



# **BORR DRILLING**

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GRANULAR CAPITAL LTD.  
London

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## Prologue

We are long-term investors. Our objective is to compound capital over long periods of time at mid double digit rates or above. To do this, we try to find companies trading at reasonable valuations that will grow free cash flow per share at mid double digit rates.

This prologue precedes a write up of our investment in Borr Drilling, an oil services company. Given it is somewhat unfashionable for long-term investors to invest in capital intensive businesses in cyclical industries (outside of tech at least!), we felt we should write a short foreword to explain ourselves.

We will get into the specifics of the Borr investment case in the memo that follows, but we wanted to set out a few high level points here about the capital cycle to explain why we believe the Company has the potential to develop into a predictable long-duration cash machine.

Given our desire to own businesses compounding at high rates, it will come as no surprise that much of our portfolio is invested in capital-lite businesses. As the saying goes, capital is the enemy of high returns on capital.

In Borr we believe we have found one of the rare situations in which a company can earn high returns on its tangible assets for a long period of time. There are numerous historical precedents – including railroads, cell towers and cable – of businesses in capital intensive industries that were extraordinary long-term investments following a period of boom and bust. The duration of the opportunity to generate extraordinary profitability following a bust depends on the ease with which new capital can come in and bring returns back down.

The exciting aspect of the Borr investment case is that it is difficult to imagine an industry less likely to attract new capital. Starting with the big picture, given ESG dynamics, pools of capital throughout the financial value chain – private equity players, their limited partners, and the banks that finance them – have committed not to invest in oil and gas.

ESG commitments can obviously be worked around, but to do so the investment case has to be incredibly simple to overcome the friction that has built up in the system. Borr owns and operates the industry's youngest fleet of high-specification jackup rigs, an overlooked niche within the cyclical and possibly structurally declining offshore drilling industry. Making things even more complicated, it is commonly accepted that oil demand and production is in structural decline. Given that jackups are supposed to operate for around 30-40 years, this expected decline in oil demand is difficult to square with an investment committee approving orders for new rigs today.

Further raising the barriers to new capital flowing into the jackup market, the industry has suffered from years of awful returns. Anyone involved in the construction of a jackup rig since the GFC would have lost their shirt. Today, rigs change hands at less than 50% of replacement cost; a rig ordered today would be worth less than 50c on the dollar the moment it was tugged out of its dry dock.

Jackups are expensive assets, so new orders today have to come from institutional capital providers. New rigs would cost \$300 million and take 2-3 years to build if the supply chain was working properly, which it isn't. Today, construction yards require up to 50% cash downpayments which is a far cry from the old days when they would take orders with only a 5% deposit, allowing cowboy operators to place highly speculative orders to play the cycle.

It will take a seismic change in perception before institutional capital is attracted back to the jackup market. Until there is a dramatic appreciation in day rates, it is hard to see anything that could change the situation in a way that will incentivise the construction of new rigs. Demand for jackups has grown at approximately 2% per year since 2017, which has been enough to tighten the market, but hardly the sort of exciting growth rates that generate the enthusiasm required to mobilise large amounts of capital to order new rigs.

Moreover, if contracted at current market day rates, a new rig would earn unlevered returns on capital in the high single digits, which is below the cost of capital of most listed companies in the sector today. Given that oil demand is

expected to start declining in a decade, it would be reasonable for potential investors to require starting returns on capital of at least 20% per year to be able to pencil out a doubling of their money before demand starts to decline.

Even if capital is eventually tempted back into the space, it will be difficult to prevent the jackup fleet from declining over the next decade. We include more detail in the memo, but the key point here is that during the construction boom that lasted from 2006 to 2016, the world built on average 22 jackups per year. Half of these rigs were built in Singapore which has pivoted away from jackups and towards growth industries like wind turbines and LNG tankers. Singapore's apparent permanent shift away from jackups leaves theoretical global capacity of approximately 10 rigs per year, though all of this is currently tied-up with other non-jackup projects. Out of a current fleet of ~410 contracted rigs, 86 are more than 39 years old and should be retired over the coming decade.

In summary, we believe the jackup fleet is likely to shrink for the foreseeable future. With fleet utilisation today above 90%, no new rigs ordered in over a decade, and growing demand for jackups, the outlook for day rates seems asymmetric.

As the market has tightened over the last two years, day rates have risen to long-term mid-cycle levels. As it rolls its jackup fleet on to current market day rates, Borr Drilling will soon be generating enough cash to return 1/3 of its market cap to shareholders every year. While this yield is impressive, what makes Borr compelling to us as long-term investors is that we believe this level of cash flow is sustainable long-term, and comes with significant upside optionality.

### **Executive Summary**

Borr Drilling is an international oil services company with a fleet of 24 modern and efficient jackup drilling rigs. Jackups are used to produce oil from low-cost, shallow water oil reserves. Demand for oil from such reserves is structurally growing, and so is demand for jackup rigs.

Having been through a period of extraordinary oversupply following the oil price crash of 2014-2016, supply/demand dynamics in the jackup market are now tight, with fleet utilization at greater than 90%.

Despite the tightness in the jackup market, current day rates are only at mid-cycle levels. Even at current levels, however, Borr earns substantial cash flows from its assets. As Borr rolls its fleet onto current market day rates, its revenue, profitability and cash flow is increasing rapidly. Just using today's day rates, we estimate that Borr's EBITDA will increase from \$ 530 million in 2024 to \$ 844 million in 2026. Thanks to a young fleet requiring minimal capex and efficient operations, Borr delivers attractive free cash flow conversion: we estimate 2026 FCF of \$ 705 million and FCFE of \$ 545 million. This level of cash generation compares attractively to Borr's current enterprise value of \$ 3.3 billion and market cap of \$ 1.5 billion.

We believe that Borr can generate a high level of cash flow for many years to come. The longer it takes for significant numbers of new rigs to be ordered, the longer it will be before there is any significant downward pressure on Borr's revenue and cash flows.

To stimulate significant numbers of new rig orders, contract terms will have to improve dramatically from current levels. We estimate average day rates would have to increase by at least 30-40% with contract lengths extending to five years, up from the a current average of two years. Obviously, if clients were willing to sign these sorts of contracts, Borr's cash generation would explode and its trading multiple would likely look very different from current levels. To provide some context, a new ready-to-drill rig ordered today would cost ~\$300 million. If Borr traded at replacement cost (while ignoring its profitable backlog), its enterprise value would be \$7.2 billion and market cap would be \$5.4 billion.

Even if contract terms do improve to the level necessary to stimulate new orders, it will take years for a significant number of new rigs to come into service; the yards that built most of the existing jackup fleet have been dismantled

or repurposed, and the remaining shipbuilding yard capacity is booked-out for several years building other sorts of vessels.

While demand for jackups is cyclical, we appear to be closer to a trough than a cyclical peak in demand. The low and volatile oil prices of recent years have depressed oil capex budgets. Most regions in the world are still using fewer jackups today than they were in 2014 but are in the process of rebuilding their jackup fleets as they seek to grow offshore production to meet domestic demand and balance budgets.

Borr was founded in 2016 by Tor Olav Troim, one of the savviest oil and gas investors of the last few decades. Troim founded Borr to take advantage of the oil price collapse in 2014-2016 and assembled the best portfolio of jackup rigs in the industry at below 50% of replacement cost. The company is run by Patrick Schorn, one of the best operators in the industry. Both are highly aligned fiduciaries seeking to maximise the FCF of Borr's fleet and return capital to shareholders as efficiently as possible.

### **Business Snapshot**

- Borr Drilling owns 24 modern jackup drilling rigs. Their fleet is the youngest and highest quality in the industry, with an average age of only 7 years
- Borr was founded in 2016 to take advantage of the 2014-2016 oil price collapse to acquire rigs at heavily discounted prices. Borr acquired its rigs for an average price of ~\$120 million
- A new rig ordered today would cost ~\$300 million, implying a replacement cost for Borr's fleet of ~\$7.2 billion
- Management is deeply experienced and well-aligned with shareholders:
  - Chairman and Founder: Tor Olav Troim. Former CEO of Seadrill, Founder of Golar LNG, and Himalaya Shipping. Troim owns ~7% of Borr today
  - CEO: Patrick Schorn. 30 years in the industry. Borr board member since 2018. Schorn left his role as COO of Schlumberger to take over as CEO of Borr in September 2020
- Market capitalization: ~\$ 1.5 billion; Net debt: ~\$ 1.8 billion; Enterprise value: ~\$ 3.3 billion
- Financial snapshot:

(\$ million)	<u>2022</u>	<u>2023</u>	<u>2024E</u>	<u>2025E</u>	<u>2026E</u>
Revenue	444	772	1,022	1,225	1,389
EBITDA	142	367	530	716	844
FCFE <sup>1</sup>	(-226)	(-84)	196	381	545
EV / EBITDA			6.2x	4.6x	3.9x
FCFE <sup>1</sup> /Mkt cap			13%	25%	36%

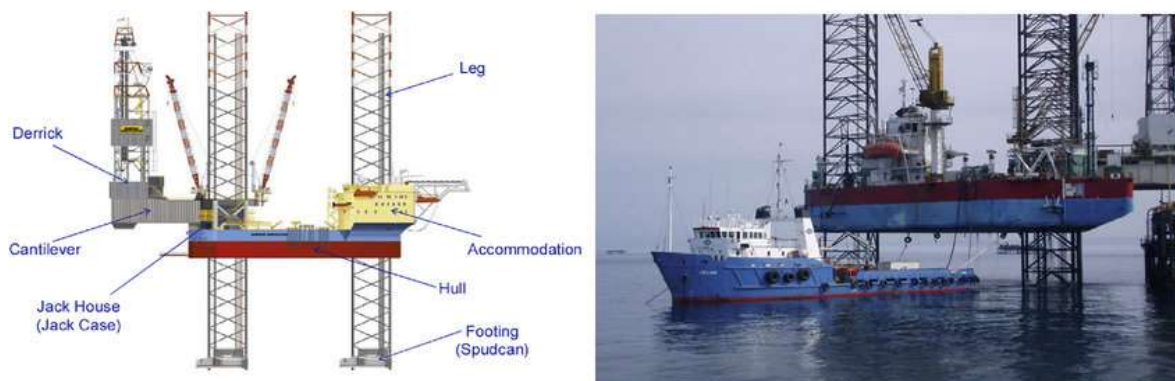
Source: Granular Capital

### **Business Description**

Borr owns 24 modern jackup rigs. Jackup rigs are drilling platforms used to produce oil and gas from shallow water reserves (<400ft) and are widely considered as the workhorses of the drilling industry. The rigs have buoyant hulls so they can be transported from one location to the next. Once in position, their legs are ratcheted down to the seabed and the hull is lifted out of the water to provide a stable platform for drilling. Once a well is complete, the legs are "jacked up" and the rig is towed to its next drilling location.

<sup>1</sup> As described in Balance Sheet section below, Borr's debt has annual amortization and cash sweep provisions. The FCFE we show here for 2025 and 2026 shows FCF before debt pay down to reflect the value accruing to equity owners. We model a minimum distributable FCFE after debt amortization & cash sweep of around \$ 230 million for each 2025 and 2026, which is likely materially higher in practice as the sweep mechanics do not apply if bonds are trading above 105c as is the case currently

Jackups are predominantly used to drill “infill” wells in proven oil fields to bring on production, rather than for new exploration in speculative areas. Infill wells utilize existing hydrocarbon takeaway/processing infrastructure and are very efficient for operators; they leverage existing fixed capital investments and form an integral part of multi-year field development plans. Given this dynamic, operators are unlikely to postpone infill wells in periods of low oil prices. This reduces the cyclicity of demand for jackups relative to other parts of the offshore oil production ecosystem that are more tied to expansionary capital investment.



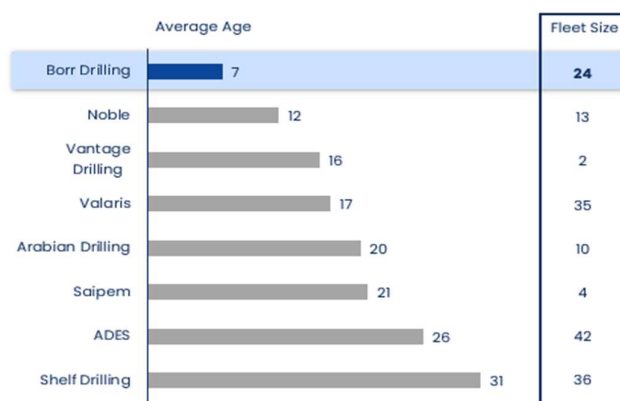
Borr’s rigs are high quality and with an average age of only 7 years, significantly younger than the average fleet in the industry (Noble, one of Borr’s competitors, has the next youngest fleet with an average age of 12 years).

Newer rigs are more versatile than older rigs – they can typically stand in deeper water and drill deeper underground wells. They also drill much more efficiently, due to their higher ‘hook loads’, larger decks and storage capacity that provides more room for drilling and well construction equipment reducing the requirement for logistical support; these properties mean that a modern rig can drill deeper and more efficient wells. It is also important to note that old rigs cannot be retrofitted or upgraded to the same standards that would make them competitive to the most modern rigs in the global fleet.

Modern rigs also have more powerful drilling engines, and more advanced drilling/targeting systems which drive improved accuracy and efficiency. Alongside their benefits for the actual drilling, modern rigs also have higher-quality accommodation for their crews, and better safety features, which helps with recruitment and regulatory compliance.

More than half of Borr’s premium jackup rig fleet features offline capabilities, allowing crews to handle multiple tasks simultaneously, enhancing efficiency and supporting premium day rates. Borr’s fleet mainly consists of 400ft-capable rigs, compared to competitors’ designs that are often limited to 350ft, enabling Borr to operate in deeper waters and further distinguish itself. Additionally, most of Borr’s rigs are Singapore-built, coming from a yard globally recognized for its exceptional construction quality.

#### The industry’s youngest fleet



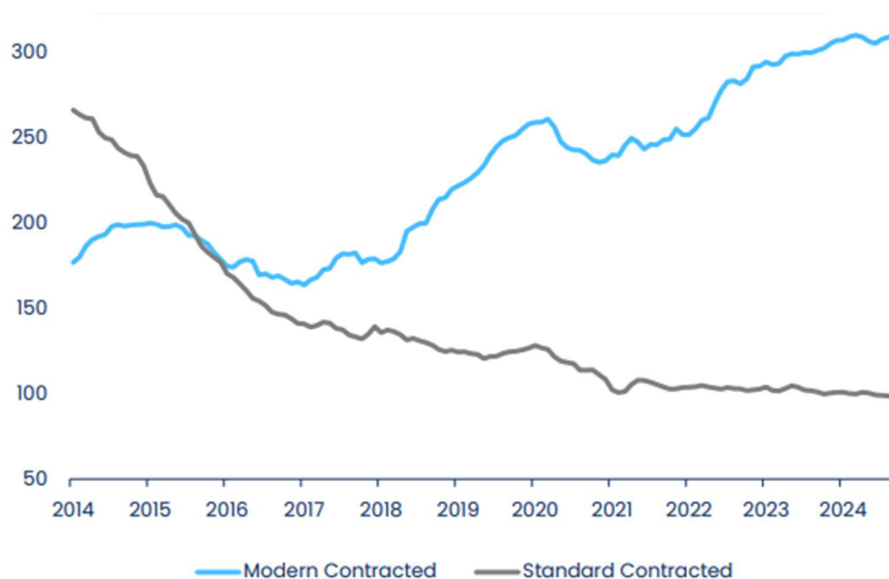
Source: Company presentation / Petrodata by S&P Global

The clear benefits of modern vs. older rigs has led to a steady increase in the market share of modern rigs over time. Modern rigs now comprise 75% of the contracted jackup fleet, up from 50% in 2015. Given their greater capability and better efficiency, newer rigs command significantly higher “day rates” than older rigs. Modern rigs typically command day rates with premiums often above 30% versus standard rigs.

Modern rigs not only generate higher revenue, but also significantly higher cashflow than standard rigs. Newer rigs need much lower and more predictable maintenance capex. Modern units can therefore generate free cash flows many times larger than older units with materially less variability.

We expect the number of standard jackups in service to continue to decline over time. Key markets for old jackups, such as India, are focusing more on safety. As they do so, older jackups will increasingly struggle to meet requirements stipulated in tenders. This should lead to steady retirements of older jackups and a further tightening of the overall market. For example, the Indian Parliament has debated a bill that would impose a 21 year age limit on jackups; this single bill would remove 26 of 37 jackup rigs used by India’s National Oil Company (NOC), ONGC, from service.

### Historical Contracted Rig Count



Source: Company presentation / Petrodata by S&P Global

Rig companies like Borr typically operate and staff rigs themselves. Clients pay a day rate for the jackup for a pre-agreed period of time and Borr is responsible for hiring the crew and operating the rig to deliver the contracted program of wells. As they are intensively involved in day-to-day operations - and not simply asset owners – Borr’s operating track record is a critical consideration in any tender process.

Borr Drilling’s infrastructure offers a significant competitive advantage in the global market. Its tax structure, legal entity framework, work permits, local licenses, and specialized knowledge create a distinct strength that most other regional jackup drilling companies lack. This is a crucial factor in securing premium day rates, particularly in more challenging regions like West Africa.

With the best fleet in the industry and an excellent operational track record, Borr is consistently able to secure day rates ahead of market averages. So far in 2024, Borr has secured \$ 650 million of backlog at average day rates of \$184k, or a ~30% premium to the reported market average day rate of ~\$130-150k.

Borr runs a truly international operation with rigs deployed in all key jackup markets. Borr’s peers, particularly those listed in the Middle East, often do not have an operating track record or trusted relationships with operators outside their home markets. With little credible alternative, these players can be forced to accept below market rates by

powerful local clients. Because Borr is a truly international player, it can move rigs around the world to wherever it can secure the best contracts. This flexibility is a key source of Borr's ability to secure above-market day rates.



Source: Company presentation

For completeness on the jackup competitive landscape, there are currently no viable alternative technologies to jackups to explore and produce oil and gas from shallow water basins. In very shallow water, it is possible to build 'islands' on which normal onshore 'land rigs' can be situated but these projects are very rare and only viable in very near shore locations. These islands are highly capital intensive and in any case not directly competitive with Borr's rigs as they are only viable in water below 40ft which is too shallow for Borr's rigs to access.

### **Business Model / Unit Economics**

Borr makes money by contracting individual rigs and crew for drilling services to oil & gas producers. Contracts vary in duration from months to several years and they are priced at a negotiated day rate for the duration of the contract. Borr's costs of operating and maintaining the rig have been broadly stable over time at ~\$50k / day (this cost varies by region but this is Borr's approximate average cost today), and the operating profit Borr makes is the difference between these costs and the day rate agreed with the customer, which has historically varied between ~\$50k / day when the market is oversupplied and ~\$250k / day when the market is tight. Borr's current average day rate across their fleet in FY 2024 is ~\$135k and as noted the average rate of contracts signed this year is ~\$184k. Due to the modern and efficient nature of Borr's fleet, they have the lowest unlevered cash break-evens in the industry at ~\$59k per rig per day (including \$6k in company SG&A and \$3k in maintenance capex), providing for highly attractive unit economics that lead to rapid growth in cash flow generation when rates are rising. The high degree of operating leverage in the model is shown at various day rates in the table below on a per rig basis:

Illustrative Rig Economics	\$125k Dayrate	\$150k Dayrate	\$175k Dayrate	\$200k Dayrate
	\$'Ms	\$'Ms	\$'Ms	\$'Ms
<b>Revenue (95% utilisation)</b>	<b>43.3</b>	<b>52.0</b>	<b>60.7</b>	<b>69.4</b>
OPEX	(18.3)	(18.3)	(18.3)	(18.3)
SG&A	(2.2)	(2.2)	(2.2)	(2.2)
<b>EBITDA</b>	<b>22.9</b>	<b>31.6</b>	<b>40.2</b>	<b>48.9</b>
<i>EBITDA Margin %</i>	<i>53%</i>	<i>61%</i>	<i>66%</i>	<i>71%</i>
Maintenance CAPEX	(1.5)	(1.5)	(1.5)	(1.5)
<b>Unlevered FCF per rig</b>	<b>21.4</b>	<b>30.1</b>	<b>38.8</b>	<b>47.5</b>

Source: Granular Capital



The figures above show that at blended market day rates of \$150k, Borr's rigs generate an average FCF of \$30 million per year, a figure which rises quickly even with modest increases in rates. At the leading edge rates they have been achieving recently of ~\$184k, unlevered cash flow per rig is ~\$42m or 68% above the company's current average FCF/rig. This means that Borr will see meaningful cash flow growth even if market rates stay flat, as some of their rigs which have older, lower-priced contracts expire and are repriced at prevailing levels. Borr is already signing contracts at well above these levels. For example, in April 2024, the company secured a contract for 480 days in Africa for a day rate of ~\$200k including mobilization paid by the client.

It's worth reiterating that Borr's young fleet has lower maintenance requirements than other players. All rigs have to undergo regular special surveys (typically every five years). The costs of bringing rigs up to standard for these surveys increase as rigs age. The capex requirement for a special survey for an older rig can be as high as \$20-30 million; older rigs require large lump-sums investments just to remain in business. We assume Borr's average Special Periodic Survey (SPS) cost per rig over the next 10-15yrs should be below \$10 million. In addition to the difference in costs, the SPS duration and scope for younger rigs is far more predictable, leading to less out of service time.

### **Demand for jackup rigs**

At a high level, it is important to note that demand for oil and gas is likely to continue to grow for some time. Almost all projections expect oil demand to grow until at least 2030-2035. While we do not know when oil demand will peak, we will need to be producing large volumes of oil for decades to come. Even most sensible "2050 net zero" scenarios still expect oil demand of >70 million barrels / day in 2040 (vs ~105 million barrels / day today). Consumption of oil is critical to modern existence and the shift to alternatives will be a gradual process.

Keeping oil production steady at ~105 million barrels / day for the next 10 years and at required levels thereafter will require significant capital investment as current sources of production decline and need to be replenished. Conventional production naturally declines at ~5% per year, and unconventional reserves much faster, meaning just to hold oil production flat, the world needs to bring online ~5 to 10 million barrels/day of incremental production every year, which requires considerable capital investment.

Over time, more and more of the incremental production required has been coming from offshore reserves. Oil was initially produced from low-cost and easy-to-access onshore fields, but as they have depleted we have been producing from increasingly complex reserves (conventional offshore reserves – first in shallow water and then in deeper water, unconventional onshore, high pressure/high temperature offshore reserves, and tar sands).

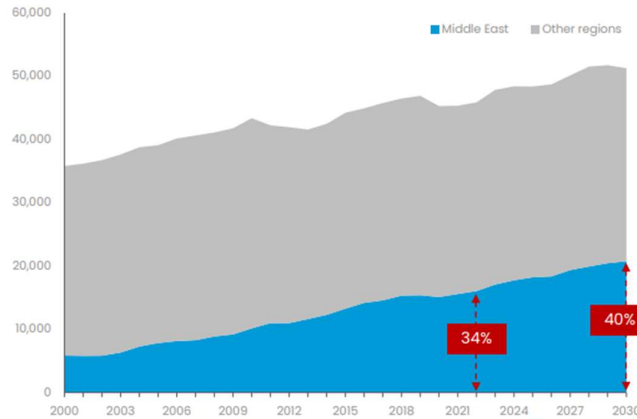
Borr's customer base has evolved to comprise 67% National Oil Companies (NOCs) and 33% International Oil Companies (IOCs) and independent operators. NOCs, with some of the lowest breakeven costs and a strong need to fund national budgets, are likely to produce the last oil barrels in the world. This makes NOCs a highly desirable customer base for long-term business.

### ***Shallow water oil production is growing***

As shown below, offshore oil production has grown steadily over the last two decades. Within this, shallow water production has grown its share from approximately 64% in 2015 to approximately 66% today. There has been a significant shift in the source of shallow water oil over time. The US and the UK led the way in shallow water production in the 1970s, though it has declined to very low levels in these regions over the last two decades. The decline of US and UK shallow water production has been offset by growth in shallow water offshore production elsewhere.

### Middle East with increased focus on offshore shallow water

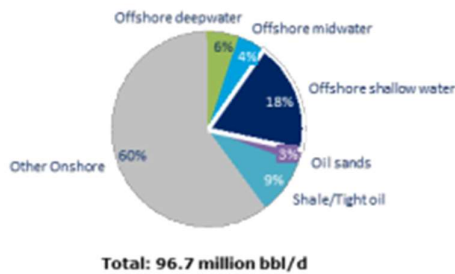
Offshore production<sup>1</sup> by region ('000 boe/day)



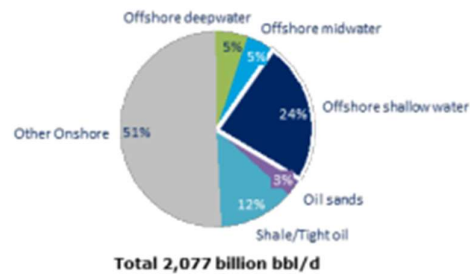
Source: Company presentation / Rystad Energy

Most importantly, the remaining shallow water hydrocarbon resource is enormous. While shallow water has accounted for approximately 18% of global annual oil production in recent years, ~24% of all known remaining oil reserves are in shallow water reserves. That equates to over 450 billion barrels of oil equivalent of remaining shallow water hydrocarbon resource, which would be sufficient to maintain current shallow water hydrocarbon production at current levels for 70 years.

Historical liquids production by supply source  
(2017 production – million bbl/d)



Remaining discovered oil and gas resources per supply segment (billion bbl/d)



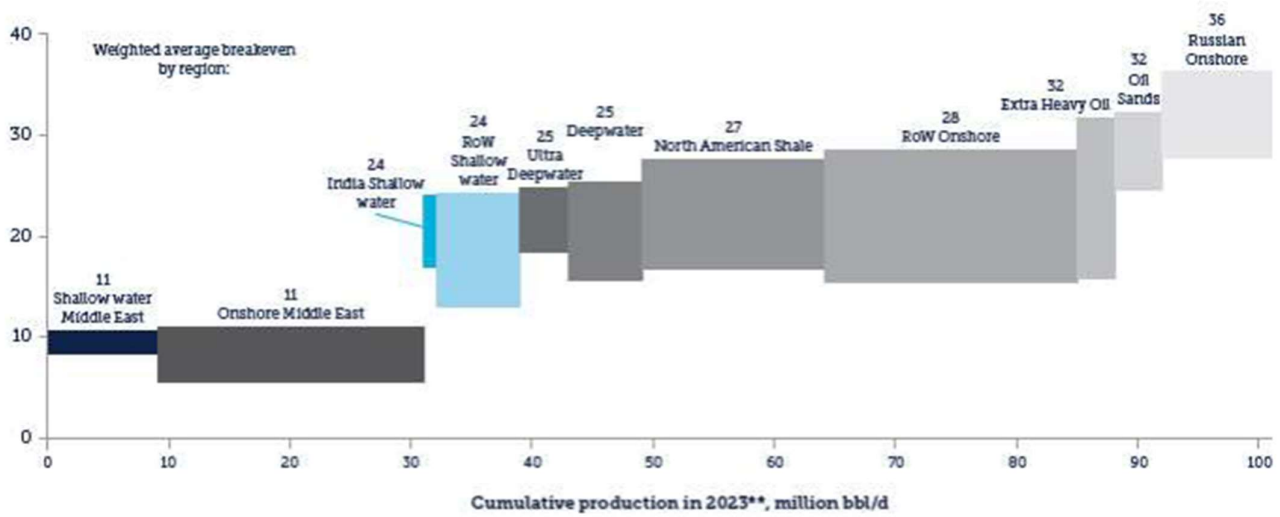
Source: Rystad Energy UCube, 30 May 2018

After conventional onshore resources, shallow water reserves are typically the cheapest sources of hydrocarbons due to lower geological risk (brownfield) and shorter cycles (existing infra-structure). As shown below, shallow water reserves reside on the left hand side of the global cost curve, with all-in breakeven production costs of \$10-\$30/barrel. Given these attractive characteristics, there are no realistic oil demand scenarios where it wouldn't make sense to keep drilling shallow water for decades to come.

Shallow water wells are short-cycle, meaning they can be drilled and producing liquids in as fast as 30-60 days, vs. many years to first production from more complex offshore reserves. The combination of low costs and short payback periods is driving more investment into the shallow water space.

It is also worth noting that shallow water wells are in general lower risk (geology, existing infra, lower breakeven) than more complex greenfield deepwater offshore wells, and hydrocarbons produced from conventional shallow water wells are also less resource and energy intensive – and therefore cleaner – than hydrocarbons produced from unconventional (shale) wells or tar sands.

**Global Liquids Cost Curve**  
**Brent Equivalent Forward-looking Breakeven\* Oil Price, \$/bbl**



\* Breakevens are calculated as of the current year. All historical cash flows are sunk, 10% NPV \*\*20-80 percentile range  
 Source: Rystad Energy research and analysis; Rystad Energy Ucube, February 2021

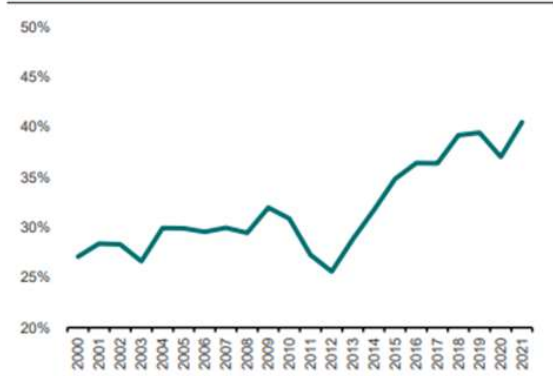
The drivers behind the increasing production from shallow offshore reserves are likely to continue long-term as onshore reserves deplete which means demand for jackups rigs will grow. In recent years, the biggest increase in jackup rig demand has come from National Oil Companies (NOCs). This is significant because these NOCs have huge stated reserves of hydrocarbons, and are choosing to grow their offshore production.

The fact that NOCs around the world are increasingly drilling shallow water reserves confirms their attractive economics and suggests it is becoming harder to maintain production from remaining onshore reserves. In other words, there is a long-term structural driver of demand for jackups as NOCs look to maintain oil production and increasingly have to move offshore to do so.

For example, in the last decade, Saudi Aramco has increased offshore oil production by 60%, from 3 mbpd to 5 mbpd. In order to drive this significant increase in shallow water offshore production, Saudi Aramco increased its jackup count from ~20 to ~60 over the same period.

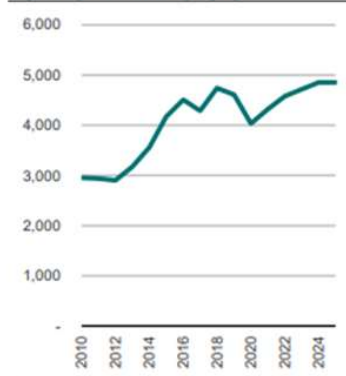
We see similar behaviour in the UAE which recently stated it would increase its oil production capacity, otherwise known as Maximum Sustainability Capacity (MSC), to 5 mbpd by 2027. The UAE’s national oil company, Adnoc, has increased offshore liquids production from ~1.3 mbpd in 2010 to ~2.25 mbpd by 2023 and over the same period the jackup count has risen from ~15 to ~35.

**Saudi Arabia – share of liquids production from offshore**



Source: Rystad Energy

**Saudi Arabia – offshore liquids production (kbpd)**



Source: Rystad Energy

**Saudi Arabia – jackup count**



Source: S&P Global

UAE – share of liquids production from offshore



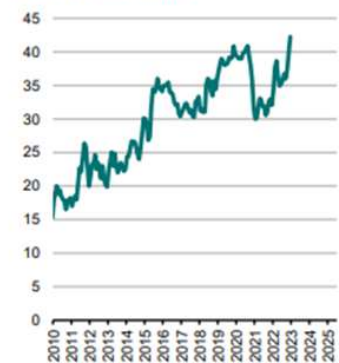
Source: Rystad Energy

UAE – offshore liquids production (kbpd)



Source: Rystad Energy

UAE – jackup count



Source: S&amp;P Global

Outside the Middle East, producers have been slower to rebuild their jackup operations since the 2014-2016 oil price crash. Many regions still have jackup rig counts below previous peaks and are producing significantly less oil today than they were in 2013. This is starting to change.

In the last 18 months, demand for jackups has been increasing from both NOCs and international oil companies in many regions outside the Middle East. Demand has been particularly strong in SE Asia, but is also increasing in West Africa, Guyana, Mexico, and even in regions which have not historically employed many jackups like Brazil, Trinidad and Suriname. In a clear sign of this market evolution, Borr recently signed a 4 year contract at a day rate of ~\$180k in Brazil for its Arabia I rig. This deal was signed in July 2024 only two months after the Arabia I had been suspended by Saudi Aramco. The new Brazilian contract was at a 60% higher dayrate than the prior contract with Aramco, which had been agreed in late 2022.

When we speak to rig brokers, they see significant demand for young and premium jackups today. Brokers are aware of firm requirements for new additional jackup work/tenders that exceed the number of jackups rolling off contracts. This new activity will result in fleet utilization grinding higher over coming months. Including the brokers' assessment of 'possible' new projects the market would be currently undersupplied and for the first time in history, no newbuilds are coming to address the shortfall.

Regions	Contracted Jackups		Chg since prior peak
	Apr-14	Sep-24	
Middle East	127	171	44
India	32	38	6
West Africa	20	14	-6
SE Asia	67	40	-27
North Sea	46	28	-18
Mexico	50	32	-18
US GoM	15	4	-11
China	30	60	30
Other	42	23	-19
<b>Total contracted</b>	<b>429</b>	<b>410</b>	<b>-19</b>

Source: IHS Markit

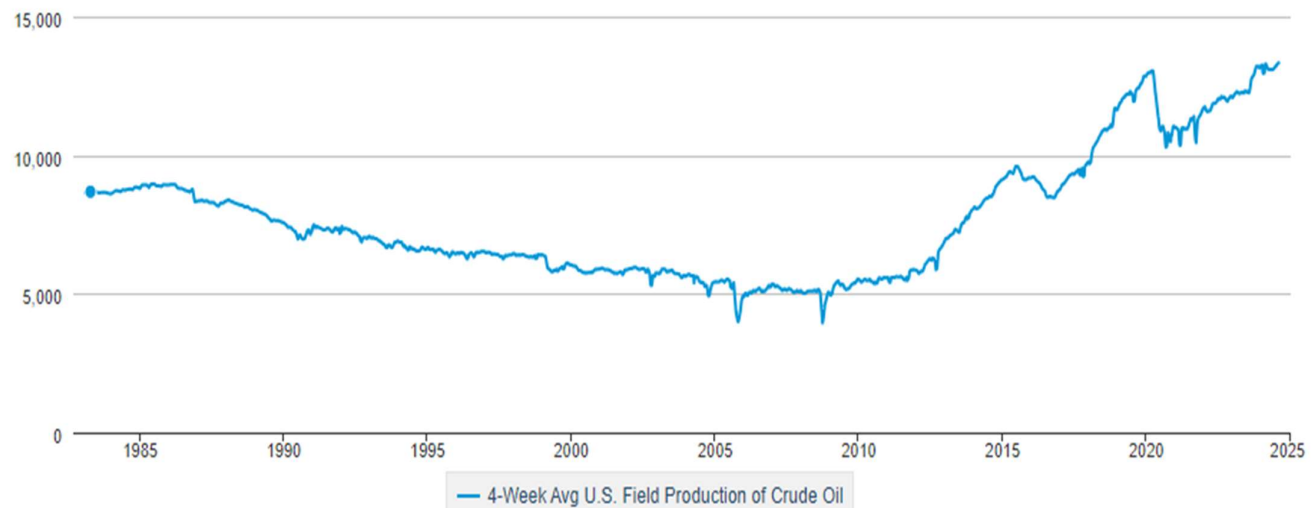
The recovery in demand for jackups from the 2016 lows has occurred despite the concurrent increase in supply from US unconventional oil and gas reserves (shale) of ~8 million barrels / day. It seems unlikely that American shale will deliver the same level of output growth over the next decade, and there's a good chance shale output struggles to grow from current levels; there has been a considerable consolidation among US shale producers which has brought

more discipline to capex spending and the number of wells drilled. At the same time, there is some evidence that shale inventory quality is declining as many of the best locations have now been drilled. If shale production struggles to increase, the call on shallow water offshore reserves – and therefore jackup demand – could increase significantly.

In summary, oil production from offshore shallow water reserves grew solidly from 2015 to 2023 despite the decline in shallow water production in the UK North Sea and the US Gulf of Mexico and the massive growth in production from US shale. Neither of those negative drivers is likely to be repeated and demand for jackups from other markets seems to be growing healthily. This supports a solid low- to mid- single digit annual demand growth outlook for shallow water oil and jackups over the next decade.

#### 4-Week Avg U.S. Field Production of Crude Oil

Thousand Barrels per Day

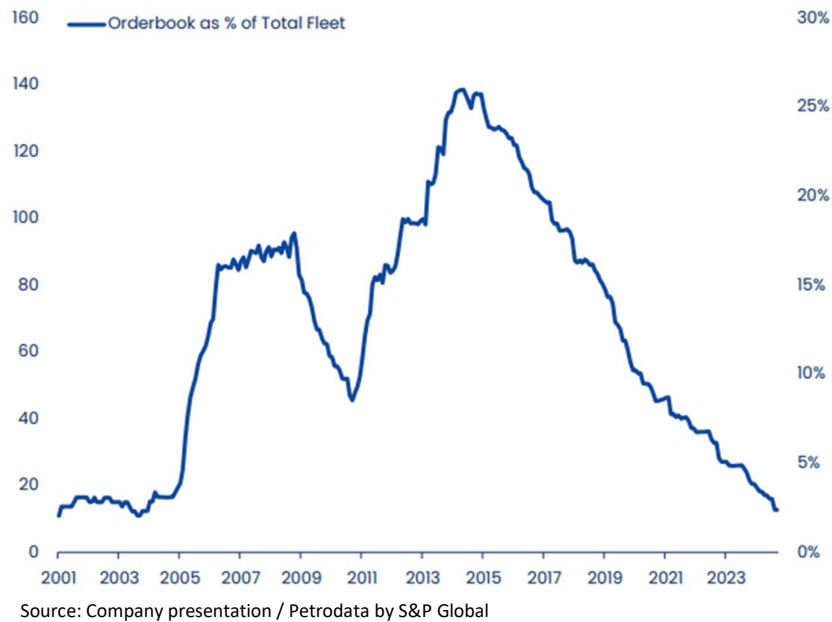


Source: U.S. Energy Information Administration

#### A short history of the jackup market

Hard asset industries are historically cyclical. When thinking about cyclicity, investors often focus on demand, but it is typically supply that pushes cycles to extremes. This dynamic is evident in jackups, which have experienced multiple booms and busts in the building of new rigs since the inception of the industry.

It is in this context that the current backdrop is so exciting, as there is virtually zero new supply coming to the market while much of the existing fleet is old and needs to be scrapped in coming years.



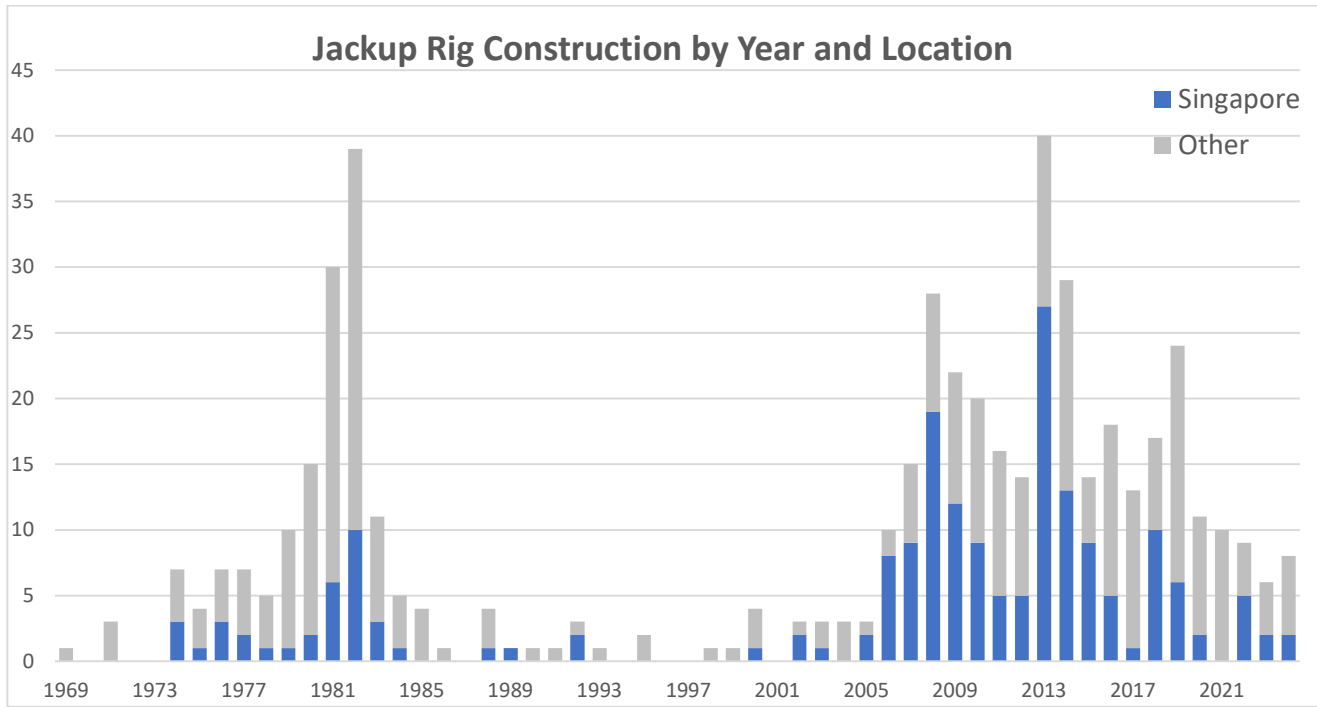
In order to better understand the supply backdrop we must first explore the history of jackup construction over the last couple of decades. In the mid-2000s, fuelled by talk of a commodity super-cycle and record day rates, orders for new rigs surged. New orders paused temporarily following the 2008 financial crisis, but then a wave of new jackup orders were placed between 2011 and 2014 as resilient day rates and growing oil & gas demand attracted more capital to the sector. This speculative building boom was exacerbated by state-supported construction yards (mostly in Singapore) who were taking orders with as little as 5% deposits to stimulate employment in the wake of the Global Financial Crisis.

By 2015, almost 150 rigs were under construction, resulting in a wall of new supply. More than 25% of the existing fleet was scheduled to be delivered in 2015 and beyond. The timing of the new rig orders could not have been worse. The jackup orderbook peaked while the oil price was in the process of falling from ~\$110 / barrel in mid-2014 to ~\$30 / barrel by early 2016. Oil exploration and production budgets were slashed and marginal projects were being cancelled just as the newly built jackups were entering the market. Worldwide utilization of the modern jackup fleet collapsed from ~95% in 2014 to ~65% by 2017, which sent day rates down from ~\$150k/day to ~\$50k/day, their lowest level in decades. At \$50k/day, a rig struggles to cover its operating costs. With only 5% deposits at risk, speculators walked away from the orders they had placed, leaving shipyards building rigs for which they had no buyers.

As we will come on to later, Tor Olav Troim set up Borr to capitalize on the distress in the market by buying rigs at knockdown prices. He was confident that the long-term drivers of demand for modern jackups were sound, and that eventually the new supply would be absorbed and the market would heal. Borr was founded in 2016 and started buying rigs in 2017. By 2019, the market was beginning to mend and day rates were rising. Then COVID hit and delayed (but did not derail) the recovery process. Utilization is now above 90%, day rates have recovered to mid-cycle levels, and Borr is nicely positioned to generate high levels of cash flow for years to come.

### Supply of jackup rigs

Two Singaporean construction yards (Keppel & PPL) built approximately 50% of all jackup rigs operating today, and the majority of the rigs built in the boom described above. These two construction yards were so damaged by the 2014-2016 oil price bust that they had to be bailed out by the Singaporean government and merged into one entity (now called Seatrium). With the merger, Seatrium has permanently reduced a significant amount of production capacity; the old PPL jackup construction yard is currently being redeveloped into waterfront property.



Source: IHS Markit

### The Redevelopment of the Sembawang Shipyard

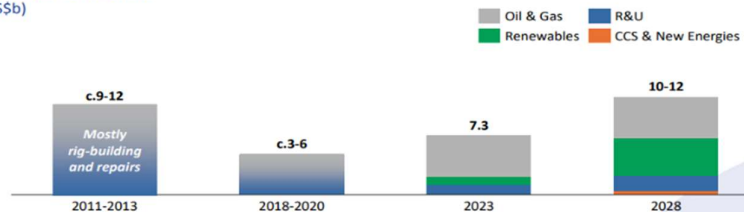


At the same time as it is reducing jackup production capacity, Seatrium is working hard to fill its remaining production capacity with anything other than drilling rigs. Seatrium expects its revenue from oil and gas related work to fall from S\$9-12 billion prior to the 2014-2016 oil price crash to less than S\$4 billion in 2028. Within its shrinking oil and gas segment, Seatrium is resolutely focused on growing its business in floating LNG and FPSOs where it is a market leader.

### BUILDING A MORE RESILIENT PORTFOLIO WITH STRONG REVENUE GROWTH



#### REVENUE EVOLUTION (S\$b)



- Strong revenue growth:**
- Sharpen focus on prioritised segments
  - Support from sector tailwinds
  - Competitive advantages in key markets

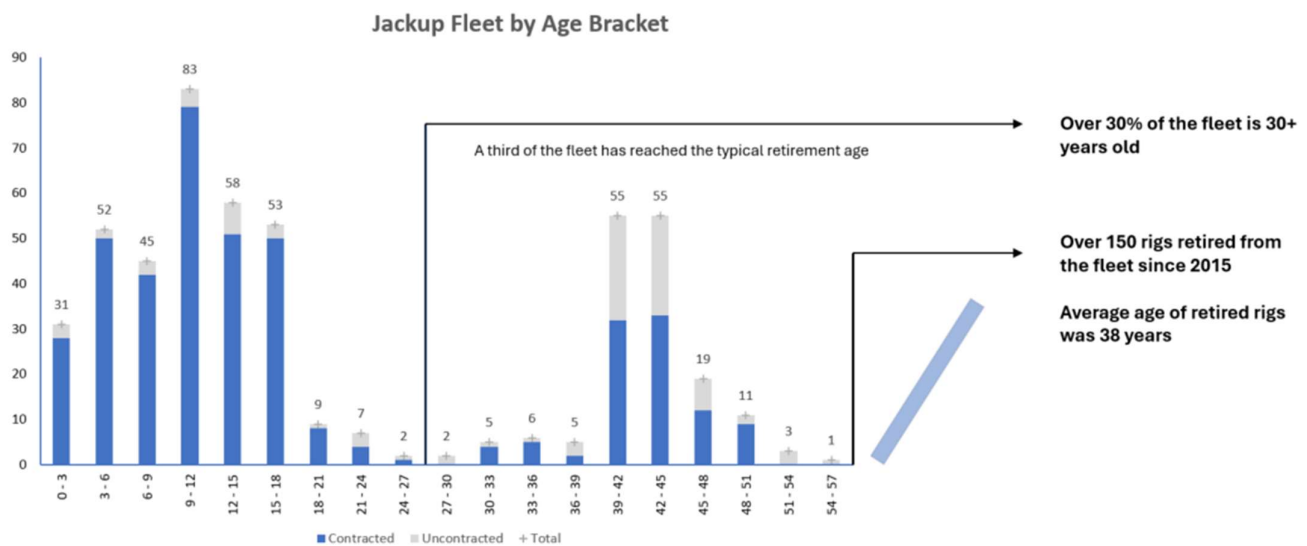
- Build a more resilient and diversified portfolio:**
- More "green" products
  - Increase share of Repairs & Upgrades baseload revenue
  - Improve contract terms with shared risks and progressive milestone payments

Having been effectively bankrupted by an over reliance on the oil and gas sector in the past, Seatrium is intent on diversifying its revenue streams. The company is pushing aggressively into offshore wind and the repairing and upgrading of the global shipping fleet. Seatrium is not just toying with a push into new industries; they are expected to form the core of the company over time. 50% of Seatrium's debt will soon come from 'green bonds' which effectively locks the company onto a 'transition path'. In other words, the company means what it says about its new trajectory; it has made deep commitments with all its stakeholders which adds resistance that would have to be overcome before the company can consider taking significant numbers of jackup orders in the foreseeable future.

In summary, Seatrium has made numerous interlocking commitments that will limit building of jackups to only a fraction of the levels of previous peak levels. The company also makes repeated reference to ensuring that any project moving forward will have robust margin targets and onerous milestone payment terms. In short, even if it accepts a few orders over time, Singapore is highly unlikely to ever subsidize the construction of jackups again.

It is important to mention that a similar consolidation trend has also happened in China during the period, even if to a smaller extent than in Singapore. Furthermore, even yards that could still be interested in rig building are unlikely to be interested in small order volumes as this does not provide the much needed scale in vessel building. Lastly, there has been no investment in new or updated rig designs, meaning that even in the unlikely event of a future wave of construction, those assets would have no significant advantage against Borr fleet.

The removal of jackup production capacity has not mattered much in recent years as no new orders for jackups have been placed since the 2014-16 crash. Almost all the new rigs that were ordered pre-2015 have now been delivered and are currently working. Out of the approximately 10 jackups recorded as under construction, only 4 rigs are expected to be competitive and in condition to be delivered within 24 months (one of these is Borr's, due to be delivered at the end of 2024).



While approximately 100 new jackup rigs have been delivered since 2014, the global jackup fleet has actually shrunk since then as more than 150 old rigs have been scrapped. Despite all this churn, ~21% of the currently contracted fleet is still over 39 years old. As noted above, safety regulations are rising around the world which is increasing the costs of keeping old rigs in service. It seems likely that older rigs will continue to be retired over the coming years.

With no new supply and continuing retirements of older rigs, the jackup fleet will shrink in the near future. Given the growing demand for jackups outlined above, this creates an unsustainable situation given that utilization of the existing fleet is already above 90%.



It is worth reiterating this point; during the boom years of rig construction in 2006 to 2016, the world produced on average 22 jackups per year, of which the Singaporean yards built 50-60%. With the Singaporean yards now eschewing jackup business, the world's theoretical new jackup production capacity is therefore ~10-12 rigs per year, if the yards weren't already full of other projects. Today, ~86 contracted jackups (~21% of the working fleet) are more than 39 years' old and should be retired over the next few years. Even if all the theoretical global jackup capacity started making jackups today, it is difficult to see how the fleet will grow by more than 1% per year over the next decade. Every year that goes by without a new jackup order being placed will make it harder just to maintain the fleet at its current size as retirements accelerate.

#### *Towards a less cyclical market structure*

As noted above, the jackup market has historically been cyclical. Nevertheless, unless something significant changes, the most likely outlook for jackup demand appears to be low- to-mid single digits per year. This sort of growth outlook does not get anybody's pulse racing. Except for ours.

The longer it takes for anyone to be excited about demand growth in the jackup market, the longer it will be before anyone attempts to place orders for new rigs. With no new orders and a steady, if sluggish, growth outlook combined with accelerating retirements, this market should be significantly less cyclical over the next decade than it has been at any time since the beginning of the industry in the 1970s.

#### *Potential for consolidation in the jackup market*

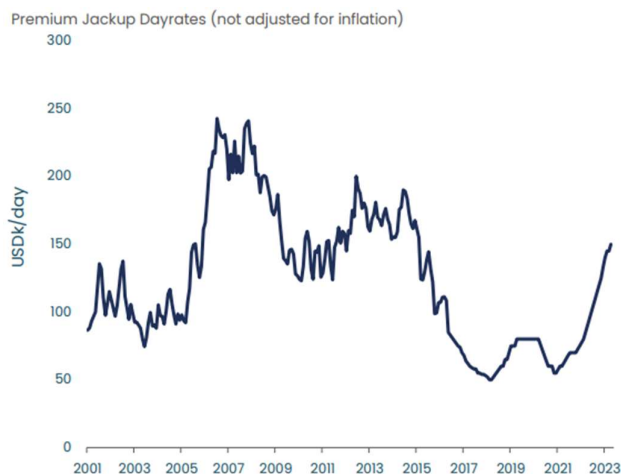
The jackup market has historically been highly fragmented. Since the GFC a number of large players have been created – Shelf Drilling acquired 37 rigs from Transocean in 2012 and later some units from Maersk Drilling; Ensco and Rowan merged to form Valaris (~50 jackup rigs today, including the ARO JV); Borr assembled its portfolio of 24 rigs starting in 2016, and then the Middle Eastern players ADES (46 jackups), ADC (12) and Adnoc Drilling (35) have been assembling their fleets in recent years. In 2014, the top seven players owned ~132 rigs out of a market of over 450 operating rigs. Today, the top seven players own over 200 of a total of ~400 operating rigs.

Given the significant differentials in recent performance and future cash flow prospects between various players, there is the potential that the market could consolidate further in coming years.

With the market as tight as it is today, a combination between any of the bigger players could catalyse a significant change in market dynamics. In particular, while some weaker players with heavy debt burdens are forced to operate old assets to generate cash, a stronger player might be able to take the decision to retire older assets, foregoing current cash flow to take tired assets out of the fleet and further tighten the market.

#### **Current day rate environment**

The recent path of day rates in the jackup market has been so volatile that it is important to take a step back. As the market has tightened since 2021, average day rates have increased around 200%, from \$50k to \$150k today. While the speed of this increase has been dramatic, \$150k day rates are only in-line with long-term market average rates, and this is without adjusting for inflation or the improvement in quality of rigs over time.



Source: Company presentation / DNB Markets / Petrodata by S&P Global

Utilisation remain strong and back at 2014 levels



While clients have likely been surprised by the speed of the recent move in jackup pricing, there are early signs that they are adjusting to the current reality. As operators are seeing the market tighten, they are beginning to scramble to secure rigs, and are seeking longer-term contracts. Average contract lengths are hitting recent highs of around ~2 years, up from ~1yr in 2016. Of course, this locks in higher rates for rig owners, and further exacerbates the supply shortage for clients.

### Increasing contract duration



Source: Company presentation / Petrodata by S&P Global

Given the solid demand growth outlook and lack of new rig supply, it seems reasonable to place a relatively high degree of confidence in the assumption that market day rates should be at least stable around current levels. Our confidence in this assertion has increased over recent months as the market has calmly absorbed around 20 globally competitive modern rigs recently suspended by Saudi Aramco. We address this topic in more detail below, but the key point to make here is that the sudden and unanticipated increase in rig supply did not drive market rates below their long-term average. In fact, Borr has signed contracts in 2024 at an average rate of \$184k per day while increasing contract length. This shows that there is significant depth of demand for rigs at current day rates.

The table below lists the contracts Borr has secured over the last ~18 months, and it shows how they have been able to recontract their rigs at increasingly higher rates, as well as negotiating longer term contracts. These rates include mobilization paid by the clients and are meaningfully higher than those in the market averages chart above, demonstrating the premium that Borr's high quality assets command.

Rig	Date Announced	Contract Length	Customer	Day Rate
Arabia I, Gunnlod & Norve	July 2024	1,779 days	Petrobras, Marathon Oil, ENI	185k
Prospector I, Gunnlod & Vali	April 2024	820 days	Various (undisclosed)	193k
Norve, Mist & Thor	February 2024	495 days	BW Energy, Valeura Energy, undisclosed	166k
Idun	November 2023	2 years	PTTEP	170k
Natt & Prospector 5	August 2023	1,307 days	ENI	160k
Gerd	July 2023	270 days	Bunduq	170k
Thor	July 2023	151 days	Petronas Carigali	165k
Hild	April 2023	725 days	Fieldwood Energy	170k
Ran	January 2023	200 days	Total Energies	150k
Arabia III	December 2022	5 years	Saudi Aramco	155k

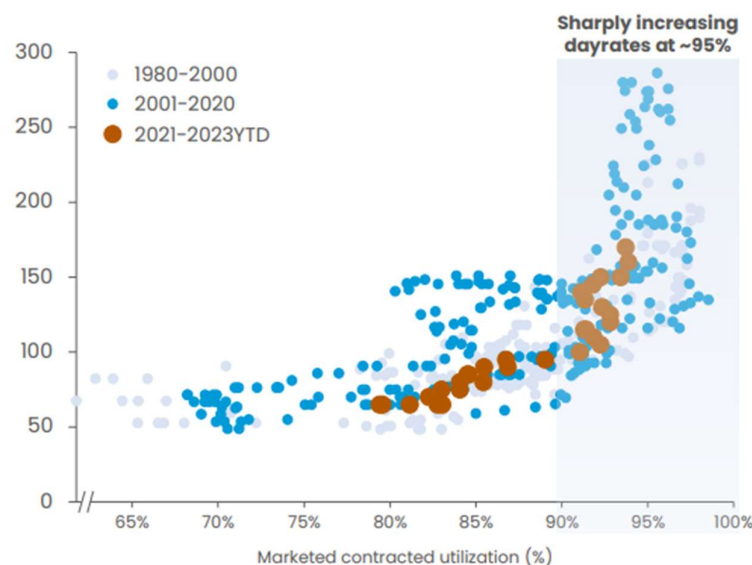
Source: Granular Capital / Company filings

It is consistent with history that with the market over 90% utilized, contract terms shift firmly in favour of rig owners. As utilization moves above 90%, the market starts to become effectively “sold out.” Jackup rigs are not commodities, there are numerous different types and specifications with requirements differing from tender to tender. At the same time, demand for rigs is diversified all over the world, and you only need one market to be sold out to increase day rates in all other markets.

When rigs start to move across markets to fulfil demand, day rates can start to gap upwards. To explain, it can cost \$10-\$20 million to move a rig across an ocean. In a tight market, this mobilization cost is borne by the client, increasing the effective day rate of a one year contract by \$27k-\$54k per day. Rig owners competing in a tender against rigs coming from another region can therefore increase their offered day rate by over \$27k per day versus the previously prevailing local market rate. When clients are paying mobilization fees to secure a rig, they will also be incentivized to lengthen the contract term to reduce the impact on the effective day rate they are paying. So as the market tightens, it is natural to see contracts both jumping in price and extending in duration.

What is somewhat unusual is that we are at mid cycle day rates despite the fact that there is no new supply of rigs under construction, and utilization will grind higher in coming years. In the past, when it appeared the market might be entering a period of undersupply, day rates inflected sharply above \$150k/day; in the early 2000s they rose as high as \$300k/day.

Jackup Dayrates USDk/day (inflation adjusted)



Source: Company presentation / Pareto Securities

Clearly, the market is complacent and does not anticipate a sudden tightening in jackup utilization. We are comfortable with this outlook. In a stable day rate environment, Borr's cash returns to shareholders will increase dramatically.

However, we are excited about the fact that as the market is so tight it creates a highly asymmetric profile for day rates from here. As noted, with no new supply on the horizon, the market is reacting calmly to unexpected negative changes in demand. On the other hand, a slight increase in the competitive intensity by clients to secure new rigs could catalyse a dramatic increase in day rates, as has happened a number of times in the past.

There are numerous catalysts that could positively inflect demand for jackup rigs. An increase in oil prices could accelerate field development plans around the world; OPEC could increase production quotas; Saudi Arabia could reinstate its MSC target of 13 million barrel / day; US shale oil growth could stall or reverse (we note that Presidential candidate Harris appears to be no friend of the shale drillers). We believe it is very dangerous to predict the price of oil, but like the fact that by owning Borr we are effectively being paid to own a valuable option that would pay off handsomely in any of these scenarios. To be clear, under the current demand / supply dynamics we do not need any of these scenarios occur in order to earn highly attractive returns from Borr.

An additional point to note is that jackup demand is relatively inelastic given the low cost of shallow water offshore reserves and the very high returns that can be achieved from them. Even with jackup day rates above \$500k per day, Borr's clients can still generate over 30% IRRs at current oil prices, providing significant headroom for day rates to rise before we start to see destruction of demand for jackups.

#### *Newbuild economics*

A critical plank of our thesis is that current day rates of ~\$150k are too low to justify new jackup construction. Assuming 90% utilization, at \$150k/day a rig generates FCF of ~\$27 million per year. A newbuild costs at least \$300 million, suggesting a 9% cash on cash return. This seems far too low given the risk; the rig would not be delivered for at least 30 months, which is a long time to wait given how cyclical the jackup market has been over time. Importantly, it is impossible to use leverage to juice equity returns today; yards require an equity downpayment of ~50% to take an order, and in any case, even Borr, the best operator in the sector pays 10% interest on its bonds.

It is important to reiterate here that Borr and its peers currently trade at enterprise valuations of \$120-140 million per rig. No sensible investor should consider placing an order for a new \$300 million rig when the market is currently valuing contracted, cash flowing new rigs at around \$120-140 million a piece.

For Middle Eastern players the situation could be different, as their cost of capital is dramatically lower and valuations higher. Nevertheless, these players have no experience ever building rigs and also trade at lower valuations than replacement cost, even if dramatically higher than their western counterparts.

Clearly, day rates will need to increase significantly before it would make sense for someone to consider placing new rig orders. Not only will day rates need to rise, but someone placing an order for a new rig would need to have a high degree of confidence that day rates will stay high for a long time and/or have in hand a contract for five years or more at that higher day rate. It seems unlikely that any client would provide that contract for a theoretical new rig when they can lease a modern rig from Borr or its peers in the market today. Moreover, as traditional bank financing is no longer available, financing of a newbuild would almost by default have to be backed by a watertight contract of significant duration.

Even if we get to the stage where buyers are willing to place orders, it remains to be seen if any yards have the capacity to build high quality jackups at scale. It is important to note that when the yards were building tens of jackup rigs / year, they had an experienced work force and a fully built out supply chain and all the necessary components lined up in their yards waiting to be assembled. Today, none of that supply chain exists and much of the labour has been repurposed (indeed, many of the workers in Singaporean yards were foreign and they were mostly sent home with their visas revoked in the wake of the 2014-2016 oil price crash). Many of the key components are long lead time items

and the manufacturers of those items have similarly been focused elsewhere in their product portfolios over the last decade. It will take a long time before an efficient supply chain can be reassembled to make a significant number of jackup rigs efficiently.

### **Management**

Borr was founded by Tor Olav Troim, one of the savviest oil and gas investors of the last few decades, and is today run by Patrick Schorn, formerly a top Schlumberger executive and one of the best operators in the industry. Both are highly aligned with shareholders and intend to maximise Borr's cash flow and return it to shareholders as efficiently as possible.

Troim has a long history of investing in the shipping and oil & gas industries. He has held various positions in the energy/offshore industries, including as CEO of Frontline, Golar LNG, SFL, Seadrill and Northern Offshore. He is a marine engineer by training, and cares deeply about the quality of the assets he owns, but he thinks like an investor, not an empire builder. He has been vocal in encouraging other players in the industry to remain disciplined and return cash to shareholders and intends to lead by example. Today, Troim owns ~7% of Borr and is Chairman of the Board.

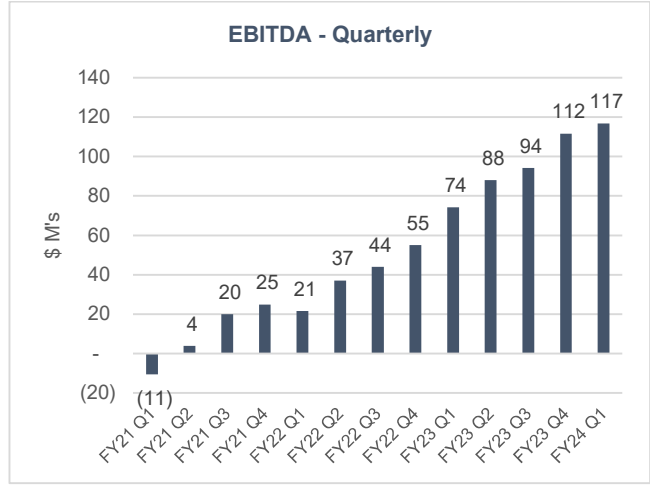
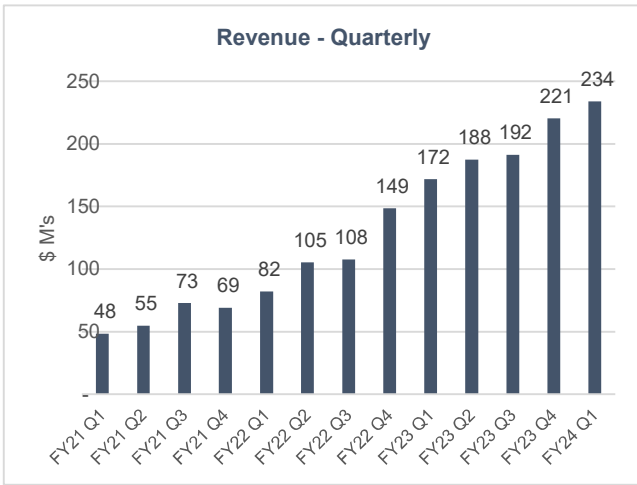
Led by Schorn, Borr's management team is deeply experienced and high calibre. Prior to taking over as CEO in September 2020, Schorn was COO of Schlumberger, where he had spent 32 years. He has been a board member of Borr since 2018, and seeing the extraordinary opportunity unfolding at the company, took the brave decision to step down from his role at Schlumberger to take the helm of what was then a microcap stock. Today Patrick owns ~0.5% of Borr, however, with his options which vest in 2025 & 2027, he owns ~1% of the company. Some (33%) of Patrick's options will only vest should Borr's share price reaches \$10 by September 2025 and remain there for three months.

### **Recent Financials**

Providing a detailed history of returns for Borr is not particularly informative as the company didn't make its first rig purchase until 2017, after which it continued to add rigs to the fleet for the next few years. Just as Borr's rig purchase program entered its final stages, COVID hit.

The pandemic presented unprecedented challenges for the industry with utilisation levels and day rates falling on the back of a shock decline in demand for oil & gas. As much as shallow water production is low cost and resilient, when oil prices go negative and clients are losing money to produce, they tend to halt efforts to produce new hydrocarbons. Despite the completely unprecedented nature of the pandemic, even in 2020 utilisation of modern units did not fall below 75% which demonstrates the resilience of the demand for jackup rigs.

Needless to say earnings throughout the COVID period were poor, with the Group posting EBITDA of ~\$20m in FY20 and ~\$38m in FY21. Due to the high leverage Borr had accrued in its asset build-up, the company went cash flow negative and was forced to issue equity and sell rigs to make ends meet. As the company emerged from the pandemic and utilisation levels have started to climb, so too have day rates, and Borr's underlying performance has improved rapidly and consistently:

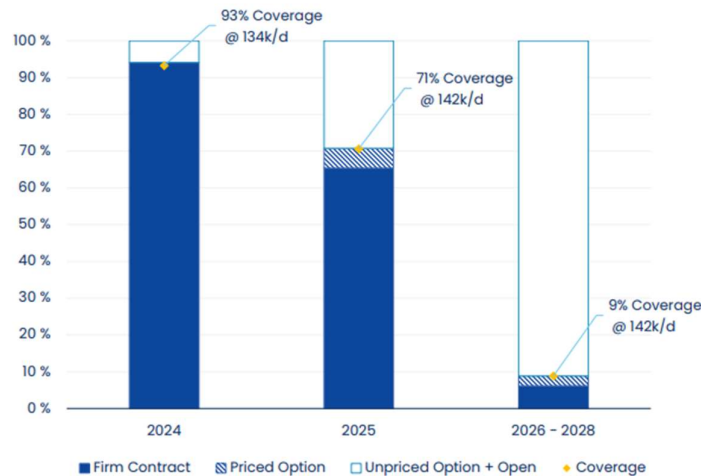


Source: Granular Capital / Company filings

Average backlog day rates increased steadily from ~\$84k in FY21 to ~\$121k in FY22, and ~\$135k in FY23. They have continued to rise since, and in FY24 YTD Borr has been signing contracts at an average of \$184k/day. Alongside the improvement in rates, the expansion of average contract lengths has given the Company greater revenue predictability, and Borr Drilling now has contracts that cover nearly all of their rig years for FY24 and the majority for FY25 as well. This guarantees a minimum healthy level of earnings, whilst also enabling them to benefit from further rises in rates across their remaining capacity.

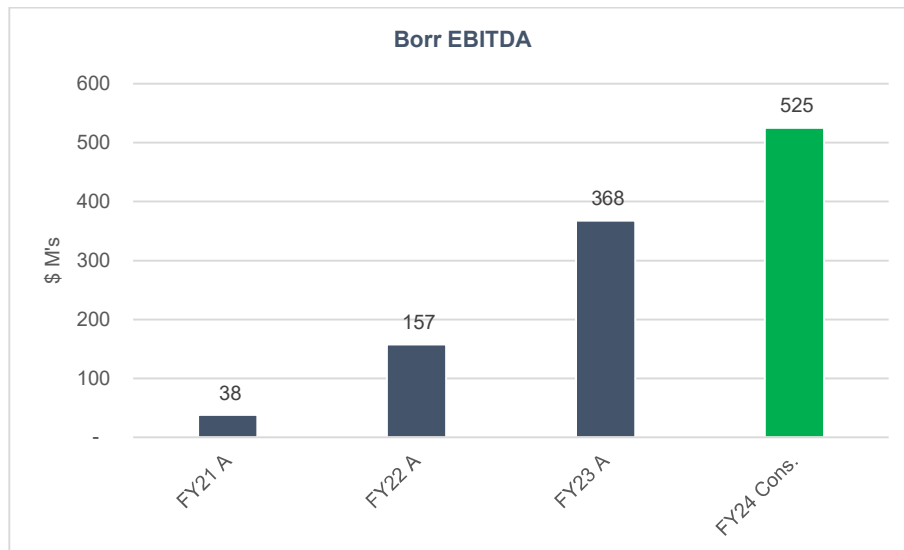
**2024 coverage above 90%**

Available Fleet Coverage (%)



Source: Company presentation

Following on from a couple of years of rapid improvement in profit generation and in light of the constructive supply/demand backdrop, the company have guided towards a range of ~\$500-550m in EBITDA for FY24, and the strong prospect of materially higher earnings power in subsequent years.



Source: Granular Capital / Company filings

Reflecting its desire to return cash to shareholders, as Borr began to generate solid operating cash flow it initiated a quarterly dividend of \$0.05 per share in December 2023, and increased the dividend to \$0.10 per share following the 2024 Q1 results. Borr is currently paying an industry leading dividend yield of ~7%, with the Group also introducing a \$100m share buyback authorisation late in FY23. (No buybacks have been completed under the programme as yet, with Borr first seeking to finalise their capex programme i.e. the purchase of the newbuilds, which will be completed by the end of 2024).

Profitability improvements from now on will result in further increases in shareholder distributions; management have made it clear that their intention is to return excess cash to shareholders.

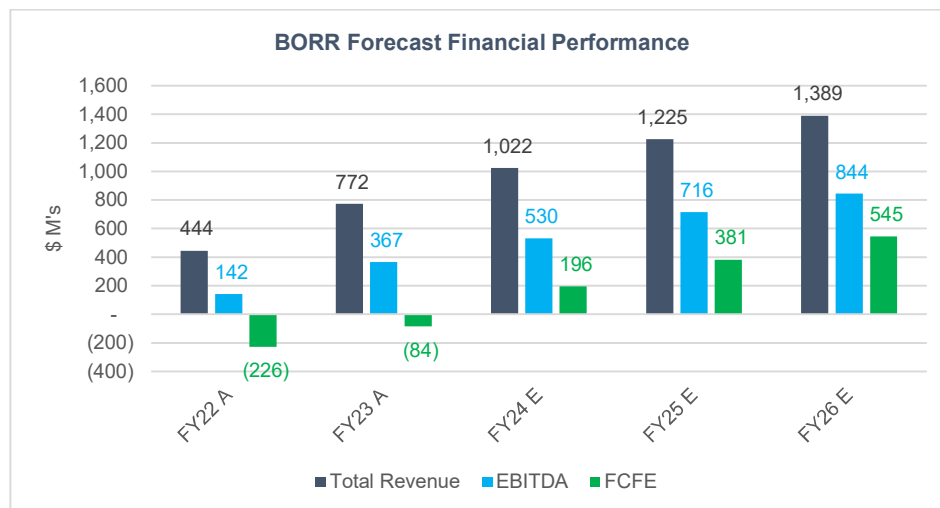
### ***Forecast Financial Performance***

Borr's future financial performance is highly sensitive to developments in day rates and utilization, though we have reasonable visibility for the next couple of years due to the high contracted rate out to FY25.

To project Borr's financials into the future, we roll each rig as it comes off its existing contract onto a market day rate of \$150k in 2024, \$160k in 2025, and \$170k in 2026, with an assumed utilization of ~93% in each year (to account for time to move rigs from one contract to the next). These assumptions compare with Borr's rig utilization in 2023 of 92% and with average day rate secured so far in 2024 of \$184k. We have assumed that the roll over day rates are lower than those currently being agreed by Borr, allowing for significant upside to our forecast if conditions continue to improve.

Using our base case assumptions, we estimate that Borr's EBITDA will grow from \$530 million in FY 2024 to \$909 million by 2027, and to keep growing from there. FCFE increases from \$196 million in FY 2024 to ~\$545 million in FY 2026.

We note that Borr's historical FCF profile to date has been lumpy. Steadily growing operating cash flow from its contracted rigs has been masked by lots of moving parts; as it dealt with the volatility related to COVID, Borr was forced to defer rig deliveries with yards, negotiate with bond holders, sell off rigs under construction, and raise equity. Over the last 18 months, things have settled down considerably, Borr refinanced its debt stack in late 2023 and takes delivery of its last rigs in 2024. From 2025, we expect the cash flow profile to become much more straightforward. With an end to lumpy capex related to new build deliveries, FCFE should track operating cash flow and debt will fall smoothly over time as Borr follows its contractual amortization schedule.



Source: Granular Capital

### Balance Sheet

Borr has gross debt today of ~\$1.8bn which breaks down as follows:

Debt	Date Announced	Maturity	Amount	Principal Remaining	Interest Rate
2028 Senior Secured Notes	Nov-23	Nov-28	\$1,025m	\$988m	10.0%
Additional 2028 Senior Secured Notes	Mar-24	Nov-28	\$200m	\$193m	10.0%
2030 Senior Secured Notes	Nov-23	Nov-30	\$515m	\$503m	10.4%
Convertible Bonds	Feb-23	Feb-28	\$250m	\$239m	5.0%
Deferred Finance Fees / Debt Discount				\$(78.4)m	
<b>Total Indebtedness</b>				<b>\$1,844m</b>	

Source: Granular Capital / Company filings

The Senior Notes have annual amortization and a cash sweep provision. The cash sweep states that if the leverage ratio at the end of a year exceeds 3.0x then 75% of that year's "excess cash flow" must be used to offer to buy back debt at 105c/\$; if leverage is 2.0-3.0x then 50% of "excess cash flow" must be used for this offer, if leverage is 1.5-2.0x then 25% of the "excess cash flow" must be offered. Borr's bonds currently trade at or above this threshold which means that in practice it is unlikely that the bond holders will elect to be repaid at 105c/\$.

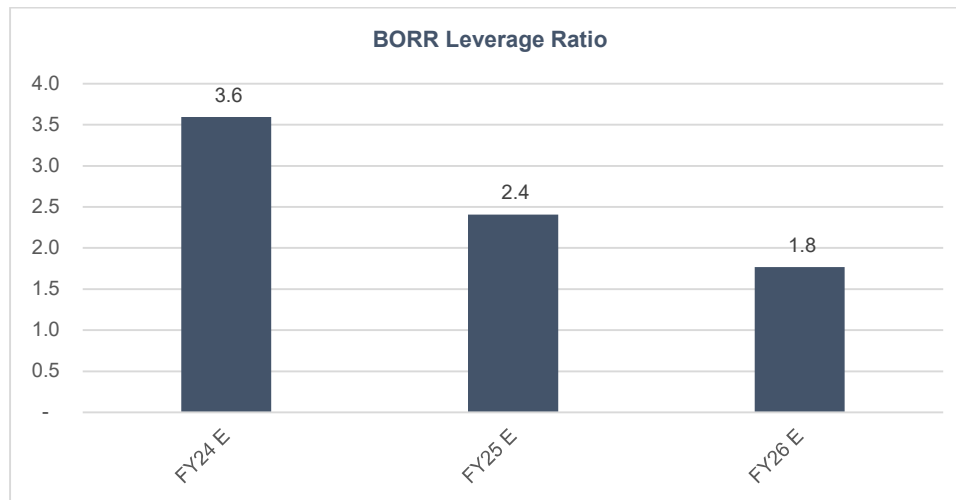
The convertible bond of ~\$239.4m has a strike price of \$7 per share. As the dividend payments grow, the conversion price will be reduced, making it likely that the convert will be in the money before the redemption date of Feb-28.

### Leverage

Borr has a leverage target of ~2x net debt/EBITDA in the near-to-medium term and a longer term steady state leverage target of ~1.5x. At the end of Q2 2024 Borr had cash of \$200 million, and aims to maintain minimum liquidity of ~\$100 million.

We forecast net debt at year end 2024 of ~\$1.9bn, translating to a leverage ratio of ~3.6x. As the fleet rolls onto higher day rates and EBITDA increases Borr's leverage metrics will improve quickly. Using our base case forecasts, we expect the leverage ratio fall to ~1.8x by YE 2026 despite rapidly growing dividend distributions.





Source: Granular Capital

When considering Borr's debt, it is worth bearing in mind that the company has a secured order backlog of ~\$1.9bn which provides some guaranteed cash flow. Another way of looking at the leverage is on a per-rig basis: Borr has a net debt per rig of approximately \$70m, which compares comfortably to replacement costs of \$ 300 million or its EV/rig today hovering around \$120-140 million.

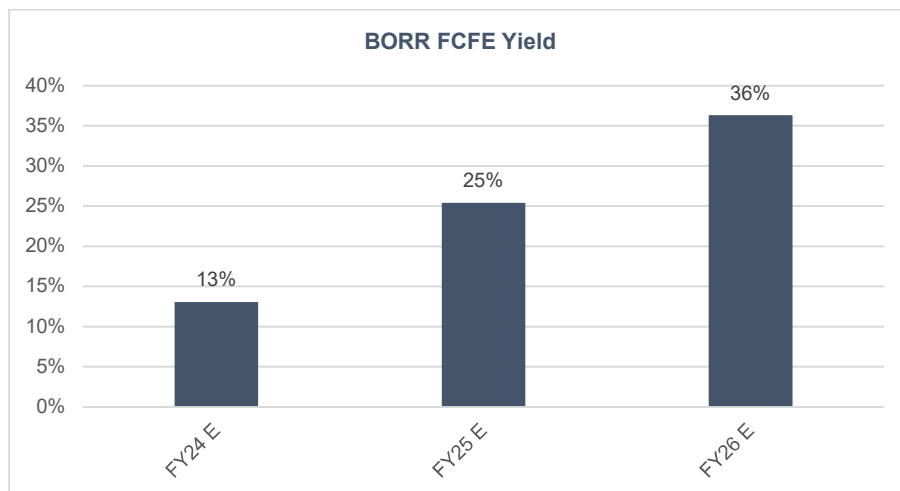
### **Valuation & Expected Returns**

#### *Attractive FCF yields and scope for significant cash returns*

Borr looks attractively valued any way we look at it. Using our base case assumptions, the company will generate FCFF of \$575 million in 2025 and \$705 million in 2026, and FCFE/mkt cap yield (equity yield) of 25% in 2025 and 36% 2026. Given the supply/demand picture discussed above, we are optimistic about the development of Borr's cash flow long into the future. As footnoted above, our estimates for Borr's FCFE are before debt repayment to properly reflect the value accruing to equity owners.

Capital returns are only just starting, and we expect them to grow meaningfully. Dividends are unusually attractive here due to the low tax rate provided by the company's Bermuda domicile, and we expect them to form the bulk of capital returns going forward (as noted, some FCFE will go to amortizing debt too but these should be equity accretive).

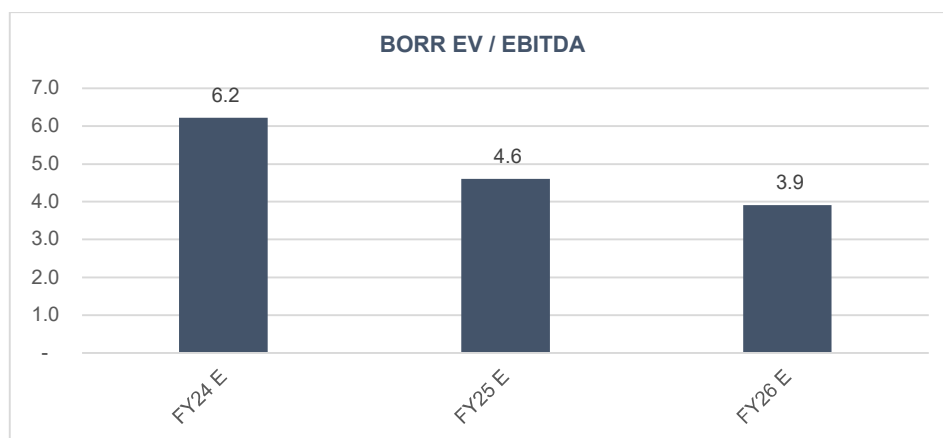
If we are roughly accurate about Borr's FCFE progression in coming years, they should be in a position to return more than the current market cap to shareholders in just a few years. As discussed, we expect this high level of payouts to be durable long-term, providing a highly attractive cash flow stream.



Source: Granular Capital

### *Compelling relative valuation*

When we look at Borr's valuation relative to its peers in the Middle East, the company appears very cheap, despite its superior fleet, management, operations and international footprint. We estimate that Borr trades at less than 4x EV / FY26E EBITDA today, whereas ADES, ADC and Adnoc Drilling all trade at ~9x EV/EBITDA. Given Borr's leverage, this implies Borr's equity has upside potential of close to 300% from re-rating to peer multiple levels.

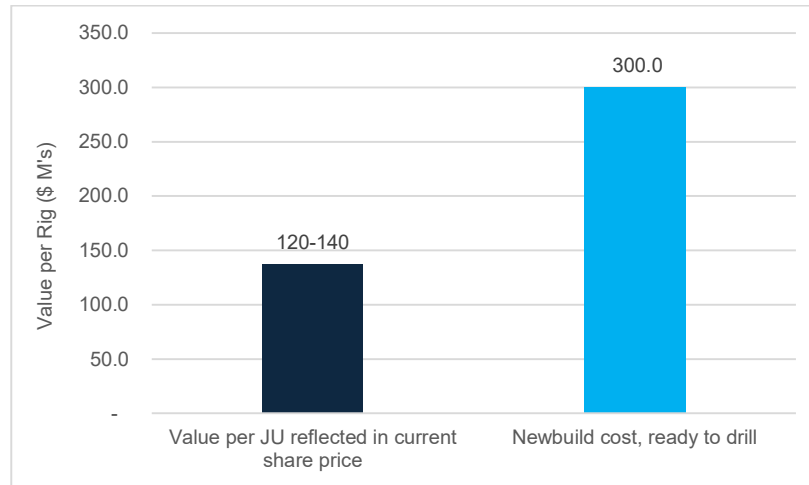


Source: Granular Capital

### *Attractive Discount to Replacement Cost*

Borr's current EV suggests a value per rig of around \$140 million. If we crudely assume that the company should trade at close to the replacement cost of \$300 million per rig, it implies an enterprise value of \$7.2 billion, or an equity value of \$5.4 billion. This also implies close to 300% upside to the current market capitalization.

This is obviously a crude analysis. If we put more emphasis on this analysis, we would have to add in the cash flow that Borr will generate while a new rig was in construction, and factor in the risks of time and cost over runs that are involved in any new build project. This would tilt the analysis more firmly in Borr's favour.

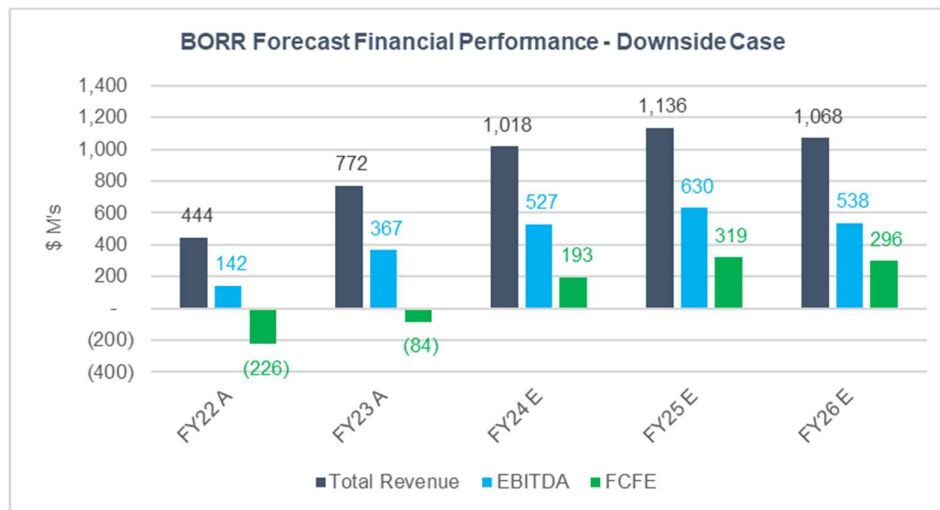


Source: Granular Capital

### Downside scenario – Borr is resilient to a prolonged period of weak day rates

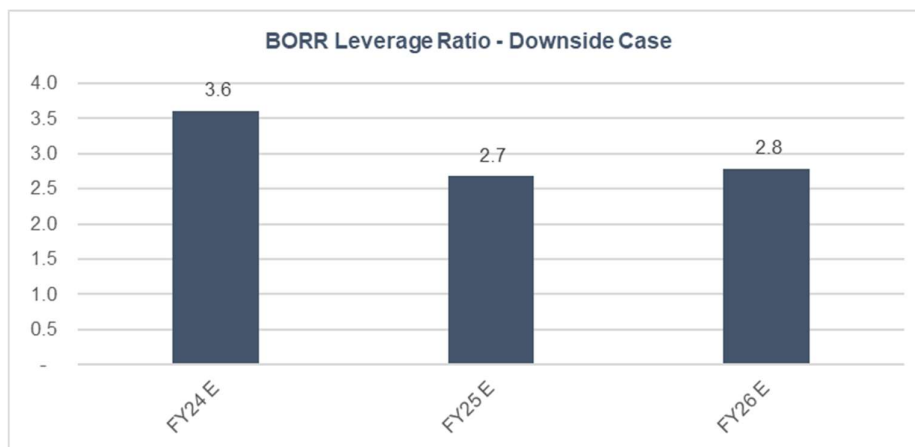
In our downside scenario, we assume market day rates fall 20% immediately and do not recover. We model that from today, as Borr's rigs come off contract they roll onto new contracts at \$125k (after a one month idle period with no revenue and full operating costs). We believe this scenario is quite conservative given \$125k is 45% below the rates Borr has agreed so far in 2024. All other assumptions are consistent with the Base Case except the fact that we assume the quarterly dividend remains at \$0.1/sh per quarter (or ~\$105 million per year).

In this downside scenario, Borr's EBITDA grows slightly from \$530m in FY24E to \$538m in FY26E as the compression in day rates (from \$135k weighted average fleet day rates in-place today) is more than offset by the incremental EBITDA generated by the two newbuild rigs delivered in 2024 that will start working in 2025. We expect Borr's FCFE yield to increase from 12% in 2024 to 20% by 2026.



Source: Granular Capital

In this downside scenario, net debt falls to 2.8x EBITDA by FY26E. Despite this paying down considerable debt (via contractual amortization and the cash sweep provisions), Borr is able to maintain its current quarterly dividend of \$0.1 throughout the forecast period and ends 2026 with a healthy cash balance of ~\$180m.



Source: Granular Capital

To give a sense for the resilience of the company, in this downside scenario we expect Borr to end 2028 with net debt of \$1.1 billion. That level of debt would equate to \$46 million per rig or 2.1x 2028 EBITDA of \$522 million. It is hard to believe the company would struggle to refinance that level of debt even in a difficult financing market. Indeed, with those metrics it seems likely that Borr would be able to improve on its current cost of debt (~10%). It is also important to reiterate that in this scenario we are modelling that Borr deleverages *while continuing to pay dividends at a rate of ~\$105 million per year* (\$420 million in dividends paid out 2025-2028).

#### **How this may look in 5 years' time – the unusually high chance of a multi-bagger**

Though we are by nature cautious of any scenarios with exceptionally high returns, and while we by no means need the following to play out in order to be very happy with our investment in Borr Drilling, we see a reasonable likelihood that the situation here results in a true multi-bagger, and would be remiss not to include it here. If we assume that day rates rise over the next 5 years to the level required to incentivise the construction of new rigs – a not improbable situation – and Borr rigs consequently trade at newbuild replacement cost, then the total return could be somewhere in the region of 5-6x. With day rates rising to \$ 200k per day in 2028, the FCFE before debt amortization (as deleveraging comes from EBITDA ramp) would alone be \$ 3.2 billion over the next 5 years, equating to more than 2x the current market cap. At that point, Borr would then have a rapidly growing cash flow stream from industry-leading assets in a supply-tight and booming market, which would likely be reflected in a significant multiple re-rating towards newbuild parity. If we assume that it trades at \$ 300m per rig, then we have an EV of \$ 7.2 bn and a market cap of \$ 5.4 bn, or 3.6x the current, and when combined with the cash flow generated, the total shareholder return is somewhere in the ballpark of 5-6x vs current.

To reiterate, if Borr's premium day rates fall from here and plateau at mid-cycle levels of \$ 150k for the long-term, you still get a dividend stream around 15-20% annually vs the current share price while proactively paying down debt to de-leverage the business, and that stream of earnings would last for the remaining life of the assets, or over thirty years for the fleet today. As the assumed day rates aren't nearly high enough to encourage new rig construction, we wouldn't see new supply coming in to push down returns. We believe, however, that this situation is unlikely to play out as we have never heard of such an annual cash stream not being competed away therefore would expect the stock to re-rate to effectively reduce the yield to more normal levels, boosting returns.

#### **Key risks to the thesis**

Given Borr's low valuation vs replacement cost and its very high prospective cash flow yield, combined with the attractive supply/demand dynamics of the wider industry, we believe the chances of losing money here are low on a >5yr view. The high current utilization in the jackup market, mid-cycle day rates, and lack of new supply provide strong support for Borr's cash flow; together with the low current trading price of Borr's shares we believe the situation has meaningful downside protection.

If we do see permanent capital loss, however, we think the likely causes could include: further rig suspensions from Saudi Aramco, OPEC reducing output, major additional oil supply coming to market, new rig supply growing more than expected, or re-financing issues.

#### Rig suspensions from Saudi Aramco

The Middle East has led the market in terms of jackup demand in recent years with Saudi Aramco being main driver. Aramco increased their rig count dramatically from ~50 in Jan-21 to ~90 by Oct-23, with this sudden increase coming after Saudi Arabia pulled forward their plans to increase its Maximum Sustainable Capacity (MSC) to 13 million barrels per day by 2027, rather than 2030. The decision to accelerate the MSC increase came in response to a sharply rising oil price as the world emerged from COVID.

In 2024, Saudi Aramco was producing only 11 million barrels a day while the oil price languished around \$70/bbl. The US had counter-intuitively reduced sanctions on Venezuela and Iran, adding ~1.5mm barrels to global supply, while draining its own strategic inventories, and there appeared to be no immediate need for Saudi Arabia to increase capacity so much and so quickly. In January 2024, Saudi Aramco received a directive to leave its MSC at 12 million barrels. In response, Aramco has suspended 27 jackup rigs, adding unexpected supply to the market and spooking investors. Of these rigs, only 22 are modern units, of which 5 are not being marketed outside of Saudi Arabia. The net result of this has therefore been that 17 rigs entered the competitive fleet outside of Saudi Arabia. This effectively reduced utilization of the modern fleet by around ~5%.

The suspensions were largely served to Saudi-backed operators (ADES, ADC and ARO), who quickly obtained permits to move their rigs. Many of these rigs have now been contracted in South East Asia, which has led to greater competitive intensity in the region, depressing day rates locally.

As a reminder, Borr only has two rigs working in Saudi Arabia, so the risk to Borr is that increased competition outside of Saudi Arabia reduces the day rates it can secure rather than the financial impact of the suspensions itself. So far, Borr has been able to navigate the impact of these rig suspensions thanks to strong day rate momentum in other regions. It bears repeating that one of Borr's rigs – the Arabia I – was served a suspension notice from Saudi Aramco in April 2024, but just three months later the company had re-contracted the rig in Brazil at a 60% higher day rate than it was earning in Saudi Arabia.

In a nutshell, as jackup demand increases across the globe, operators elsewhere are seeing Aramco's suspensions as the opportunity they needed to secure supply, something which they were not fast enough to do when emerging from the pandemic.

In spite of the suspensions, modern rig utilization has remained above 90%, with regions outside of Saudi Arabia quick to benefit from the additional supply coming to the market. Thanks to its international footprint, Borr has so far proven resilient to the short-term market pressure resulting from the cancellations.

Most operators believe Aramco's suspension program is finished, with Aramco recently awarding new contracts to rigs which were due to roll off. It is possible that Saudi Aramco will suspend more rigs. There must be a limit to how quickly rigs can be absorbed without an impact on prices, so further suspensions might dampen the market. Nonetheless, given how quickly the previous rigs have been absorbed, it seems reasonable to assume that downward pressure on rates and utilization from further suspensions should be relatively manageable.

#### OPEC+ cuts

In Nov-22, OPEC+ pledged to curb production by 3m bpd in response to the fall in the oil price, which was exacerbated by unprecedented releases from the US Strategic Petroleum Reserve (SPR). From 2022 to 2024 the US reduced its SPR by ~40%, helping to reduce the impact of oil breaching \$100 a barrel. The OPEC+ decision to cut production has led members to scale back output with many below their recent averages, and the production curbs are expected to be extended into 2025.

Jackup demand is correlated to production capacity rather than production output per se in the very near term, in a way that marginal swings in policy should not impact the day to day running of this business and contracting the rigs

in the market. Moreover, OPEC+ has made it clear these voluntary reductions can be halted or reversed at any time if market conditions necessitate it.

We obviously can't rule out additional production cuts, but there is a limit to how far output can be reduced given the reliance many member states have on oil revenues. Further, even with the recent cuts, modern jackup demand remained resilient. Utilisation remained above ~90% throughout as most clients are planning their production schedules many years out and domestic oil demand continues to climb in most producer countries.

#### Major additional oil supply coming to the market

One of the main threats to Borr comes from a major new discovery of reserves, or from currently underexploited or restricted capacity coming back into the market in a big way. A flood of incremental supply would probably impact the oil price, which would in turn likely pressure demand for rigs.

The boom in US shale production, which has added ~8 million barrels per day to global supply since 2010 was the primary cause of the 2014-15 oil price crash (the other cause was OPEC's attempt to break the shale industry by crushing oil prices). The increase in supply from shale and ensuing price war precipitated a very rough patch for jackups. We cannot rule out the possibility of another discovery of the magnitude of U.S. shale, although we do believe the probability seems slim, particularly given the low levels of exploration capex in the hydrocarbon energy industry today.

It is also important to note that the US shale revolution did not occur overnight; it required decades of experimentation, followed by the uniquely American combination of the (over-)abundance of cheap capital, entrepreneurial endeavour, technical know-how, and brute force. Although there is plenty of shale resource around the world, it is hard to imagine how the shale revolution could be replicated anywhere else and we place this risk fairly low down our worry list.

A more probable downside risk comes from known, but currently restricted production capacity entering the global market in significant volumes. There are huge hydrocarbon reserves in Venezuela, Russia, Iran, Iraq, and Libya, to name a few, that are not being fully exploited and/or entering the mainstream market due to a variety of geopolitical restrictions. If this were to change and meaningful new capacity were to enter the market, it could precipitate an oil price crash and / or reduce production from shallow water oil reserves and reduce demand for jackups (importantly, none of the countries above are major users of jackups today).

While this is a risk, we have actually had a dry run of this scenario in the last couple of years – Russia is still selling large volumes of hydrocarbons to global markets and Venezuela and Iran between them have added almost 1.5 million barrels of oil production per day to global supply in the last couple of years. Of course more supply could come from these markets, but would likely take some time to scale up production significantly from current levels and to be incorporated into global markets. It is therefore likely that any negative impact on the jackup market would arrive over time, rather than resulting in a precipitous reduction in jackup utilisation and day rates.

#### New rig supply growing more than expected

Another potential source of downside in the long run is if our assessment that supply additions will be constrained in coming years is wrong, and a meaningful number of new jackups are built. Whilst no orders have been placed in a decade, as day rates appreciate and contract terms lengthen, the returns on newbuild orders will begin to appear more palatable.

Yard capacity will likely remain a limiting factor for the foreseeable future, with many tier 1 yards fully booked for years making other types of vessels. But a hypothetical buyer could pay up for yard capacity or seek to engage a tier 2-3 yard, risking quality but securing capacity. Additionally, NOCs tend to have a low cost of capital and may be willing to underwrite newbuild orders at low returns if they see jackups as strategic assets.

While it is possible that new orders are placed at some point, this is not a binary risk for Borr given the starting point in the market. If we imagined someone commissioned construction of five new rigs per year starting in 2027 (a fairly ambitious assumption from where we stand today), it is likely that the existing jackup fleet would still shrink over the medium term given retirements of older rigs.

We do not view modest levels of new construction activity as a major risk to the base case thesis. Given demand growth, the market should be able to absorb a handful of new rigs per year without impacting day rates significantly.

As long as day rates remain at or around mid-cycle levels – with the market therefore telling us that there is no significant shortage of jackup rigs – it seems hard to imagine that we will ever see huge orders of new rigs placed that dramatically alter the supply/demand picture in the market.

Of course, if day rates ever reach the level that stimulates large newbuild orders, Borr will be making a lot of money, and will likely trade at a very different valuation versus replacement cost than it does today.

It is possible that Aramco will start building its own jackup rigs. In 2017 Aramco started a joint venture, IMI, with Lamprell (then a small UK-listed offshore EPC company), Hyundai Heavy Industries, and Bahri (the national shipping carrier of Saudi Arabia with a fleet of VLCCs and chemical tankers). IMI is envisaged to be the Saudi Arabian “national champion” maritime construction yard. So far, this yard has produced only one jackup rig that was many years delayed, and Lamprell effectively went bankrupt in 2022. In its marketing materials, IMI states a maximum capacity of four drilling rigs per year and seems to be focused on building VLCCs and other shipping vessels.

So far, new supply from IMI does not appear to be a major threat to the jackup market. It seems unlikely that IMI’s jackup ambitions are viewed as a priority for Saudi Arabia today. Saudi Arabia appears to be doing everything they can to diversify away from oil and gas – they are building solar farms and electrolyzers. They want to become significant players in green ammonia and are building new cities in the desert. Aramco just suspended 27 jackups. It seems unlikely that – unless they believe the jackup market is worryingly tight – Saudi Arabia would be interested in scaling up an effort to build jackups.

#### Financial leverage

Borr Drilling carries a significant amount of debt. As noted, this leverage is not particularly high when compared to current rig values and especially not versus rig replacement cost. The leverage is also relatively low when compared to the earnings power of the rigs in today’s market environment. Nonetheless, we acknowledge that Borr’s financial leverage comes on top of the natural operating leverage in the business which enhances the risk of a prolonged period of low day rates.

Borr has stated that it views a debt value of \$50 million per rig as sustainable through even severe market downturns. With the current amortization provisions, we expect that by the end of 2027 (first debt maturity is in 2028), Borr’s senior secured notes will have reduced to \$1.2 billion, or below \$50 million per rig. Cash interest at 10% on this debt would cost \$5 million per year. Assuming day rates of \$100k per year and the unit economic assumptions on page 5 above, a rig generates FCF of \$14.5 million per year which is plenty to service the debt at \$50 million per rig and still leave significant cash flow left over to further pay down debt or pay out to equity holders. Either way, it seems reasonable to assume that Borr should be able to refinance its debt at \$50 million a rig in 2028, even in a low day rate environment.

#### Closing remarks

All in all, we believe the Borr Drilling investment strikes the right balance of dramatic upside with resilient downside protection. Borr Drilling’s operational execution over the last few years has been exemplary. This has driven consistent improvement in cash flow from operations and excellent returns on the capital invested in its existing assets. This solid operational execution has been masked by the cash flows associated with taking delivery of new rigs, and with managing a balance sheet strained by the difficult COVID environment. With the balance sheet refinanced in 2023 and rig deliveries ending in 2024, from 2025 Borr will become a much simpler story. We fully expect that the company will be rewarded for all its hard work with a higher valuation multiple placed on a rapidly growing stream of earnings. Further industry consolidation and/or asset retirements would likely bring this reality forward, while the growth in day rates and free cash flow will force investors’ understanding of the quality of the asset when compared to alternatives. We believe after years of building a consistent track-record, it is time for Borr Drilling to handsomely reward its shareholders.