![Blue Circle](#)
- Price Pressure: ![Arrow Down](#)

**Buyer**
- Market Demand: ![White Circle](#)

**Category Positioning**
- Power: ![Yellow Square](#)
<table>
<thead>
<tr>
<th>Company</th>
<th>Experience</th>
<th>Presence</th>
<th>Fleet Size</th>
<th>Fleet Capability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Maersk Drilling</td>
<td>40+ years</td>
<td>Regional</td>
<td>15</td>
<td>Mixed</td>
</tr>
<tr>
<td>Noble Corporation</td>
<td>30+ years</td>
<td>Global</td>
<td>14</td>
<td>Mixed</td>
</tr>
<tr>
<td>Shelf Drilling</td>
<td>5+ years</td>
<td>Global</td>
<td>38</td>
<td>Standard to Premium</td>
</tr>
<tr>
<td>Rowan</td>
<td>90+ years</td>
<td>Global</td>
<td>25</td>
<td>Mixed</td>
</tr>
<tr>
<td>ENSCO</td>
<td>40+ years</td>
<td>Global</td>
<td>34</td>
<td>Mixed</td>
</tr>
<tr>
<td>SeaDrill</td>
<td>10+ years</td>
<td>Global</td>
<td>32</td>
<td>Mixed</td>
</tr>
<tr>
<td>COSL</td>
<td>10+ years</td>
<td>Regional</td>
<td>36</td>
<td>Mixed</td>
</tr>
<tr>
<td>Borr Drilling</td>
<td>2+ years</td>
<td>Global</td>
<td>17</td>
<td>Mixed</td>
</tr>
<tr>
<td>Paragon Offshore</td>
<td>2+ years</td>
<td>Global</td>
<td>34</td>
<td>Mixed</td>
</tr>
<tr>
<td>NDC</td>
<td>40+ years</td>
<td>National</td>
<td>21</td>
<td>Mixed</td>
</tr>
</tbody>
</table>
# Total Cost of Ownership
## OFFSHORE JACK-UP RIGS

## TOTAL COST OF OWNERSHIP COMPONENTS

<table>
<thead>
<tr>
<th>Parameter</th>
<th>Service Cost</th>
<th>Switching Cost</th>
<th>Performance Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost Visibility</td>
<td>High</td>
<td>Medium</td>
<td>Low</td>
</tr>
<tr>
<td>Description</td>
<td>The rates and charges agreed in a contract for the performance of the service</td>
<td>The non-productive time and cost related to bring a new rig into operation</td>
<td>The cost impact of lower or higher performance than expected</td>
</tr>
<tr>
<td>Cost Driver</td>
<td>Mobilization Fee, Rates, Operating, Standby, Moving, Force Majeure, Re-drill, Poor Performance, Zero, Downhole Equipment loss and repair, Demobilization Fee</td>
<td>Standby/Operating charges during rig swap and/or rig up</td>
<td>NPT, Learning Curve</td>
</tr>
<tr>
<td>Commercial Impact</td>
<td>High</td>
<td>Low</td>
<td>Medium</td>
</tr>
</tbody>
</table>
## Contracting Strategy

### OFFSHORE JACK-UP RIGS

### CONTRACTING OPTIONS

<table>
<thead>
<tr>
<th>Parameter</th>
<th>Day Rate</th>
<th>Footage Rate</th>
<th>Lump Sum</th>
</tr>
</thead>
<tbody>
<tr>
<td>Typical Application</td>
<td>Full lifecycle</td>
<td>Development &amp; Production</td>
<td>Exploration &amp; Appraisal</td>
</tr>
<tr>
<td>Contractor Risk</td>
<td>Low</td>
<td>Medium</td>
<td>High</td>
</tr>
<tr>
<td>Price Competitiveness</td>
<td>High</td>
<td>Medium</td>
<td>Low</td>
</tr>
<tr>
<td>Commercial Alignment/Contractor Incentive</td>
<td>Low</td>
<td>High</td>
<td>Low</td>
</tr>
<tr>
<td>Contractor Preference</td>
<td>1</td>
<td>2</td>
<td>3</td>
</tr>
</tbody>
</table>
In the current market environment buyers must balance their competitive strength with building relationships that can foster higher performance. Offshore jack-up rigs are a major value contributor to oil & gas companies and small increases in performance can have a significant impact on oil revenues and well costs. Consequently it is important to use the buyer’s competitive power to reduce costs and also to maximize value through improved performance.

STRATEGIC OBJECTIVES

1. Maximize cost reductions
2. Maximize value add through continuous improvement and innovation
3. Maintain a degree of flexibility

PREQUALIFICATION CRITERIA

<table>
<thead>
<tr>
<th>Quality</th>
<th>HES</th>
<th>Financial</th>
<th>Technical Capacity</th>
<th>Experience</th>
</tr>
</thead>
<tbody>
<tr>
<td>✗</td>
<td>✗</td>
<td>✗</td>
<td>✗</td>
<td>✗</td>
</tr>
</tbody>
</table>

MARKET APPROACH

- Open Tender
- Selective Tender
- Negotiated Tender
- Serial Tender

NEGOTIATION STRATEGY

STYLE: Firm but fair. Exploit competitive environment

NEGOTIATION TARGETS:

1. Price
2. Rig specification
3. Performance Commitments
4. Early Termination

STRENGTHS

Market forces
Term duration

WEAKNESS

Strain on relationship
Performance Management
OFFSHORE JACKUP RIGS

Performance Objectives

- Quality Operation
- Safe Operation
- Timely Operation
- Cost Effective Operation

KPI's

- Experience of crew: years, certification etc.
- Crew Continuity: % of returning crew
- Breakdown Hours Consumed: per month
- Planned vs. Actual PM's: % completed

- HES Incidents: frequency and severity.
- Leading Indicators: tool box talks, safety scorecards, management presence etc.

- Non Productive Time: hrs/day
- Drilled ft/hr: drilling efficiency (per well type)

- Contribution to Well Cost: %/well
- Additional Cost due to Performance: $ per well

Contractual Value Drivers

- Crewing
- Rig Maintenance
- Continuous Improvement
- Operation Management
For more information get in touch at:

Email: info@scmdaleel.com
Phone: +974 6620 7593