Oil & Gas Industry - Key Success Factors

BUSINESS RISK ASSESSMENT

Quality of Reserves and Replacement Strategy

The analysis covers the company's existing proven and probable reserves, its quality and replacement strategy. Acknowledgment of reserve must be certified by a credible and independent appraisal. The assessment on life of reserve and its quality are key factors used to determine the company's growth strategy, capital spending and future business performance. Replacement strategy will be more crucial for player with mature reserve.

Diversification

Diversification is crucial to reduce business risks including anticipation of the fluctuation of oil price. Following the long-term contract with the buyer for gas, a company that is able to produce oil and natural gas should have better revenue stability than the one that is exposed to high business interruption risks. Spread-out location of oil and gas reserve may help to lower business interruption risks.

Cost Position

The analysis covers the company's lifting cost and finding cost. Those costs vary depending on the location and availability of infrastructure. A company with cost position advantages can mitigate oil price fluctuation and generate profits.

Operating Management

The analysis covers the company's human resources, infrastructure, productivity, drilling success rate and cost structure. Condition and utilization of the equipment and the integration of technological improvements will also become important factors to achieve the company's degree of efficiency in its operational activities. The analysis on operating margins (EBIT and EBITDA) is also assessed by comparing the company's ratios with other players in the same industry or other industry with similar characteristic, which is important in analyzing the company's competitiveness. The analysis is helpful to measure operating efficiency.

FINANCIAL RISK ASSESSMENT

Financial Policy

The analysis includes a review of management's philosophy, strategy and policies toward financial risk (historical, current and future). It also includes examination of management's financial targets (growth, leverage, debt structure and dividend policy), hedging and other policies in an effort to reduce the company's overall financial risk (historical vs. future). The company's track record on fulfilling its previous financial obligations is also examined to determine the degree of its commitments and willingness and consistency to pay obligations on a timely basis.

Capital Structure

The analysis covers careful examination of the company's historical, current and projected leverage (total and net debt in relation to equity and EBITDA), debt structures and composition (rupiah vs. foreign currencies, short-term debt vs. long-term debt, fixed rate vs. floating rate). Management of its liabilities is also thoroughly reviewed.

Cash Flow Protection And Liquidity

The analysis covers thorough reviews of the company's cash flow generation and capability to meet its short-term and long-term financial obligations. The degree of its debt-servicing capability level is measured by the company's interest and debt coverage ratio. The degree of its liquidity in fulfilling its short-term liabilities relative to its sources of cash is also thoroughly assessed. The sources of cash are assessed, which include cash balance, estimated cash from operations, unused credit facilities, and other sources of cash. The uses of cash other than short-term liabilities, such as capital expenditure, are also assessed.

Financial Flexibility
The analysis covers combined evaluations of all the financial measures above to arrive at an overall view of the company's financial health. Analysis of other related factors or figures that are not specifically examined above, such as insurance coverage, restrictive covenants in loan/bond agreements or parental linkage and support, are also covered. Other analytical tasks covered are the evaluation of the company's options under stress, including contingency plans and other capabilities and flexibility to deal with various adverse scenarios. Shareholder support and commitment are also greatly considered.