MOODY'S
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Rating Action: Moody's upgrades Indika to Ba3; outlook stable

Global Credit Research - 12 Dec 2017

Singapore, December 12, 2017 -- Moody's Investors Service has upgraded the corporate family rating (CFR) of Indika Energy Tbk (P.T.) (Indika) to Ba3 from B2 following the completion of its acquisition of an additional 45% stake in Kideco Jaya Agung (P.T.), Indonesia's third largest coal producer.

At the same time, Moody's has also upgraded the ratings on the $500 million backed senior secured notes due 2023 issued by Indo Energy Finance II B.V., the $265 million backed senior secured notes due 2022 issued by Indika Energy Capital II Pte. Ltd, and the $575 million backed senior secured notes due 2024 issued by Indika Energy Capital III Pte. Ltd. to Ba3 from B2. All notes are unconditionally and irrevocably guaranteed by Indika and rank pari passu.

The outlook on all ratings is stable.

The rating action concludes Moody's review for upgrade initiated on 25 September 2017.

RATINGS RATIONALE

On 8 December 2017, Indika announced it had completed the Kideco acquisition after receiving all requisite approvals, increasing its shareholding in the coal producer to 91% from 46%. It had also successfully raised $575 million of new notes at 5.875% due November 2024 to fund the acquisition.

The total purchase consideration, comprising an upfront payment of $517.5 million and contingent liability of $160 million, and the coupon on the new $575 million notes are in line with Moody's expectations.

"The upgrade of Indika's ratings to Ba3 reflects the improvement in the company's operating profile as it now controls the steady cash flow generation at Kideco, Indonesia's third largest coal mining asset. It also incorporates the company's stronger credit metrics in 2018-19 with consolidated leverage of around 3.4x-3.6x," says Rachel Chua, a Moody's Assistant Vice President and Analyst.

Kideco has a long reserve life of over 13 years, based on its projected 2017 production volume of 32 million tons. In the first six months of 2017, the mine generated $200 million of operating cash flow. On a pro-forma basis, Moody's expects Kideco will account for over 70% of Indika's EBITDA.

Overall, Indika's Ba3 ratings reflect its long dated debt maturity profile with no material maturity until 2022 and its good liquidity position. The ratings also take into consideration Indika's ongoing commitment to conservative financial policies which balances its risk profile during periods of volatility in thermal coal prices.

"However, there remains a high degree of event risk, given the expiry of Kideco's coal contract of work (CCoW) in 2023. Negotiations for the extension of the CCoW can only commence in 2021 and while it is our current view that an extension on similar terms will be forthcoming, we remain cognizant of the regulatory risk and the impact on Indika's credit profile and ratings should that renewal not materialize in a timely fashion," adds Chua, who is also Moody's lead analyst for Indika.

The ratings outlook is stable, reflecting Moody's expectations that operations at Kideco will continue without disruptions through the management and ownership transition and that Indika will continue to execute its business strategy as planned over the next 12-18 months.

A further near-term upgrade of the ratings is unlikely. Nevertheless, upward momentum in the ratings could develop over time if Indika is successful in extending the Kideco CCoW beyond its 2024 bond maturity with no material changes to existing terms while demonstrating a sustained improvement in its financial profile. Specific indicators we would consider include adjusted debt/ EBITDA below 2.5x - 3.0x and adjusted EBIT/ interest above 3.0x - 3.5x for an extended period.

Downward ratings pressure could arise if (1) Indika's cash flow generation is weakened by a sustained decline in coal prices; (2) it fails to extend the Kideco CCoW at substantially similar terms; or (3) it engages in aggressive shareholder distributions or capital investments demonstrating a departure from management's track record of liquidity preservation.Specific indicators we would consider include adjusted debt/ EBITDA above 3.5x - 4.0x or adjusted EBIT/ Interest below 2.0x for an extended period.

The principal methodology used in these ratings was the Global Mining Industry published in August 2014. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

Indika Energy Tbk (P.T.) is an Indonesian integrated energy group listed on Indonesia's Stock Exchange. As of 8 December 2017, its principal investment is a 91% stake in Kideco Jaya Agung (P.T.), Indonesia's third-largest domestic coal producer and one of the world's lowest-cost producers and exporters of coal.

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