FITCH REVISES INDIKA'S OUTLOOK TO NEGATIVE; AFFIRMS AT 'B+'

Fitch Ratings-Singapore-22 July 2014: Fitch Ratings has revised Indonesia-based Indika Energy Tbk's (Indika) Outlook to Negative from Stable. At the same time the agency has affirmed Indika's Long-Term Foreign and Local Currency Issuer Default Ratings (IDR) at 'B+'. Indika's senior unsecured notes have also been affirmed at 'B+' with a Recovery Rating of 'RR4'.

The outlook revision reflects weakened interest coverage at Indika due to the currently weak coal industry dynamics. The affirmation of the ratings, however, factors in Indika's adequate liquidity arising from its cash reserves and the absence of major debt maturities till 2018, as well as Fitch's expectation that some, albeit marginal, recovery in coal prices will happen in the next 12-18 months. The rating headroom is however limited. Given varying ownership and control of its many operating entities, Fitch has focused on credit metrics calculated based on the EBITDA of Indika and its fully owned subsidiaries, including dividends from its other operating entities (holding company EBITDA).

KEY RATING DRIVERS

Weak Interest Coverage: Indika's interest coverage - the ratio of the holding company EBITDA to the interest expenses of Indika and its fully owned subsidiaries - fell to about 2x in 2013 from 3.2x in 2012. This was due to a near halving of dividend inflows, especially from its 46% owned coal asset, PT Kideco Jaya Agung (Kideco), which paid Indika USD108m of dividends, or nearly 70% of Indika's total cash inflows, in 2013. Fitch expects holding company interest coverage to weaken further in 2014 and 2015 because of a further decline in dividends from Kideco based on realised coal prices in 2013 and so far in 2014. Dividends from Kideco will decline to USD88m in 2014 and Fitch expects this to further decline to below USD50m in 2015. In addition to dividends from Kideco, we expect about USD20m of dividends per annum from Indika's other associate companies and subsidiaries.

Given lower dividends and capex on a new office building and investments in a new coal asset PT Multi Tambangjaya Utama, Fitch expects the holding company to generate negative free-cash flows in 2014. Indika's listed investments, contract mining company PT Petrosea Tbk (Petrosea) and barging company MBSS, are self-sufficient and require no financial assistance from Indika. Fitch, however, expects an improvement in holding company interest coverage from 2016, due largely to the expected improvement in coal prices, albeit only marginally, and an increase in the volume of coal produced at Kideco.

Weak Coal Prices: The agency expects benchmark Newcastle coal prices (currently at about USD70/MT) to gradually increase. This is due to the agency's belief that a sizable proportion of coal supplied to the sea-borne market is unprofitable at current prices. We also note that most coal miners have been selectively mining in the more cost-effective areas of the mines, which generally are at the expense of long-term reserves and cannot be sustained. However, any improvement in prices will occur slowly because the market will remain oversupplied, especially with weak demand from China.

Adequate Liquidity: Indika's next bond maturity of USD300m is due only in 2018. The company had about USD300m of cash and equivalents (excluding those of the non-fully owned subsidiaries), which should comfortably cover the expected negative free cash flows at the holding company level in 2014 and 2015. Indika also has another USD500m of debt maturity due in 2023. Of this USD500m, USD115m has been on-lent to its 70%-owned subsidiary Petrosea.

RATING SENSITIVITIES

Negative: Future developments that may, individually or collectively, lead to negative rating action include:

-A material weakening of liquidity at the holding company level as measured by a decrease in the freely available cash balances at the holding company and its fully owned subsidiaries to below USD150m

- A failure to improve the holding company EBITDA interest coverage to above 1.5x on a forecast basis

- weaker-than-expected coal prices

Positive: Future developments that may, individually or collectively, lead to positive rating action include:

- Fitch may revise Indika's rating outlook to Stable, while affirming its IDR at 'B+' if the company can improve its holding company interest coverage to over 1.5x and maintain strong liquidity

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Applicable criteria, "Corporate Rating Methodology: Including Short-Term Ratings and Parent and Subsidiary Linkage", dated 28 May 2014 are available at www.fitchratings.com

Applicable Criteria and Related Research:
Corporate Rating Methodology - Including Short-Term Ratings and Parent and Subsidiary Linkage
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=749393