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Ocean Yield (OCY NO, OYIEF) Update on FPSO Maintain NEUTRAL

We are maintaining a NEUTRAL Rating as the company announced an extension of the option for the FPSO vessel with Aker Energy until September 1st. That does ensure the FPSO will generate some income and cash flow in 2Q19 and 3Q19. If terms remain the same ($50,000 per day), it adds about 3-cents to 2Q in EPS and 2 cents for 3Q.

Aker Energy has submitted a revised plan to Ghana for development of a multi-year deepwater drilling project. It expects to get feedback from the government and expects to receive final approval in the 3Q19. Also, in the news, Aker is exploring the use of an FPSO from SBM Offshore or Yinson on the project, which may be bad news for Ocean Yield.

There are multiple reasons to still expect Ocean Yield's ship to be used. Aker owns 49% of Aker Energy and 61.7% of Ocean Yield. Also, the project expects to be producing oil within 35 months of final approval. That gives ample time to modify the Ocean Yield FPSO. It is debt free as well, so it is not costing anything during this time. It should also help Ocean Yield stock and bolster the dividend coverage for the largest investor.

Ocean Yield is also marketing the ship to other projects that are starting up as well. It believes it should be able to resolve the matter by 1Q20, which is essentially the time-frame we have been targeting. We actually think by then; a new deal will be in place or the ship will be sold.

We have believed that 2019 would be the transition year and there is enough cash and liquidity to sustain the dividend until the FPSO situation is concluded. However, if there is no deal or sale of the vessel, the dividend would likely need to be reduced. The company indicated that if neither solution is in place by then, it may adjust the dividend down to 15-cents per quarter from 19.1 cents. That would save the company about $6.5 million per quarter ($26 million annually) in dividends and create a sustainable situation with an idle FPSO. The dividend yield would be 9.1% vs. the current 11.5%.

Longer term, we still believe the FPSO situation will reach an end and not remain an idle vessel for Ocean Yield in 2020 and beyond. It's on the books for $232 million and is debt free. It has already had an impairment charge in late 2018 when Reliance did not exercise the purchase option. Even if it is sold for $100-$150 million, we believe Ocean Yield can leverage that capital 4-1 and invest in new ships worth $500-$750 million. It has been earning double-digit rates of returns these deals and should be able to produce more than $26 million annually to cover the potential dividend reduction. For example, the company's 49.9% equity investment in 6 containerships cost $162 million and is producing equity income of $5.7-$6.0 million per quarter.

If Aker signs a long-term deal on the FPSO it is expected to be a double-digit rate of return on $232 million plus $200-$300 million of modifications made and financed by Ocean Yield. That again should be a figure higher than the $26 million discussed above.

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