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Rating Action: Moody's changes rating outlook for Indika to negative; B1 ratings affirmed

Global Credit Research - 22 May 2014

Singapore, May 22, 2014 -- Moody's Investors Service has changed the rating outlook for Indika Energy Tbk (P.T.) (Indika) to negative from stable.

Concurrently, Moody's affirmed Indika's B1 corporate family rating (CFR) and the B1 ratings on the USD300 million notes due 2018 and USD500 million notes due 2023, issued by Indo Energy Finance B.V. and Indo Energy Finance II B.V., respectively. The entities are wholly owned subsidiaries of by Indika. The notes are unconditionally guaranteed by Indika.

RATINGS RATIONALE

"The change in outlook to negative reflects the increasing pressure on Indika's operations as a result of the persistent weakness in thermal coal prices coupled with Moody's expectation that coal prices will remain under pressure during the next 12 months," says Brian Grieser, a Moody's Vice President and Senior Analyst.

"We estimate that lower coal prices will drive Indika's financial leverage towards 5.0x over the next twelve months from 4.2x in March 2014," adds Grieser.

The Newcastle thermal coal price index, a benchmark for Asia, has fallen to \$73 per ton in 2014 from an average of \$84 per ton in 2013. We expect Newcastle coal prices to average between \$75-80 per ton this year, down from our original expectation of \$80-85 per ton back in December 2013.

Indika generates a substantial portion of its cash flow through dividends from its 46% stake in PT Kideco Jaya Agung (Kideco, unrated), Indonesia's third largest coal producer. Kideco has seen the average selling price (ASP) of its coal drop to \$55 per ton in the first quarter of 2014 from \$60 per ton in the prior year. We expect the ASP to continue to fall towards \$50 in 2014 resulting in a meaningful reduction in earnings at Kideco this year.

"Accordingly, we estimate Indika's share of dividends from its key cash-generating investment Kideco, to be paid in 2015, could fall 35-45% from the \$88 million to be paid in 2014 and compared to the \$154 million in 2013," says Grieser.

Further, we expect a reduction in overburden removal volumes at Indika's contract mining business, Petrosea, and increasing pricing pressure at both Petrosea and its coal transport operations, MBSS, to weigh on profitability and cash flow, further pressuring Indika's consolidated operations. While these businesses offer some diversification to Indika's operations, they are still tied to the coal sector which means they will remain under pressure as long as coal prices stay at depressed levels.

Despite these challenges, we have affirmed Indika's B1 ratings since it has been successful in maintaining its high cash balances (\$391 million at March 2014), extending its debt maturity profile and lowering its financing costs in 2013. We expect the company to remain committed to its prudent financial policies which will help it weather what we expect will be a prolonged cyclical trough for the Indonesian coal sector. We expect Indika to generate minimal free cash flows from its diversified business portfolio in 2014-2015 and to carefully manage growth capital spending to maintain its sizeable liquidity cushion.

A ratings downgrade could occur if 1) Coal prices fail to stabilize and thus fall short of our \$75-80 per ton target in the next twelve months ; 2) Tripatra, Petrosea, and MBSS fail to win tenders and contracts to maintain existing earnings levels in 2015; 3) the relationship between Samtan and Indika deteriorates; 4) Indika undertakes any large debt-funded acquisitions; or 5) its liquidity profile deteriorates such that cash balances fall below \$200 million.

Specific indicators Moody's would look for include total debt/EBITDA (including dividends from associates) reach 5.0x and its net debt/EBITDA reaches 4.0x and EBIT/interest falls below 2.0x.

Upward ratings pressure is limited in the near-to medium-term given the negative outlook and our view that deleveraging will be challenging in the current environment for coal prices. However, the rating outlook could

stabilize if Indika improves its financial leverage, such that its total debt/EBITDA (including dividends from associates) falls below 4.0x and EBIT/interest improves to over 2.5x. Any positive action would require Indika to maintain the current strength of its liquidity profile in concert with an improvement in realizable coal prices for Kideco.

Indika, Indo Energy Finance B.V. and Indo Energy Finance II B.V.'s ratings were assigned by evaluating factors that Moody's considers relevant to the credit profile of the issuer, such as the company's (i) business risk and competitive position compared with others within the industry; (ii) capital structure and financial risk; (iii) projected performance over the near to intermediate term; and (iv) management's track record and tolerance for risk. Moody's compared these attributes against other issuers both within and outside Indika, Indo Energy Finance B.V. and Indo Energy Finance II B.V.'s core industry and believes Indika, Indo Energy Finance B.V. and Indo Energy Finance II B.V.'s ratings are comparable to those of other issuers with similar credit risk.

Indika is an Indonesian integrated energy group listed on Indonesia's Stock Exchange. Through a number of acquisitions, Indika has positioned itself as an integrated energy group with a focus on energy resources (primarily through 46% interest in Kedeco), energy services (primarily through wholly owned Tripatra and 69.8% stake in Petrosea) and energy infrastructure (primarily through its 51% stake in MBSS).

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Brian J. Grieser
Vice President - Senior Analyst
Corporate Finance Group
Moody's Investors Service Singapore Pte. Ltd.
50 Raffles Place #23-06
Singapore Land Tower
Singapore 48623
Singapore
JOURNALISTS: (852) 3758 -1350
SUBSCRIBERS: (65) 6398-8308

Philipp L. Lotter
MD - Corporate Finance
Corporate Finance Group
JOURNALISTS: (852) 3758 -1350
SUBSCRIBERS: (65) 6398-8308

Releasing Office:
Moody's Investors Service Singapore Pte. Ltd.
50 Raffles Place #23-06
Singapore Land Tower
Singapore 48623
Singapore
JOURNALISTS: (852) 3758 -1350
SUBSCRIBERS: (65) 6398-8308



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