

Transocean Ltd. (RIG)

\$6.16 (As of 01/13/20)

Price Target (6-12 Months): **\$7.50**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 10/19/17)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:D

Value: D

Growth: F

Momentum: A

Summary

Being the largest provider offshore contract drilling services, Transocean's recent \$352.9M addition to backlog offers cash flow visibility. Further, with U.S. offshore industry signaling signs of revival, Transocean is poised to capitalize on trend effectively, given its technologically advanced and versatile drilling fleet. As it is, the buyout of Songa Offshore and Ocean Rig has boosted its fleet size and future prospects. However, Ocean Rig acquisition has also impacted the financials of RIG, leading to stock issuance, debt addition along with cash reduction. Moreover, Transocean is bearing the brunt of operational inefficiency which is likely to continue in the upcoming quarters as well, limiting the earnings of the firm. Hence, investors are advised to wait for a better chance.

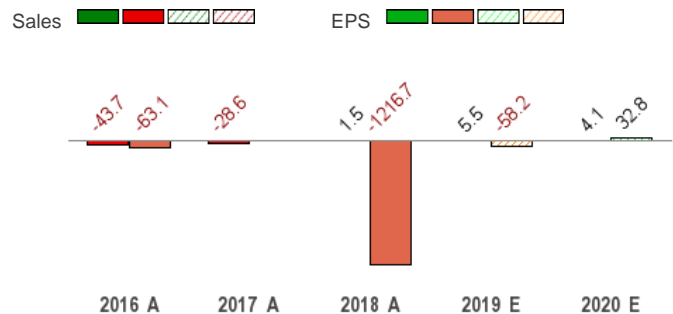
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$9.79 - \$3.76
20 Day Average Volume (sh)	14,288,294
Market Cap	\$3.8 B
YTD Price Change	-9.3%
Beta	2.00
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Oil and Gas - Drilling
Zacks Industry Rank	Bottom 33% (169 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	5.0%
Last Sales Surprise	0.5%
EPS F1 Est- 4 week change	0.8%
Expected Report Date	02/17/2020
Earnings ESP	7.7%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020	814 E	804 E	818 E	837 E	3,315 E
2019	754 A	758 A	784 A	821 E	3,183 E
2018	664 A	790 A	816 A	748 A	3,018 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	-\$0.20 E	-\$0.23 E	-\$0.21 E	-\$0.20 E	-\$0.84 E
2019	-\$0.30 A	-\$0.34 A	-\$0.38 A	-\$0.31 E	-\$1.25 E
2018	-\$0.48 A	-\$0.04 A	\$0.06 A	-\$0.34 A	-\$0.79 A

*Quarterly figures may not add up to annual.

P/E TTM	NA
P/E F1	NA
PEG F1	NA
P/S TTM	1.3

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 01/13/2020. The reports text is as of 01/14/2020.

Overview

Switzerland-based Transocean, Inc. is the world's largest offshore drilling contractor and leading provider of drilling management services. The company provide rigs on a contractual basis to explore and develop oil and gas. Transocean offers offshore drilling rigs, equipment, services and manpower (with particular emphasis on ultra-deepwater and harsh environment drilling services) to exploration and production companies worldwide.

Transocean's fleet is considered one of the most modern and versatile in the world due to its emphasis on technically demanding segments of the offshore drilling business. Transocean's fleet can be broadly divided into three distinct groups based on drilling capabilities: ultra-deepwater floaters, harsh environment floaters and midwater floaters, which accounted for 59%, 32% and 9%, respectively, of its total revenue for 2018.

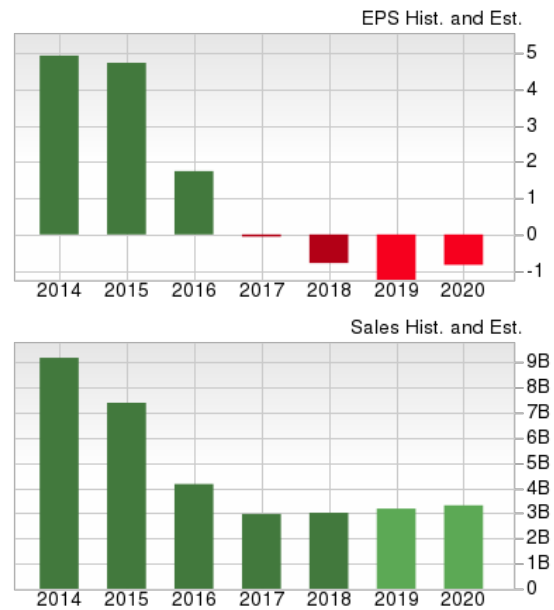
Transocean's 31 ultra-deepwater floaters are capable of drilling in water depths of 4,500 feet and more. The company's 14 harsh environment floaters are capable of drilling in harsh environment at water depths between 1,500 and 10,000 feet with greater displacement. The four mid-water floaters operate at water depth of less than 4,500 feet.

Moreover, four ultra-deepwater drillships and one harsh environment semisubmersible are currently under construction. Transocean's fleet is considered one of the most modern and versatile in the world due to its emphasis on technically demanding segments of the offshore drilling business.

Recent Acquisitions: Songa & Ocean Rig

In early 2018, Transocean acquired Norway-based drilling contractor Songa Offshore for \$3.4 billion. As a result of the transaction, the company got seven mobile offshore drilling units, including five harsh environment floaters and two midwater floaters.

In December 2018, Transocean snapped up smaller rival Ocean Rig UDW for \$2.7-billion. The deal further strengthened its portfolio, in turn expanding fleet size and quality. Notably, the acquisition gave Transocean 11 mobile offshore drilling units, including nine ultra-deepwater floaters and two harsh environment floaters.



Reasons To Buy:

- ▲ Transocean's recent addition of \$352.9 million to its backlog since its last fleet status update in October 2019, which showed a backlog of \$10.8 billion reflects steady demand from the customers and offers earnings and cash flow visibility.
- ▲ Transocean completed two big buyouts in 2018 which has bolstered the offshore game of the company to a considerable extent. The acquisition of Songa and Ocean Rig has not just boosted the Transocean's fleet size, it also likely to provide the company with significant commercial and operational synergies along with boosting long-term growth prospects.
- ▲ With U.S. offshore industry witnessing early signs of revival, as evidenced by the increasing project sanctions, Transocean is poised to capitalize on trend effectively, given its technologically advanced and versatile drilling fleet. With more than 100 offshore projects green-lighted in 2019, demand for rigs is likely to improve, benefiting the offshore drilling giant. As it is, the company has been taking necessary steps to enhance its fleet with modern and competitive rigs, while scrapping off old and incompetent drillships, which is expected to make its operations more technically effective and efficient.

Transocean's robust backlog of \$10.8 billion offers earnings and cash flow visibility.

Reasons To Sell:

- ▼ Over the past few quarters, the company is bogged down by operational inefficiencies which are hurting its margins. Further, the firm forecasts a sequential increase in its operation and maintenance expenses in the third quarter. It also expects its capital outlay to increase in the upcoming quarter, which may limit its earnings.
- ▼ While Transocean's acquisition of Ocean Rig in a stock-cash deal worth \$2.7 billion bodes well for long term growth, it has adversely affected the financial position of the company. The transaction has led to stock issuance, debt addition along with cash reduction. Notably, the company's long term debt increased to \$9.6 billion in 2018 from \$7.1 billion in 2017.
- ▼ Notably, Transocean has sold couple of Ocean Rig's drillships including Paros and Eirik Raude owing to high reactivation costs. Also many of the Ocean Rig's drillships are currently stacked, involving stacking costs. Moreover, charges related to the reactivation of such drillships along with the technical challenges to make them operational after such long breaks remain a concern. Rig reactivation and impairment charges amid retirement of drillships are likely to weigh down on the company's margins in the coming periods as well.

Transocean is bogged down by high costs which is limiting its earnings.

Last Earnings Report

Transocean posts narrower than expected loss in Q3

Transocean Ltd. posted third-quarter 2019 adjusted loss of 38 cents a share, narrower than the Zacks Consensus Estimated loss of 40 cents. Strong revenues from the Ultra-Deepwater and Harsh Environment floaters together with higher dayrates led to this outperformance. However, the bottom line came in against the year-ago earnings of 6 cents due to higher shipyard costs and lower fleet utilization.

Meanwhile, the offshore drilling powerhouse generated total revenues of \$784 million, beating the Zacks Consensus Estimate of \$780 million. But the top line declined 3.9% from the prior-year figure of \$816 million.

Quarter Ending **09/2019**

Report Date	Oct 28, 2019
Sales Surprise	0.46%
EPS Surprise	5.00%
Quarterly EPS	-0.38
Annual EPS (TTM)	-1.36

Segmental Revenue Break-Up

Transocean's Ultra-deepwater floaters contributed about 63.01% to total contract drilling revenues while Harsh Environment floaters and Midwater floaters accounted for the remainder. In the quarter under review, revenues from Ultra-Deepwater and Harsh Environment floaters totalled \$494 million and \$281 million, respectively.

Revenue efficiency was 97%, marginally lower than the second-quarter level. The figure reflected an increase from the year-ago number of 95%.

Dayrates and Utilization

On an encouraging note, average dayrate in the quarter under review rose to \$314,500 from the year-ago level of \$295,000 owing to an uptick in activity in the Asia Pacific. The company witnessed year-over-year higher average revenue per day from midwater floaters. Overall fleet utilization was 58% during the quarter, down from the prior-year utilization rate of 65%.

Backlog

Transocean's backlog, which was recorded at \$10.8 billion as of October, reflects a decline of \$700 million from the year-ago figure. In the third quarter, the company added approximately \$130 million to its backlog.

Costs, Capex & Balance Sheet

Transocean's costs and expenses rose 17.71% year over year to \$804 million. Operating and maintenance costs also increased to \$547 million from \$447 million a year ago. Transocean spent \$121 million on capital expenditure in the third quarter. Cash provided by operating activities totalled \$91 million, inducing a negative free cash flow of \$30 million. The company had cash and cash equivalents of \$1.9 billion on Sep 30, 2019. Long-term debt was \$9 billion with a debt-to-capitalization ratio of 43.08% as of the same date.

Guidance

For the fourth quarter, the company expects its adjusted contract drilling revenues to be roughly \$825 million. Meanwhile, capital expenses for maintenance are anticipated to be \$106 million.

Full-year operating and maintenance costs are predicted to be around \$2.1 billion. Further, the company projects its G&A expense in the range of \$175-\$185 million.

Recent News

Transocean Adds \$352.9M to Backlog Since Last Fleet Status

On Jan 8 Transocean Limited issued a new fleet status report, lending an insight into its portfolio of drillships, recent contracts and backlog.

Since its last fleet status update in October 2019, which showed a backlog of \$10.8 billion, the company has been successful in securing \$352.9 million worth additional contracts, courtesy of new deals and extensions of its existing projects.

Following the fall in oil prices during mid-2014, the offshore drilling market had been hit hard as operators ramp down offshore exploration and development activity. Now, with crude price being back above \$60 per barrel, the offshore rig market is witnessing an upswing.

Cashing in on this optimism, Switzerland-based Transocean has been able to snap up a number of contracts for its ultra-deepwater and harsh environment drilling services of late. Apart from contributing to the company's top line, this upside will considerably improve dayrates and provide material benefit to the company's cash flows.

Digging Into Details of the Newly-Clinched Contracts

While the company won a few deals since the last fleet report in October 2019, the \$91-million worth one-year drilling contract off the coast of Trinidad and Tobago for its semisubmersible Development Driller III served as the fundamental component to boost its backlog. This new pact with leverage to command an estimated day rate of \$250,000 is scheduled to start in the second quarter of 2020. Further, it is expected to help the company progress in terms of both backlog and cash flow.

Moving on, the Leiv Eiriksson rig, which operates for ConocoPhillips, gained a 125-day contract offshore Norway and is expected to be effective August 2020. Drillship Discoverer Inspiration, working for Talos Energy, also clinched a 120-day contract in the US Gulf of Mexico with a dayrate of \$210,000. Notably, Discoverer Inspiration is set to conclude a contract with Chevron Corporation in the US Gulf during the first quarter of this year.

Further, the company was awarded new agreements for its drillships including Dhirubhai Deepwater KG2 and Deepwater Asgard.

The slew of contracts to the company's credit reflects steady demand from customers, underscoring its earnings and cash flow visibility. Markedly, Transocean, sitting atop a record backlog, is the largest provider of offshore contract drilling services.

With U.S. offshore industry witnessing early signs of revival, evidenced by the spurt in project sanctions, Transocean is poised to capitalize on this trend effectively, riding on its technologically-advanced and versatile drilling fleet.

With numerous offshore projects expected to be green-lighted in 2020, demand for rigs is likely to be spurred benefiting this offshore drilling giant. The company has been taking necessary steps to enhance its fleet with modern and competitive rigs while scrapping the old and incompetent drillships to make its operations more technically sound.

Valuation

Transocean shares are down 26.4% over the trailing 12-month period. Over the past year, the Zacks sub-industry and sector are down 20.9% and 0.8%, respectively.

The S&P 500 index is up 26.8% in the past year.

The stock is currently trading at 10.7X trailing 12-month EV/EBITDA, which compares to 8.68X for the Zacks sub-industry, 5.06X for the Zacks sector and 12.12X for the S&P 500 index.

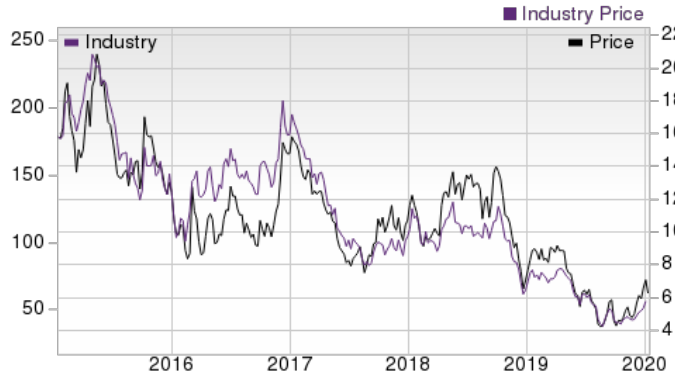
Over the past five years, the stock has traded as high as 10.91X and as low as 2.8X, with a 5-year median of 5.38X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$7.5 price target reflects 1.38X F12M sales.

The table below shows summary valuation data for RIG

Valuation Multiples - RIG					
		Stock	Sub-Industry	Sector	S&P 500
EV/EBITDA TTM	Current	10.7	8.68	5.06	12.12
	5-Year High	10.91	13.01	10.22	12.86
	5-Year Low	2.8	4.07	4.56	8.48
	5-Year Median	5.38	8.1	6.49	10.67
P/S F12M	Current	1.15	1.05	0.89	3.5
	5-Year High	2.28	2.48	1.44	3.5
	5-Year Low	0.69	0.79	0.67	2.54
	5-Year Median	1.21	1.48	0.99	3
P/B TTM	Current	0.32	0.46	1.23	4.46
	5-Year High	0.58	0.91	1.59	4.47
	5-Year Low	0.19	0.32	1.02	2.85
	5-Year Median	0.32	0.59	1.31	3.61

	0.104	0.02	0.03	1.01	0.01
As of 01/13/2020					

Industry Analysis Zacks Industry Rank: Bottom 33% (169 out of 254)



Top Peers

Diamond Offshore Drilling, Inc. (DO)	Neutral
Helmerich & Payne, Inc. (HP)	Neutral
Nabors Industries Ltd. (NBR)	Neutral
Noble Corporation (NE)	Neutral
Precision Drilling Corporation (PDS)	Neutral
Pioneer Energy Services Corp. (PESX)	Neutral
Patterson-UTI Energy, Inc. (PTEN)	Neutral
KONINKLIJKE VPK (VOPKY)	Neutral

Industry Comparison Industry: Oil And Gas - Drilling				Industry Peers		
	RIG Neutral	X Industry	S&P 500	DO Neutral	HP Neutral	NE Neutral
VGM Score	D	-	-	D	C	F
Market Cap	3.82 B	389.66 M	24.31 B	911.54 M	5.02 B	286.58 M
# of Analysts	5	5.5	13	5	10	4
Dividend Yield	0.00%	0.00%	1.76%	0.00%	6.14%	0.00%
Value Score	D	-	-	B	D	D
Cash/Price	0.64	0.36	0.04	0.23	0.08	0.47
EV/EBITDA	-46.23	4.13	14.12	11.72	9.46	-8.23
PEG Ratio	NA	8.80	2.05	NA	8.80	NA
Price/Book (P/B)	0.32	0.36	3.34	0.28	1.26	0.08
Price/Cash Flow (P/CF)	6.78	3.43	13.66	5.26	6.67	8.43
P/E (F1)	NA	18.03	18.82	NA	141.87	NA
Price/Sales (P/S)	1.25	0.47	2.64	0.97	1.79	0.25
Earnings Yield	-13.46%	-13.88%	5.29%	-34.44%	0.71%	-127.83%
Debt/Equity	0.76	0.76	0.72	0.60	0.12	0.96
Cash Flow (\$/share)	0.92	0.62	6.94	1.26	6.94	0.14
Growth Score	F	-	-	F	A	F
Hist. EPS Growth (3-5 yrs)	-50.60%	-34.19%	10.56%	-37.63%	-27.87%	NA
Proj. EPS Growth (F1/F0)	32.91%	13.18%	7.49%	20.50%	-81.37%	11.51%
Curr. Cash Flow Growth	-30.57%	-20.32%	14.83%	-62.45%	25.65%	-87.45%
Hist. Cash Flow Growth (3-5 yrs)	-26.35%	-16.19%	9.00%	-30.31%	-8.86%	-54.00%
Current Ratio	2.53	1.85	1.23	1.84	2.72	0.58
Debt/Capital	43.09%	43.64%	42.99%	37.41%	10.67%	49.06%
Net Margin	-47.50%	-19.76%	11.08%	-38.61%	-1.20%	-60.35%
Return on Equity	-6.26%	-7.51%	17.16%	-10.44%	4.68%	-8.76%
Sales/Assets	0.12	0.40	0.55	0.16	0.47	0.13
Proj. Sales Growth (F1/F0)	4.14%	-0.73%	4.23%	3.64%	-12.27%	1.27%
Momentum Score	A	-	-	D	F	F
Daily Price Chg	0.16%	-0.62%	0.73%	-0.15%	-0.58%	-0.86%
1 Week Price Chg	-11.51%	-5.89%	0.39%	-13.11%	1.46%	-15.33%
4 Week Price Chg	3.48%	3.30%	1.84%	8.88%	9.05%	22.38%
12 Week Price Chg	36.24%	9.66%	6.48%	20.80%	20.35%	-12.88%
52 Week Price Chg	-25.89%	-27.57%	23.15%	-42.44%	-13.11%	-65.77%
20 Day Average Volume	14,288,294	273,903	1,578,594	2,946,396	1,358,095	4,527,772
(F1) EPS Est 1 week change	0.68%	0.00%	0.00%	-0.37%	-4.40%	-0.69%
(F1) EPS Est 4 week change	0.84%	0.00%	0.00%	-0.37%	-12.60%	-0.69%
(F1) EPS Est 12 week change	3.08%	-19.61%	-0.48%	-15.24%	-52.50%	-19.61%
(Q1) EPS Est Mthly Chg	-1.25%	-0.42%	0.00%	0.00%	-16.67%	-0.83%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	D
Growth Score	F
Momentum Score	A
VGM Score	D

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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