Case Study of Tidewater and The Capital Cycle by John Chew

Tidewater **(TDW- $**6 on **March 17, 2020**, $315 million Enterprise Value, EBITDA of $15.3 million) offers an asymmetric risk reward opportunity for investors who can understand:

- this deeply cyclical industry. An investor must relate *Tidewater* to its environment.
- what *Tidewater's* clean balance sheet of only $61 million of net debt (debt of $279 – 218 million of cash or 24% net debt to market capital using a $6 price per share as of March 17, 2019 and 42.4 million fully diluted shares) allows management to further consolidate a depressed industry at its trough while almost all its public competitors are distressed with zero equity values. Those circumstances offer *Tidewater's* management a strong strategic but *temporary* advantage.
- that *Tidewater's* assets are trading perhaps at 1/8 to 1/10th of their replacement value, and--while the market may further deepen the discount between the market price and replacement value during the current market dislocation—it shows the potential opportunity. Replacement values will be relevant when and if the industry can return to its normal economic returns of 45% to 50% vessel operating profits. Currently, replacement values have no bearing on market prices because the entire industry is distressed. Replacement values indicate the price of new supply.
- management has had successful experience consolidating the industry during the industry's last major trough of 1982 to 1990. Some industry participants *(The Cajun Mariner)* consider this the worst downturn in the 65-year history of the OSV industry. "Too many ships, too much debt, and too many managers."
- the current perceived oversupply of 1,200 boats may be overestimated by the market because of the deteriorating economics of returning vessels to service and the length of layups. Vessels are rusting in place.
- institutional shareholders such as *Robotti & Co., Third Avenue Value, Moerus,* and *Raging Capital* are all experienced small cap investors who can protect the interests of long-term shareholders.
- the necessity to be a long-term (three-to-five year) shareholder who is not adversely affected by price volatility and who *will sell* when capital becomes available for building new vessels. When capital returns aggressively to this cyclical industry, will be the sign to exit.
- that the offshore oil and gas industry *must* resume projects to replenish dwindling reserves while onshore tight oil and gas (fracking) declines rapidly in supply due to capital constraints and less Tier 1 acreage.
- Conclusion and Summary on page 41.

The Capital Cycle

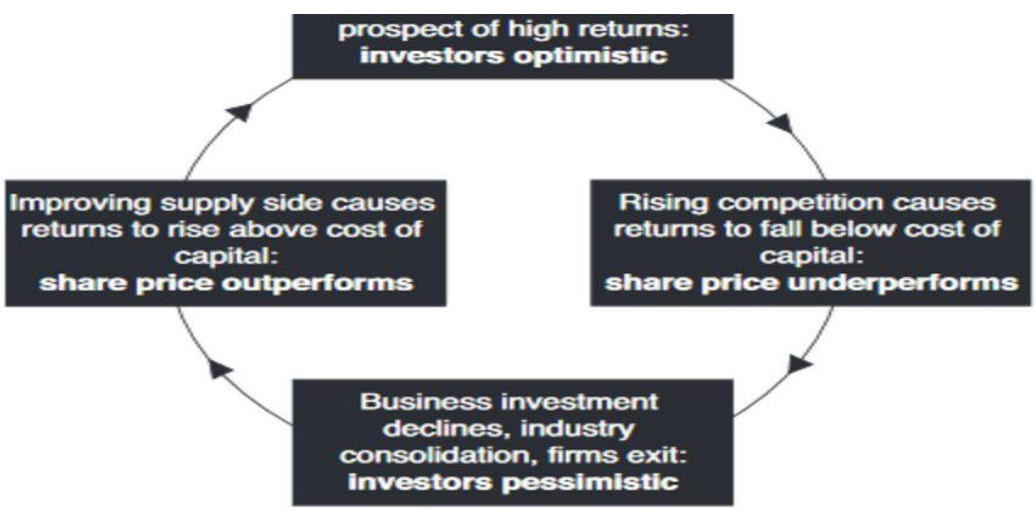
Since the Offshore Support Vessel industry ("OSV") is deeply cyclical because the vessels are capital equipment—vessels built new cost about $30 to $60 million--that service offshore oil and gas drillers who, in turn, are highly capital intensive and these customers base their spending plans on input costs to find and extract oil and gas and the expected price for their commodities. OSVs are a second derivative of offshore exploration and development activity. There are no barriers to entry in this commodity-based business except for capital constraints in a trough of the capital cycle like today.

Let's go through the capital cycle diagram below starting from the left side moving clockwise. Improving supply allows for returns to rise to the cost of capital. Equity prices begin to ascend, analysts raise their earnings forecasts, growth investors take notice.

Returns go above the cost of capital, momentum investors pile in, the high current profitability often leads to overconfidence by managers, who confuse the robust industry conditions with their own skill. Investors and managers extrapolate the good times. The high profitability loosens capital discipline in the industry.

Capex expansion shown by capex greatly exceeding depreciation leads to more supply and competition. While investors are cheering expansion, returns begin to fall below the cost of capital and the share price underperforms.

The capital cycle turns down and bottoms as excess capacity becomes obvious and past demand forecasts are shown to be overoptimistic, profits collapse, losses mount, management teams are changed, capex is slashed, and the industry starts to consolidate. The reduction in investment and the contraction in supply allows for a recovery of profits. The full cycle can take years or decades. Since 2014, the OSV industry has been in contraction and is—I believe—with the double whammy of an oil price war and Covid-19 Virus pandemic close to a trough within the next few months if not year.



The capital cycle illustrates the cyclicality of markets and reversion to the mean.

To understand the capital cycle approach to investing, I recommend these video interviews:

- Edward Chancellor Interview on the Capital Cycle
- Follow the Capital Cycle Part 2 Chancellor

Read: *The Behavior of Aggregate Corporate Investment Sept 2014 Working Paper*

The book, *Capital Returns, Investing Through the Capital Cycle: A Money Manager's Reports 2002-2015* is suggested

The Capital Cycle and *Tidewater*/OSV Industry

To learn from a successful OSV entrepreneur who has three decades of successful experience, I suggest reading all of Mr. Charles Fabrikant's Letters to stockholders of *Seacor Holdings, Inc.* Start with 2001's Letter and read up to 2016's Letter. *Seacor Holdings* spun-off *Seacor Marine* in 2017. Mr. Fabrikant managed to average about a 14% to 16% return on capital while the industry earned half that rate and only during the upside of its cycle. In other words, the OSV industry does not earn its cost of capital over its full capital cycle. See page 9, **Alix Partners Sept 2019 Report This Rising Tide Won't Float All Boats**

Darkening Clouds appear in 2013 as OSV supply ramps up. Mr. Fabrikant writes in his 2013 Letter:

> The Outlook: Tomorrow Cloudy with Patches of Sunshine; Long-Term Forecast: Likelihood of Rain and Possible Storms.
>
> As of our most recent survey, there were 78 mobile drilling offshore rigs working in the U.S. Gulf of Mexico, 45 in deep-water, and 33 on the "shelf." This compares with 72 rigs currently in 2013. Although additional rigs will be arriving in the U.S. Gulf, many of those presently working have contracts ending later this year. Until these rigs are re-engaged, **it is difficult to feel confident about the last quarter of 2014 or 2015.** Most of our vessels in the Gulf of Mexico, particularly those with the highest potential earning power, do not have long-term contracts and live "hand to mouth." We estimate that there are about 50 additional large PSVs under construction in the United States. **This robust order book could portend a thunderstorm or a Category 3 event a few years from now** *(New supply will enter in about 18 months).* Approximately 405 U.S.-flag PSVs could be available, assuming no attrition in the fleet. One of the safety valves for U.S. operators in past years was the option to position equipment into international markets, which now seem to have an adequate supply of large PSVs. There is also ample shipyard capacity to meet potential increased demand in short timeframes. Chinese shipyards are now reliable suppliers for new equipment. One can order a PSV from a Chinese yard that would be roughly comparable to "industry standard" for about **$30 million to $34 million**, $10 million to $15 million less than the tariff at most United States yards. **The cost in Europe could be $55 million to $60 million**, and, in Brazil, possibly more. Although Chinese yards do not command "designer label" prices, their vessels do the job.
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> The storm arrives in 2014 as Mr. Fabrikant compares the current decline 2014 - ?? in his 2014 Letter:
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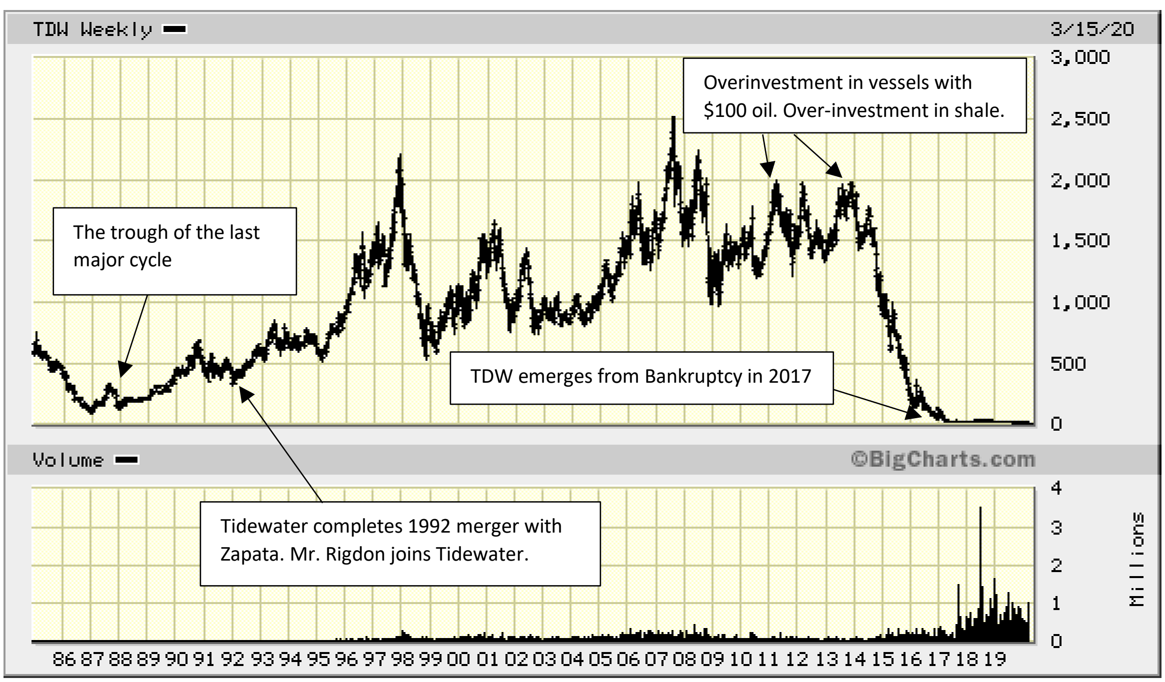
> *SEACOR* marked its 25th year in business this past December. The *SEACOR* of today is an evolution of an opportunistic "leveraged buyout" of a local Gulf of Mexico business that operated supply vessels in

the United States, and a few small tenders in Nigeria. Conditions in the oil patch were difficult, and **the outlook then, not unlike that of today, was uncertain and sentiment negative.** The industry had plunged into an abyss in 1982-1983, and there **was no "APP" for calculating how long it would take to climb out.** The offshore vessel sector was struggling with significant excess capacity. Eager investors, subsidized by tax incentives and captivated by a good "story," and ambitious operators, desirous of expanding their fleets, had binged on work boats anticipating a surge in activity following the commercialization of North Sea oil, and the deregulation of natural gas prices in the United States, and a multifold increase in the oil price in the wake of the regime change in Iran. Even interest rates ranging from 12-20% failed to deter investment!

<u>In his 2015 Letter he explains the dire OSV industry conditions</u>:

As previously noted, this offshore typhoon was not unexpected. A meaningful downturn seemed likely to spawn a welcomed opportunity to benefit from our conservative balance sheet. I should have kept in mind the adage, "Be careful what you wish for, you may get it!" History does repeat. With apologies for repeating last year's letter, **today's depression in the offshore marine sector conjures up 1985–1987**, the dreariest years of the lost decade, 1985–1995. (OPEC's bickering reminds me of the 1974–1977 years.) **There are too many shipyards, too many operators, too many vessels, and too much debt, the hangover from $100 oil and irrational exuberance.** There would likely have been considerable excess capacity plaguing most of the offshore vessel business even if the price of oil were to have remained at a more "respectable" level. Vessels (and drilling rigs) now compete for scraps of work. Most are living on a subsistence diet. **Consolidation of operators and equipment is almost certainly inevitable.** The question is: **How much pain will precede it; how long will it take to work through the reorganizations?** Cancellation of orders for new equipment is also almost certain.

Tidewater's **History**



On page 30, *Tidewater's* 1998 to 2016 financial history, you will note that from 1998 to 2010, *Tidewater* had a debt to equity ratio of only 11%. As of December 2019, *Tidewater's* debt-to-equity ratio is ***27.5%*** ($279 mil. of debt/1,014 mil. of equity). However, *Tidewater* has only $61 mil. of net debt with the majority coming due in August of 2022. The company is much less levered than its competitors as we will see on page 39. *Tidewater* could generate about 15% to 25% cash flow returns from operations on its equity which is a fair return. Note the downturn in 2008/09. The business is cyclical.

Valuation

As a rough proxy for value, **TDW traded between one-time to two-times book value for 16 years.** In 2016 before bankruptcy, TDW's market price plunged to 1/10th of book value as it defaulted. Currently, TDW has a $24 book value ($1,014 mil. of equity/42.4 mil. shares[1]) which has been written down by over 50% - 70% to fair market value in July 2017 using Fresh Start Accounting upon emergence from bankruptcy. If we estimate a range of 1xs to 2xs book value, TDW might be worth **$24 to $48** in a normalized market. If we back out the 50% discount from Fresh Start Accounting, then we arrive at **$48 to $96** per share.

Another way to cross-check these assumptions is to look at when *Tidewater* merged with GulfMark in July 2018, it paid $5 million per vessel. Now TDW has 217 vessels including 61 stacked vessels of which 46 are available for sale. Excluding the vessels for sale ($0 value to be conservative), there are 171 vessels at the similar valuation of the GulfMark transaction of $5 million each, we arrive at $20 per share vessel value. Reversing the 50% discount due to Fresh Start Accounting would bring us $40. As of March 17, 2020, TDW trades at approximately $6 per share or 25% of book value (42.4 mil. OS x $6)/$1,015 mil. equity). **Since TDW is not in any danger of violating covenants on its debt** nor is it losing cash, then this discount is severe. However, in current market turmoil, the discount can widen further. The market is saying that *Tidewater* will not be able to earn a fair return on its marked-down assets for years. If the Covid-19 virus and the Saudi/Russian oil price war lasted for two years, then *Tidewater* might become impaired.

Valuation compared to building new vessels

Remember on page 3, Mr. Fabrikant of *Seacor* (CKH) spoke about building new vessels. At the low end you could pay $30 million from a Chinese yard or pay $10 to $15 million more at an American shipyard or $60 million or more at a European yard, lets plug in the low end of those values. TDW has 171 active vessels not in stack or for sale. New they would cost on average a total of $8.1 billion. TDW depreciates its vessels over 20 years, so with the average vessel being 10 years of age, ten years of depreciation would be $4.1 billion

[1] We compute dilutive shares at 39,941,327 (See F-2 of Tidewater's 2019 10-K) then add 2,483,956 in the money options, warrants, and restricted stock to equal **42.42 million fully diluted shares**. There are 5,923,399 out of the money warrants at the strike prices of $57.06 and $62.28 both with six-year terms.

deducted to leave $4 billion in theoretical vessel replacement value or **$94 per share**. Using the expensive European yards would be **$189 per share**.

We can also look at market purchases of second-hand vessels Standard Drilling buys platform supplier pair in 2017:

The company bought two UT 776 CD PSV vessels, E.R. Athina and E.R. Georgina. Both vessels are **large PSVs, built at STX Brevik Norway in 2009 and 2010 with 1,000m2 of deck space**. The two PSVs will be bought for a total consideration of $22.2 million. According to Standard Drilling, the acquisitions are expected to be completed in November 2017.

The vessels are currently working in the **UK sector of the North Sea**. The E.R. Georgina is on a term contract with Maersk Oil until July 2018 while the E.R. Athina is working in the spot market. Following the acquisition, the company will increase its fleet of 18 PSVs.

Martin Nes, chairman of the company, said: "The vessels grow our asset base and fleet and are favorably priced at around $11.1m per unit, **representing a discount of 81 percent to $57m actual newbuild price** and a **discount of 60 percent to the 25-year current newbuild parity of an eight-year-old vessel** with an implied value of **$28 million."**

Hornbeck Offshore on slides 33-34:

show how "cheap" its market value is compared to net book value and replacement value. Hornbeck's argument is valid only if the firm earns its cost of capital on its assets. Market values will decline sharply when vessels are not earning their cost of capital. Also, Hornbeck's (HOSS) 900 million dollars of net debt as of Sept. 30, 2019 swamps its current market cap of $3.8 million based on a 10-cents share price and 38 million outstanding shares. Equity can be wiped out with an overburdened capital structure. That is why *Tidewater's* clean balance sheet gives it a (temporary) competitive advantage while its competitors remain capital constrained and fall into bankruptcy.

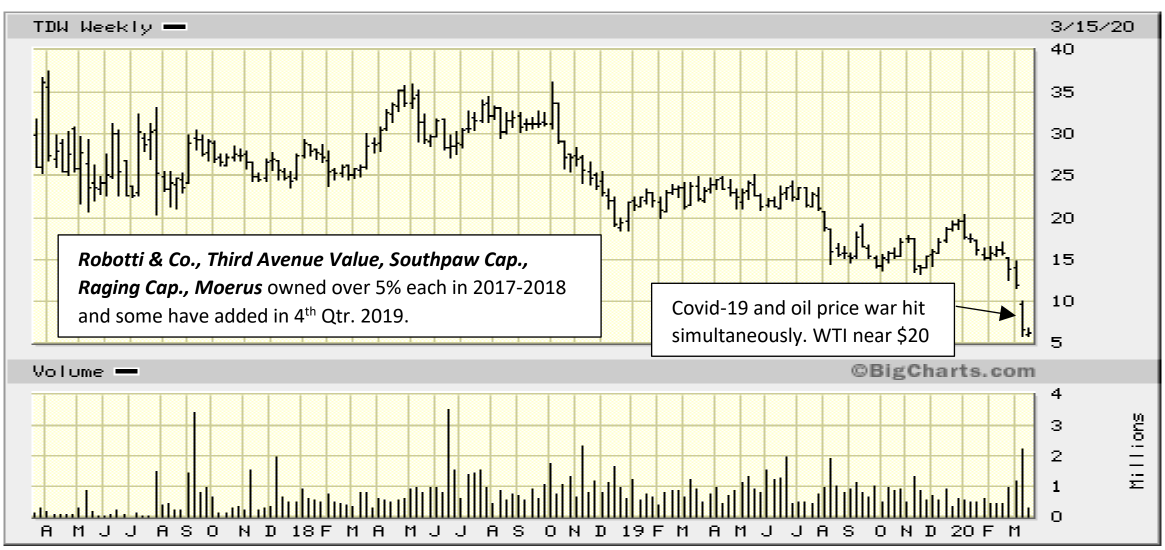
Those above replacement values will *only* be meaningful when *Tidewater* and the industry return to a higher level of profit or two to four times the charter rates of today. **Replacement value is the price to add new supply to the market.** Owners will not order vessels nor will banks finance construction unless the expected future cash flows (charter rates and utilization) justify the purchase price. *Tidewater* averages $10,000 vessel day rates with 56.5% utilization. See page 41 in *Tidewater's* 2019 10-K. Let's say the cost for a new vessel is $40 million and the return needed is 25% per year, then using 90% utilization rate (90% x 360 days), the minimum charter rate would need to be $30,000 per day or $38,500 per day for a $50 million boat. Those would be the sustainable rates to bring in new supply. There also could be labor constraints in finding competent and able crews. The replacement costs provide a barrier to new supply and a high mark for charter rates.

This is another way of saying that most if not all low spec vessels aged more than 15 years and in lay-up for more than two to three years will probably not return to service. The cost to reactivate is too high. Today, if you are an owner with a vessel needing $2 million in work to reactivate, then you need a return on the two million--or else why do it--in addition to the regular rate you are receiving now. Say there are 300 working days a year for the boat. Setting aside savings on storage/lay-up costs of $500 to $1,500 per day, the owner would need to make at least 35% a year on his money (the $2 million) in addition to his regular daily rate. (1.35 x $2 million/300 available days at best = $9,000 per day). Current average charter rates are now $10,000 per day, so the owner would need almost double his current charter rate to activate boats. No wonder almost 1/3 of the OSV fleet is rusting in place.

Jason Stanley, the Investor Relations officer at *Tidewater* commented, "Exactly. Yet, we see competitors in the market reactivate vessels for barely more than breakeven for 60-day contracts. **As capital continues to retreat from these owners' grasp**, we expect that these instances will decrease**. This is also a key driver behind why we are so aggressively getting rid of so many of our stacked vessels.** They make no sense to reactivate. We are instead focused on our higher-spec, newer tonnage. We aren't likely to see these day rates for some time to come, yet, so we have focused on the bottom line, while pushing rates up as much as possible as the market tightens. Eventually we will work towards earning the return on capital we all expect. *(Source: March 5, 2020 email reply from Jason Stanley).*

Over a third of the global OSV fleet is in cold stack which weighs on rates because of the perceived oversupply, but rates would effectively have to more than double to reactivate some of the vessels in storage. Also, customers may not be willing to sign contracts except for the newer, higher spec vessels. Why would management take a boat out of storage for an uneconomic contract? Managers want to protect their jobs, but those managers will lose their access to capital in this deep downturn. Note that Mr. Stanley is referring to the $39.3 million in assets held for sale on *Tidewater's* Dec. 2019 balance sheet as the vessels management wishes to dispose of.

A check on our thoughts might be what were other investors thinking who own *(TDW)*.



TDW traded between $20 and $35 from 2017 to 2019, then from $25 to $14 from 2019 to 2020. Assuming these experienced small-cap investors owned TDW at an average of $25 per share, the targeted upside would be conservatively 50% to 100% in order to justify the risk in such a cyclical company. Targeted prices could be **$37 to $50.** Of course, these investors did not foresee the "black swans" of a simultaneous oil price war with WTI Crude less than $25 a barrel and the Covid-19 virus outbreak. The critical question is whether TDW's value is permanently impaired or can the current market turmoil help it consolidate, improve its operations, and acquire distressed assets intelligently.

> www.Moerusfunds.com announces its initial purchase of *Tidewater* in its May 2018 Letter
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> *Tidewater* Inc., based in Houston, Texas, is an offshore oil and gas services provider. Owning and operating one of the largest fleets of offshore service vessels ("OSVs") in the world, *Tidewater* has over 60 years of experience supporting offshore energy exploration and production activities worldwide. The company provides services including towing and anchoring mobile rigs, transporting crews and supplies, assisting in offshore construction projects and performing numerous marine support services. **The past four years or so have been brutal for *Tidewater* and for the OSV industry in general.** In this business, revenues are directly related to offshore oil exploration and production activity. The collapse in crude oil prices from over $110 per barrel in mid-2014 to below $30 less than two years later hit the industry extremely hard. Suddenly finding themselves in survival mode, many oil companies dramatically cut back on their production and especially exploration activities. For the OSV industry, this meant that demand for its support vessels and services essentially fell off a cliff – and revenues collapsed as many services companies began to compete for projects with more aggressive day rates. Since then, oil prices have gradually begun to recover, but production from unconventional sources, namely onshore shale oil in the U.S., has increased steadily as shale operators, out of necessity, have wrung out costs and reduced the prices at which producing becomes economic. For producers forced to do some serious belt-tightening over the past four years, shale oil activities have become preferred investments as compared to offshore projects that often tap much larger and longer-lasting resources, but which require significantly more upfront capital expenditure, complex engineering and long lead-times to get to production.
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> While demand is extremely depressed, the supply side of the OSV market is no better. **The OSV industry is extremely fragmented, with many small owners of few vessels contributing to massive overcapacity.** Combined with demand destruction, this has resulted in average day rates which have declined by over 50% since 2014, putting most of the OSV industry into severe distress. **In our view, the industry would benefit significantly from consolidation or meaningful capacity rationalization.** We first wrote about our interest in the OSV space in the Fund's November 2016 Shareholder Letter in the context of another Fund holding, *Aker ASA.* Aker participated in a recapitalization of an OSV company, *Solstad Offshore*, to drive consolidation in the industry. Since then, what is now *Solstad Farstad* has in fact completed a couple of transactions, but it will take much more consolidation to move the needle. While Aker provided us with an intriguing indirect investment in the highly depressed OSV industry, *Solstad Farstad* represented only a small portion of *Aker*'s value. Unfortunately, virtually all the pure play OSV companies, including *Tidewater*, had highly leveraged, distressed balance sheets.
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> **However, fast forward to mid-2017: *Tidewater's* debt burden became unsustainable, and it was forced to restructure via a prepackaged bankruptcy.** With much of the pre-existing debt converted to new equity and warrants, *Tidewater* emerged in August 2017 with what is clearly one of the strongest, if not the strongest, balance sheets in the entire OSV industry. The company is virtually net debt-free, with $445 million in cash against $448 million of debt, and **has no meaningful debt maturities until 2022.** *Tidewater*, unlike most of its peers, **now boasts the staying power to**

navigate through the current industry depression, potentially consolidate or acquire heavily discounted vessels from distressed peers, and **position itself to benefit disproportionately in the event of an eventual recovery in the OSV market.**

Tidewater shares most recently traded at a discount to reported book value, which in turn reflects asset values that have been **written down by nearly 70%** as a result of fresh start accounting. While the accounting write-downs understandably reflect extremely depressed current industry conditions, they value *Tidewater's* ships at a material discount to what they could potentially sell on the secondary market today, and at a much greater discount to the actual construction cost of the vessels. In some cases, ships recently built and delivered to *Tidewater* are being carried on the books at 30-40% of their construction cost. At such a beaten-down valuation, we believe the upside potential is considerable if offshore activity and OSV demand eventually recover. This seems reasonably probable to us given that **offshore production still accounts for over 25% of global oil production yet has suffered from significant underinvestment in recent years that we expect will require catch-up spending at some point.**

www.Moerusfunds.com in its November 2018 Letter: Example: *Tidewater* Inc.

An example of the potentially divergent interpretations of reported operating results is offered by the reaction to the most recent reported results of *Tidewater* Inc., a company we wrote about in our last Shareholder Letter. The company provides offshore service vessels and associated services to offshore oil exploration and production installations, which are currently experiencing significantly depressed levels of business activity. The weakness of the current level of business activity was evident in the company's recently reported results (released in November), **which nonetheless showed positive cash earnings, no small achievement in a fragmented industry in which many of its peers are at death's door.** Meanwhile, also in November, *Tidewater* merged with a peer (Gulfmark Offshore) that had complementary operations, continuing to broaden the geographic scope of its operations while acquiring Gulfmark's fleet at what seems likely to be a significant discount to replacement cost. Our take on the merger and earnings results was generally positive in the context of the long-term building of the business value. But the majority of other investors, who are earnings-focused and probably shorter-term in nature, seemed to view these events far more negatively, with an ensuing impact on the company's stock price. **In our opinion, the currently depressed levels of offshore activity that drove *Tidewater's* results are long-known, and the company's results for the past quarter were therefore not surprising.** Yes, the past quarter's reported earnings were weak, but from our perspective as a long-term investor in a business that we believe is **building intrinsic value and strengthening its position for an eventual normalization in business conditions**, it merely reflects noise that is irrelevant to the long-term operation of the business.

Tidewater, Inc., the third largest detractor from Fund performance in Fiscal 2018, is a United States based provider of offshore service vessels ("OSVs") and associated services to offshore oil exploration and production installations, which are currently experiencing significantly depressed levels of business activity. *Tidewater* stock was negatively impacted by a sharp decline in oil prices late in 2018, which in turn reignited fears of continued near-term weakness in offshore energy activity (the primary source of demand for *Tidewater's* services). However, while conditions in its business remain quite weak, given our long-term perspective, **we believe the investment thesis remains strong, and in fact may even be strengthened given some advantages that *Tidewater* possesses relative to the rest of the industry.** Specifically, its best-in-class balance sheet allowed the company to acquire *Gulfmark Offshore's* high-quality vessel fleet at what seems to be a deep discount to replacement cost. We believe the company remains uniquely well-positioned to lead consolidation in the OSV space and emerge stronger when industry conditions normalize. In our view, *Tidewater's* valuation is increasingly compelling, at a deep discount to tangible book value, which in turn has been dramatically written down in recent years.

In their November 2019 Shareholder Letter ***Moerus Funds*** again explained their reasoning for investing:

As for *Tidewater*, its balance sheet strength is the envy of the Offshore Service Vessel ("OSV") space, providing the company with **staying power and the potential to continue consolidating this fragmented industry of distressed players at bargain prices.** Despite operating in an extremely cyclically depressed industry, *Tidewater's* recent results have been encouraging, as day rates have begun to tick up and operating expenses continue to come down (as synergies from the *Gulfmark* acquisition continue to be realized). Yet *Tidewater* shares currently trade at a deep discount to both reported tangible book value – which in turn reflects asset values that had already been written down by roughly 70% as a result of fresh start accounting – as well as a conservative estimate of replacement cost, **in addition to a low single digit multiple (< 3x) of a conservative estimate of normalized operating cash flow.**

Third Avenue Fund Discussed their investment in *Tidewater* in their 3Q18-Letter.pdf

During the quarter, *Tidewater*, which is the world's largest operator of offshore service vessels, reached an agreement to acquire smaller peer *Gulfmark* Offshore and continued to contribute strongly to Fund performance. *Tidewater* is in prime position to consolidate a beleaguered but recovering offshore supply vessel industry owing to its net cash **balance sheet and right-sized cost structure, both of which were achieved through the bankruptcy process.** Shortly after the *Tidewater* announcement, smaller industry peer Harvey Gulf International made a competing bid for *Gulfmark*, which is indicative of the amount of consolidation taking place in the offshore oil services industry today. We expect the *Tidewater* and *Gulfmark* transaction to close as announced and for **the combined company to continue to be in a unique position to seek consolidation opportunities to build scale, efficiency and market position into a strengthening market.**

Thirdave.com 2019-Q4-TAVFX-Shareholder-Letter:

One's hopes for radical changes to how the world powers itself aside, the facts are that global oil consumption continues to rise, U.S. onshore production growth has predictably begun to slow and **the reserve replacement ratio for the world's offshore oil and gas resources is too low to keep production at the current level indefinitely.** International oil companies, who today are producing near record cash flows, have always understood this to be the case. In early 2019 they began to act upon this fact pattern by increasing investment in offshore resources, albeit from incredibly low levels. For example, for the global jackup drilling rig market, the number of utilized rigs fell from roughly 450 in 2014 to a low of roughly 300 in 2017, rendering the industry in a position of rampant excess capacity. Day-rates (prices) for premium jackups fell from a 2014 peak of somewhere around USD 175,000 per day to a 2018 low of roughly USD 50,000 per day.

Third Avenue Fund 1Q 2019 Letter

A concise version of our investment thesis is that **offshore oil and gas production is critical to the global energy mix and is extremely likely to remain so for some time.** Further, we believe that for several years following a rapid oil price decline in 2014 and 2015, the reduced level of spending on offshore oil and gas exploration and production fell to levels clearly below that required to sustain production at these levels. If industry austerity persists, then production declines will result soon. **The makings of this scenario can be seen in the offshore oil and gas industry' s extremely low**

reserve replacement ratios and falling reserve lives. We believe that oil and gas producers share this view and are beginning to act in order to stave off the otherwise inevitable production declines.

However, during these extremely lean last five years, service providers were forced into survival mode and have scrapped huge numbers of drilling rigs, seismic vessels and platform supply vessels, a process which continues today. **This industry attrition will make previous levels of exploration and production activity very difficult to achieve without far higher prices for the services.** In other words, the supply and demand balance for offshore oil services is likely to become tight (driving prices higher) at activity levels well below the highs of the last cycle. This pattern of events is very much in keeping with previous offshore oil service cycles, whereby increasing asset utilization leads to rising service prices. In early 2019, the process of recovery appears to have begun in earnest but has quite a long way to go in order to reach industry normalization.

These dynamics have become clear and present as evidenced by recent operating performance reports. For example, PGS recently reported that pricing for 2019 contract work booked to date remains strong and is now more than 35% higher than the average rate in 2018. In a recent meeting with *Borr Drilling*, management projected that they would have their entire rig fleet sold out by the end of the year while recently contracted day rates for modern jack-up rigs - the type *Borr* owns - are currently running in the neighborhood of 60% higher than one year ago, in some cases meaningfully more.

Regarding the **platform supply vessel (PSV) market**, **where *Tidewater* is the world's largest operator**, oil services specialist *Fearnley's Securities* recently commented: "The spring/summer season in the North Sea is really starting to take shape for PSVs. The spot market remains close to sold out, rates are hovering at levels not seen since the downturn and term requirements continue to build." Oil service specialist *Clarksons Platou Securities* tracks the same dynamic in analysis of the North Sea PSV market where it estimates that **2019 rates are running 56% higher on average than 2018.** The light at the end of the cyclical tunnel appears to be shining brighter and brighter each day with a wide range of supporting data points.

Robotti and Company in its 4th Quarter 2019 Shareholder Letter

One of our core holdings, *Tidewater* (NYSE:TDW), provides vessels for the offshore energy industry. *Tidewater* emerged from bankruptcy in 2017 with the strongest balance sheet in the industry. In 2018, the company smartly and quickly merged with a competitor, *Gulfmark*, taking significant costs out of the business, resulting in a substantial cash savings and in the process almost doubling *Tidewater's* gross profit. **This is a large reason why *Tidewater* is currently cash break-even despite a very competitive environment.** We believe significant opportunities remain. To help ensure the company capitalized on these opportunities, late last year **we filed a Form 13-D**, sending an open letter to the board (see excerpt in next paragraph). Not even a week later, the company announced significant changes to their board, including appointing a new chairman. *Tidewater* is now focused on finding a good strategic partner, which will extend its runway for growth, improve the efficiency of the industry as a whole and position *Tidewater* as a leader in the ongoing recovery. *Tidewater* is indicative of the kind of opportunities we are seeing across our portfolio – buying a company for a fraction of the asset value with identifiable opportunities to dramatically increase its asset value while preserving a strong financial position and mitigating investment risk.

Excerpt from Robotti Company letter to *Tidewater* Board on October 2019[2]:

[2] Tidewater immediately responds: https://www.workboat tidewater-elects-rigdon-chairman-reduces-board-size/

Given the substantial cost advantages evidenced in the *Gulfmark* deal and the positioning advantages shown by the historic Zapata merger, we believe it is incumbent upon management to act with a sense of urgency to **find another suitable combination or combinations.** Post reorganization, *Tidewater* is uniquely positioned as the most desirable consolidation partner in the OSV industry. With the competitive advantage of the industry's strongest balance sheet – by a wide margin – the Company has a great opportunity to be highly selective in a well-defined, earnest and transformative process.

Finding a good strategic partner will extend *Tidewater's* runway for growth, improve the efficiency of the industry as a whole and position *Tidewater* as a leader in this ongoing recovery. There are abundant potential merger candidates which can help achieve cash flow positive results even before pricing and profitability return to the rest of the industry, further advantaging *Tidewater* as the industry's consolidator of choice. We expect management to actively engage with the full list of competitors, including managements, shareholders, and other interested holders and lenders, and complete a full due diligence on the comprehensive range of possibilities to execute value creating transactions. We further believe a right-sized, engaged and focused Board will ensure management's efforts.

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Robotti quote on the energy industry and *Tidewater* 2019 (Source: Interview in *Manual of Ideas*)

The Energy Industry Hits Reset

We view the opportunities in front of us in energy as very significant and clear. If we look back to 2013-2014, large capital projects in the energy business were not economic. Costs had increased significantly, and many projects were uneconomic by the time they were completed. There were issues with delays and cost overruns among other things. As a result, the industry started to pull back on capital spending in the beginning of 2014.

Then at the end of 2014 oil prices went into free fall. Since then, of course, oil prices have improved and gone from lows of $20 back up to $80, before trailing back at $70. What's important is not only prices of the commodity, it's also the cost structure of the business.

Costs had expanded dramatically which narrowed the funnel of projects that could make it out of discoveries and get developed while being economic. That funnel became so tight that in 2014 the industry started to retract. Today that funnel has gotten extremely wide because the cost structure has dramatically changed. Some of this is temporary, some of this semi-temporary and some of this is permanent. So, what you really have is an inventory of 5, 10 or 15 years of discoveries that had been blocked because of cost inflation and now suddenly look very economic.

Today, there are many projects that are economic at $40 oil. **There are projects offshore that are economic even at $30 oil. So, the project inventory of economic opportunities is significant. What you also need is someone with the capability and the willingness to spend the money. The Majors are in a very different situation today versus 2013 – filling their coffers, looking at improved cash flows going forward but also watching production profiles decline.** Now that all these pieces have come together, we are starting to see increasing opportunities.

Subsea 7 is an investment that we have held for a long time. We know its management very well. They have constant dialogue with the majors in terms of multibillion-dollar projects. The inventory of projects is rising and now progressing from tie-ins and brownfield activity. We think that in the next year a significant flood of new opportunities will come forward. So that's the backdrop for why we think the opportunity set in energy is strong.

Consolidation – A Cyclical Opportunity

In energy, we have two different types of investments. *Subsea 7*, which is a great business that was opportunistic in the downturn and is recovering, represents one type. ***Tidewater*** is different. It went into the downturn with a balance sheet that was poorly structured. As a result, the company went through a major restructuring last year that wiped out all the debt.

Today the company has $450 million of cash and $450 million of debt – zero net-debt. Everybody else in the industry is over-levered. *Tidewater* is now managing the process of combining with another company, *Gulfmark*, which went through a similar restructuring process. The merger is expected to go through on Thursday. Dan and I have met with the CEO and one of the board members of *Gulfmark* and talked about the deal its attributes.

The combination will create the largest company in the business. The company will also be left with a clean balance sheet at a time when every other competitor is extremely levered. With zero debt to service, *Tidewater* will have a tremendous advantage as its competitors struggle with debt burdens. We think this should force more assets to become available and that will enable *Tidewater* / *Gulfmark* to opportunistically acquire cheap assets.

Although this is a cyclical business, **at some point, new equipment needs to be put into the field. You know that no one's going to build a new piece of equipment until it makes economic sense to do that.** Day rates have gone from $6,000 a day to $12,000 a day. To build new vessel you need something like $32,000 a day. Profitability is dramatic from here.

There's also some concern over the 200 vessels that have been completed that are still sitting in the shipyard. We estimate that half of these vessels will never come out of the yards in China. We think that a fraction of the other half will end up coming out of the shipyard and will likely be purchased by an opportunistic buyer who will only be able to use them for a limited number of mandates from a narrow customer base. Most likely, these boats will not be competitive in many of the world's markets.

You already see the path to realization of the opportunity for significantly higher earnings. Today *Tidewater* has an enterprise value of roughly $1 billion. The replacement cost its vessels is closer to $3 billion. We think the earnings power potential of the business is dramatic, it's in the process of recovering and even if we are wrong its balance sheet will allow them to be a survivor while competitors continue to disappear. So, the question isn't whether we win, the question is whether the outcome is now or a little bit later. We think it's more likely now than later.

Raging Capital sent an urgent letter in May 2019 to *Tidewater* asking for governance changes and explaining why they were major shareholders

At the Annual Meeting, I (William C. Martin, CIO of Raging Bull) noted that Raging Capital is excited about the leading quality, scale and young age of *Tidewater's* global fleet, as well as the Company's best-in-industry balance sheet. Indeed, it is remarkable that *Tidewater* currently has a sub-$1 billion enterprise value, even though the Company (and its merger partner, *Gulfmark* Offshore, Inc. ("*Gulfmark*")) have invested a total of more than $4 billion in their fleet since 2010 alone. Further, the current enterprise value is less than 2x the average annual combined EBITDA of *Tidewater* and *Gulfmark* from 2005-2014,* the years before the energy crash.

*Company	Avg. Annual EBITDA 2005-2014	Combined Enterprise Value
Gulfmark	$144 million	$990 million
Tidewater	$374 million	Current Multiple/Ind. Multiple
Combined	**$518 million**	1.9xs/5xs ($4.95 billion EV @ 5xs)

Lack of Insider Stock Ownership: With the exception of director Larry Rigdon (Now Chairman of the Board), who has a valuable and impressive background in the offshore industry, not one member of the *Tidewater* board of directors (the "Board") has bought a single share of stock[3] in the open market, according to public filings.

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In May 2019, before the recent intensification of the Covid-19 and Saudi-Russia price war which has sent the price of WTI crude down (as of March 18, 2020) to near $20 a barrel, Mr. Martin of Raging Capital thought *Tidewater* at 2 times EBITDA post acquisition of *Gulfmark* was far undervalued at $990 million or **$23.6 per share**. A more reasonable multiple of 3 to 5 enterprise value to EBITDA might imply a price per share of **$70 to $117**.

The excerpts from the various letters to shareholders and to management show the *expectations* of those investors prior to this recent (March 2020) leg down in the oil market and the halting of economic activity due to the Covid-19 virus. Some investors focus on the demand side for offshore oil exploration and development. I will not analyze demand nor forecast future oil and gas prices other than to posit that the cure for low prices is low prices. Note that in the past 40 years, the price of WTI crude has rarely stayed below $30 and that is because most producers can't extract oil profitably at sub-$30 oil. See Crude oil price history chart. During the Covid-19 virus oil prices going down will not stimulate demand. If gas is $0.01 a gallon and you have filled up your car and gas storage tanks, then what more can you buy? The Covid-19 virus will pass, but the length of time and damage to economies are the major uncertainties. My advice is not to be swayed by extreme forecasts during panics. Click on the crude oil link above and note the price low in 1999 then read this article:

An excerpt from an article in "*The Economist" on May 4, 1999*: "THE NEXT SHOCK?"

The price of oil has fallen by half in the past two years**, to just over $10 a barrel.** It may fall further—and the effects will not be as good as you might hope[.]

OIL is cheaper today, in real terms, than it was in 1973. After two OPEC-induced decades of expensive oil, **oil producers and the oil industry have <u>given up hope</u> that prices might rebound soon…**

Consumers everywhere will rejoice at the prospect of cheap, plentiful oil for the foreseeable future. Policy makers who remember the pain of responding to oil shocks in 1973 and in 1979–80 will also be pleased. But the oilmen's musings will not be popular with their fellows. For if oil prices remain

[3] On March 13, 2020, Larry T. Rigdon, Chairman of The Board of Tidewater bought 20,000 shares at $6.39 and Ken Traub, Director, bought 5,000 shares at 6.48.

around $10, every oil firm will have to slash its exploration budget. Few investments outside the Middle East will any longer make sense.

Cheap oil will also mean that most oil-producing countries, many of them run by benighted governments that are already flirting with financial collapse, are likely to see their economies deteriorate further. And it might also encourage more emissions of carbon dioxide at just the moment when the world is trying to do something about global warming.

Yet here is a thought: $10 might be too optimistic. We may be heading for **$5…**Thanks to new technology and productivity gains, you might expect the price of oil, like that of most other commodities, to fall slowly over the years. Judging by the oil market in the pre-OPEC era, a "normal" market price might now be in the $5–10 range. Factor in the current slow growth of the world economy and the normal price drops to the bottom of that range…" End of article.

So much for dire predictions….

Because the success of this investment depends upon a long-term perspective, let's listen carefully to John Laborde, one of the legendary founders of *Tidewater* and the OSV industry, speak about industry tough times thirty-three years ago during the last major, major bust. *(Seacor Holdings 2015 Letter to Shareholders):*

An excerpt from a speech presented by Alden J. Laborde at the Offshore Technology Conference on **April 27, 1987: "THE OFFSHORE SERVICE INDUSTRY— WHAT HAPPENED? WHAT NOW?"**

…My title is not unlike the epitaph on the tombstone which read, "I told you I was sick." Like us in the service industry, the guy under that stone got the world's attention after it was too late…

The main thing on the minds of service people these days is whether the oil and gas business, and therefore our business, **will recover**, and if so, **when might it happen**. First I'll give you a few reasons **why it must recover**, perhaps not to the wild days of the early eighties, but to return as a viable, significant industry going about the business of supporting our customers as they supply the [world] with all-important energy products, perhaps about the level we enjoyed [in] the mid-1970's before the price of oil skyrocketed and our wisest planners and forecasters in industry…said it was headed to $75 or $100; that we'd run out of oil early in the next century.

Was it any wonder, then, **that the service industry went into a…[party] of expansion**…[B]anks came along with **easy credit**—in many cases with government guarantees, asking few questions. The oil companies told us to hurry—**there was no end in sight**. Operators…signed long-term contracts before [equipment was] ordered…Even with warning signals…in the form of oil price softness in the early eighties, down to $30 a barrel…**none thought it would go below $25…**

But lo and behold, the price kept falling—all the way down to $10, and **panic set in.** Operators all but ceased exploration, **cut to the bone on development**, cut staffs dramatically, and went into hibernation, where we still find most of them, marking time, depleting their precious reserves, their life's blood without replacement. Surely, they don't need me to tell them what they are doing and the consequences—what with their sophisticated managements and the economists and planners they all have in abundance. They are like the grocer who would sell all the groceries off his shelves, thinking business was great—until he had to replenish his inventory. I repeat that surely they know better [than that]…, and must even now be working on plans to replace their stocks and get moving again.

Unfortunately, though, most [U.S.]…corporations are driven by concern for **short term profits**—next quarter, this year, next year at the latest— preserving that bottom line is the first priority—protecting that dividend comes right behind…

Further, unfortunately, the conventional way oil companies keep their accounts and report results to shareholders allows and encourages **curtailment of activities such as exploratory drilling to protect earnings.** Under the reporting system the real values, those of **reserves in the ground**, the groceries on the shelves, so to speak, don't show up on the balance sheet and don't affect the income statement, **although they are the inventory just as surely as the groceries are…**

These are facts that we must consider in trying to understand our customers' behavior, in order to plan our business around them we must fit our business into the cracks in theirs. We can't expect from them help or charity or even sympathy. **But I am sure they will not indefinitely remain in this liquidating mode…Oil and gas are still indispensable commodities in our economy**… Judging by all the automobiles [we sold in the last few years]…we'll still be needing a lot of gasoline for a [few years.]…**Natural gas** has no peer as to convenience, cleanliness, and even price in many applications…

…I had hoped that they might blow the time whistle on me by now and I wouldn't have to tackle the second part of my assignment, **leaving the time forecast to those following me on the program**. The timing of the recovery I am promising is quite difficult to predict because the business has never operated in a free market in my long memory. And, therefore, economic models based on free supply and demand just do not work…

Of the 16 odd million barrels of oil which we consumed each day at the beginning of 1986, some nine million were produced domestically and seven million were imported. After the terrible year of attrition, we had by the end of that year **lost almost a million barrels a day domestically from shut in wells**, uneconomic ones like heavy oil producers, strippers, wells in remote areas and the like, plus the normal decline of existing producers, usually 10% to 12% per year for wells going flat out as we are pulling them. Meanwhile, **consumption has gone up 2% to 3% in response to lower prices and industrial growth**…Oil company staffs are decimated, the service infrastructure is dismantled, rigs **and boats have been scrapped to the tune of half the fleets, fabrication yards are closed, technicians gone to other fields, rig manufactures, mud companies, supply stores and the rest have left the territory.**

We'll…likely see a replay of the…story. Prices will rise sharply…The mad scramble for the existing equipment and services will begin…[M]emories are short…and **history will repeat itself.**

When will all of this happen, you repeat? I'd say when domestic production goes down another million barrels a day to 7 million and we are importing 9 plus million or so…my bracket—18 months to two years, give or take a few [1989–1990].

…So there you have it—I've stuck my neck out—it may not make much difference when it happens to those…who have already bitten the dust… Others hanging on by their fingernails may find the time quite long, too; **too long perhaps for their bankers. But those who manage to tough it out for another year or two will be glad they did."**

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Mr. Laborde has just described the capital cycle of the OSV industry at the trough of its cycle (1987-1989). Go to page 4 of this report to see the long-term chart of TDW and note Mr. Laborde's timing. The future is uncertain, but one can make intelligent assumptions about the future needs of customers. Today, just like thirty-three years ago, excess OSV supply is rusting in place or headed to the scrap yard, companies are going bankrupt, customers are skimping on replenishing rapidly depleting reserves, experts declare that oil will fall below $5 a barrel, and fear and negative sentiment are near a peak of despair as I write this on March 19th, 2020.

A reader can see from pages 18-20 from Transocean February 2019 Presentation how little oil is being found to replace dwindling offshore reserves. Partially, offshore production has been replaced by surging tight oil (fracking) production onshore, but this production is rapidly declining due to capital constraints and depleting of tier 1 acreage. See http://blog.gorozen.com/blog and Sailingstone Capital commentary

Our focus will be on *Tidewater's* ability to survive this downturn and on the perceived overestimated supply of the OSV industry.

Tidewater's Management

An investor in a cyclical, capital intensive business depends heavily on the skill of management to operate efficiently, allocate capital successfully, and act counter-cyclically.

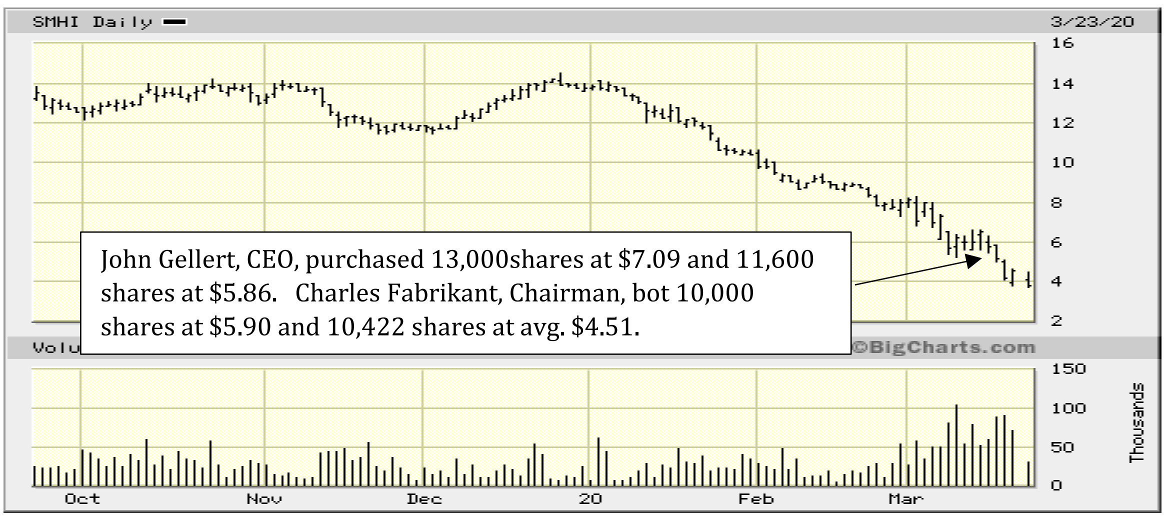
Mr. Larry T. Rigdon is the Chairman of the Board for *Tidewater*, and he has experience in consolidation from being part of the management team that joined *Tidewater* in 1992 from the Zapata merger. This merger was successful and provided a strong platform for success over the next twenty years[4].

Mr. Rigdon has been a member of the *Tidewater* Board of Directors since August 2017. He has extensive prior experience as an executive at *Tidewater*. After successive roles of increasing responsibility, he left the Company as Executive Vice President in 2002. He then successfully founded and grew *Rigdon Marine Corporation* to an owner of 28 offshore service vessels, selling the company in June 2008 to *Gulfmark Offshore, Inc.* ("*Gulfmark*"), where he became a board member thereof until 2010. Mr. Rigdon also currently serves as a director of *Professional Rental Tools, LLC.*

Insider Buying: Mr. Rigdon purchased 20,000 shares of TDW at $6.39 on March 13—a sign of confidence. Note Mr. Gellert of *Seacor Marine bought* shares. A sign of faith in the future.

[4] Source: Business Wire Jan 15, 1992: Stock analysts are hailing the deal as a win-win situation. Tidewater Inc. Chairman John Laborde simply says he's "very pleased." After months of negotiations, the merger of New Orleans-based Tidewater and Zapata Gulf Marine Corp. of Houston concluded with a public exchange of stock certificates on Jan. 15. The transaction consisted of a tax-free exchange of 24 million Tidewater shares for all Zapata Gulf shares. Through the deal, service boat giant Tidewater acquired the vessels of Zapata Gulf, thus amassing a fleet of 580 vessels serving the international offshore energy industry and becoming the largest marine energy service company in the world.

Another reason analysts are giving Tidewater high marks is because the company has significantly reduced its debt load. At the time of the merger, Tidewater borrowed $100 million and paid off $86 million of Zapata Gulf indebtedness. The company also has wiped out $62 million of previously existing long-term debt, $55 million of which as paid ahead of schedule, Laborde says. "They've pared down huge amounts of debt, they have tons of cash and they bought out their second-biggest competitor," says Dutt. "Things look very favorable."



Fast forward to July 2018

Tidewater and *Gulfmark Offshore Inc.* agreed to merge on Monday in an all-stock transaction that will create the world's largest global offshore service vessel operator. The combined company is valued at approximately $1.25 billion (based on *Tidewater's* closing price of $30.62 a share on July 13, 2018.)

The transaction is expected to be accretive to *Tidewater's* 2019 EBITDA and produce transaction-related cost synergies of approximately $30 million, which are expected to be realized no later than the fourth quarter 2019, and additional efficiencies associated with greater scale and scope of operations. See: *Tidewater-Gulfmark*-agree-merger/

The *Gulfmark* merger brought Mr. Quintin Kneen to *Tidewater*. He was appointed President, CEO and Director of *Tidewater* in September 2019. Prior to this, he served as Executive Vice President and Chief Financial Officer at *Tidewater* since November 2018 following its acquisition of *Gulfmark* Offshore where he served as President and Chief Executive Officer since June 2013.

Mr. Kneen has vowed to focus on free cash flow, rationalizing and optimizing *Tidewater's* fleet, and developing good returns on capital. He is guiding *Tidewater* to focus on a returns-based philosophy.

Here is a recent quote from Mr. Quintin in 2019:

> Quintin V. Kneen, *Tidewater* President and Chief Executive Officer, commented, "Market conditions across all of our operating areas are showing signs of recovery. Although the industry remains oversupplied, the potential to create long-term value through consolidation and disciplined capital management is clearer today than it has been in the past 5 years. We have been aggressively restructuring our shore base operations and our management structure over the past two months to improve the efficiency and scalability of our operations. Our strong balance sheet, combined with the successful rollout in October of our enhanced information system, positions *Tidewater* as the only market participant with a scalable global infrastructure capable of significant consolidation in the offshore support vessel industry."

Mr. Quintin says all the right things and now he must deliver results in a brutal market. So far, he has exceeded the stated merger savings of $30 million—subsequently bumped up to $45 million--with more than $65 million of savings or $1.53 per share, and he has generated free cash flow in a depressed market. Those $65 million and possible additional savings from the merger show the power of the right merger/consolidation. Also, *Tidewater's* Board has responded quickly to the concerns of its shareholders (Robotti & Co., and Raging Capital) by reducing its Board from ten to seven members and replacing CEO, John Rynd, with Quintin Kneen. The Board was willing to choose the best man for the job given that Mr. Kneen came from the smaller company and he would work well with Mr. Rigdon—that is my presumption.

Debt, Solvency, and Free Cash Flow

<u>Debt to Capital ratio</u>: Total Debt / (Total Debt + Equity) = ($565m/$565m + $1,015m) = $565m/$1,580m) = 36%   36 cents of debt are financing a $1 of assets.

<u>Net Debt to Market Cap</u>: (Long-term debt of $279 – Cash of 218m = $61 m) / 42.4 outstanding shares plus warrants in the money times $5.00 as of March 19th 1 PM = $61m / $212m = 29%. You will see how well financed *Tidewater* is compared to its competitors later in this report on page 30.

Tidewater has about $225 million in secured notes due in August 2022. Management paid down $125 million of these notes in 2019 which improves cash flow by $8 million less interest expense per annum.

(4) INDEBTEDNESS from 2019 10-K

The following table summarizes debt outstanding based on stated maturities:

(In thousands)		Dec. 31, 2019	Dec. 31, 2018
Secured notes:			
8.00% Secured notes due August 2022	**$**	**224,793**	349,954
Troms Offshore borrowings:			
NOK denominated notes due May 2024		10,260	12,241
NOK denominated notes due January 2026		20,788	22,988
USD denominated notes due January 2027		20,273	22,116
USD denominated notes due April 2027		21,545	24,157
		297,659	431,456
Debt premium and discount, net		(8,725)	7,548
Less: Current portion of long-term debt		(9,890)	(8,568)
Total long-term debt	**$**	**279,044**	430,436

	2020	2021	2022	2023
Total Debt Obligations*	$62.2	$41	$259	$26.3

** These are the worst-case obligations because unrecognized tax benefits (FASB No. 48) may not have to be paid in the estimated period.*

Tidewater is at about cashflow break-even from operations: if one accepts Mr. Kneen's guidance on the 4th quarter 2019 conference call where he advises an average $9.5 million per quarter of drydock expense. Thus, a total of $38 million can be backed out of 2019's heavy dry-dock expense of $70.4 million to normalize 2019's operating cash flow to about $1 million. See on next page.

(In thousands)	Year Ended December 31, 2019	Year Ended December 31, 2018
Net loss	($141,219)	($171,771)
Depreciation and amortization	77,045	51,332
Amort. of deferred drydocking and survey costs	24,886	6,961
Amortization of debt premiums and discounts	(4,877)	(1,856)
Provision for deferred income taxes	672	572
Gain on asset dispositions, net	(2,263)	(10,624)
Impairment of due from affiliate	—	20,083
Long-lived asset impairments	37,773	61,132
Loss on debt extinguishment	—	8,119
Compensation expense - stock based	19,603	13,406
Deferred drydocking and survey costs	(70,437)	(25,968)
Changes in operating assets and liabilities	4,162	(4,266)
Changes in due to/from affiliate, net	22,193	28,644
Changes in inv. and adv. to unconsol. cos.	1,039	28,177
Net cash provided by (used in) ops.	**($31,423)**	**$3,941**
$38,000 avg. Drydock costs, back out $32,437, *Or the difference of ($70,437 - $38,000)*	**Adj. $1,014**	

Tidewater generated FCF in 2019	***31-Dec***	**30-Sep**	**30-Jun**	**31-Mar**	**Dec. 31, 2018**
Net cash provided by (used in) ops.	*$5,281*	-$15981	-$17,566	-$3157	-$26,171
Cash interest expense	*8,205*	8,189	7,974	8,319	8,108
Interest income	*(690)*	(1,579)	(1,859)	(2,470)	(5,799)
Loss on debt extinguishment	-	-	-	-	8,119
Additions to properties and equipment	*(4,067)*	(5,058)	(5,757)	(3,116)	(12,275)
FCF before proceeds from asset sales	*$8,729*	-14429	-17208	-424	-28018
Proceeds from asset sales	*3,755*	4,526	10,915	9,651	29,616
Free cash flow	*$12,484*	-$9,903	-$6,293	$9,227	$1,598

Annual free cash flow	***$5,515***

Tidewater's CEO, Quintin Kneen, outlined two goals on the 4th Qtr. 2019 Conference Call:

He wants *Tidewater* to leverage a scalable shore-based footprint to operate the most vessels possible at the lowest possible cost in a region by becoming a regional super consolidator. He is deemphasizing business in Brazil and Asia to focus more on the North Sea, for example. His other major goal will be to increase free cash flow to over $50 million or $1.18 per share. Let's go through his expectations:

3 Months Ended Dec. 2019	***Tidewater* generated positive Free Cash Flow In 2019**
$5,281	Operating activities
$8,205	Cash interest expense
-$690	Interest Income
-$4,067	Additions to prop and equip
$8,729	FCF bef. Asset sales
$3,755	Proceeds from asset sales
$12,484	FCF for 4th Qtr.
$5,515	FCF for 2019 ($12,484 -$6,969 FCF 9 Mos.

Mr. Kneen expects increased free cash flow in 2020

Estimated for 2020	**In $000's**	**Actions To Be Taken**
	$10,000	Reduced G&A
Pre-sub $30 oil/Covid-19 Crisis	$10,000	Incr. CF from Vessels disposals
	$18,000	Reduced Inv. In vessels
	$10,000	Less capex
	$6,000	Improved utilization in core ops.
Totals	**$54,000**	Estimated improvement in FCF

Adjustments

If we take out the $10 million of improved FCF from vessel disposals because we assume *Tidewater* will not be able to sell boats during the current extreme market depression. We also take out $6 million in improved utilization. *Tidewater* could generate $25 to $38 million in FCF in 2020. Free cash flow to the firm consists of cash flow provided by operating activities before interest, but after capital expenditures (deferred drydocking and survey costs). Cash flow provided by operating activities is defined as cash available for shareholders. Thus, it is computed after income taxes and interest have been paid.

Notes on free cash flow from the 4th quarter *Tidewater* Conference Call:

- Expect G&A expenses to be $83 million, an improvement of at least $10 million than the $104 million expense of G&A in 2019.
- $39.3 worth of estimated value of vessels to be liquidated in 2020 to increase FCF by $10 million. These vessels and other marine equipment were written down and impaired by $37.8 million[5]

[5] The value of a long-lived asset or group of assets like OSVs is impaired when the asset's carrying amount exceeds its fair value. An impairment loss is recognized, however, only when the carrying amount of the impaired asset is not recoverable. Recoverability is determined by comparing the carrying amount of the asset with the sum of the undiscounted cash flows expected to result from the asset's use and eventual disposition.

- Heavy drydocking expense of $71 million in 2019, but this expense is expected to be $53 million in 2020 or an improvement of $18 million. $35 million estimated for 2021.
- *Tidewater* is holding 19 vessels in layup that are in the lowest specification vessel category that is employable. Capex will be $8 million which is $10 million less than in 2019.
- In its core business of operating vessels, *Tidewater* improved active utilization from 80.4% in the third quarter to 81.4% in the fourth quarter. A 1% improvement is $6 million per year increase in pre-tax profit.
- Management will be de-emphasizing certain geographic areas where returns on capital are too low such as Brazil and Southeast Asia.
- Management is not expecting any increase in the average day rate. For the entire fleet, the average day rate is about $10,000. The leverage from an increase of day rates can be tremendous. For example, at a fireside chat hosted by *Robotti & Company* on Jan 27th, 2019 for Quintin Kneen, CEO and Larry Rigdon, board chair of *Tidewater*, they highlighted the fact that at $20,000 day rates but below the rate of $35,000 to $40,000 needed to encourage any new buildings (ships) would produce $400 million in vessel gross profit—above TDW's current enterprise value of $315 million.

The emphasis on free cash flow is important as *Tidewater* navigates this industry trough because management wants to **maintain a strong balance sheet.** The company has no vessels under construction. Mr. Kneen believes, "*Tidewater's* path to improving free cash flow isn't predicated on recovery in the drilling market or further recovery in the offshore vessel market. It's based on designing a more efficient and scalable shore-based infrastructure, it is based on focusing our vessels in the fewest regions possible, while driving the highest margin on those vessels, it is about tightly managing required investment in those vessels, it is about rationalizing the fleet in layup, and about keeping the net debt low. Those are goals to develop the highest return on capital global offshore vessel company." (Source 4th quarter 2019 *Tidewater* conference call.)

Mr. Kneen's advises that *Tidewater* will have similar revenue levels as 2019 and 90% of its revenue is already contracted--a $440 million backlog--but with fewer vessels and lower operating costs, because fewer vessels are operating today—operating margins will improve.

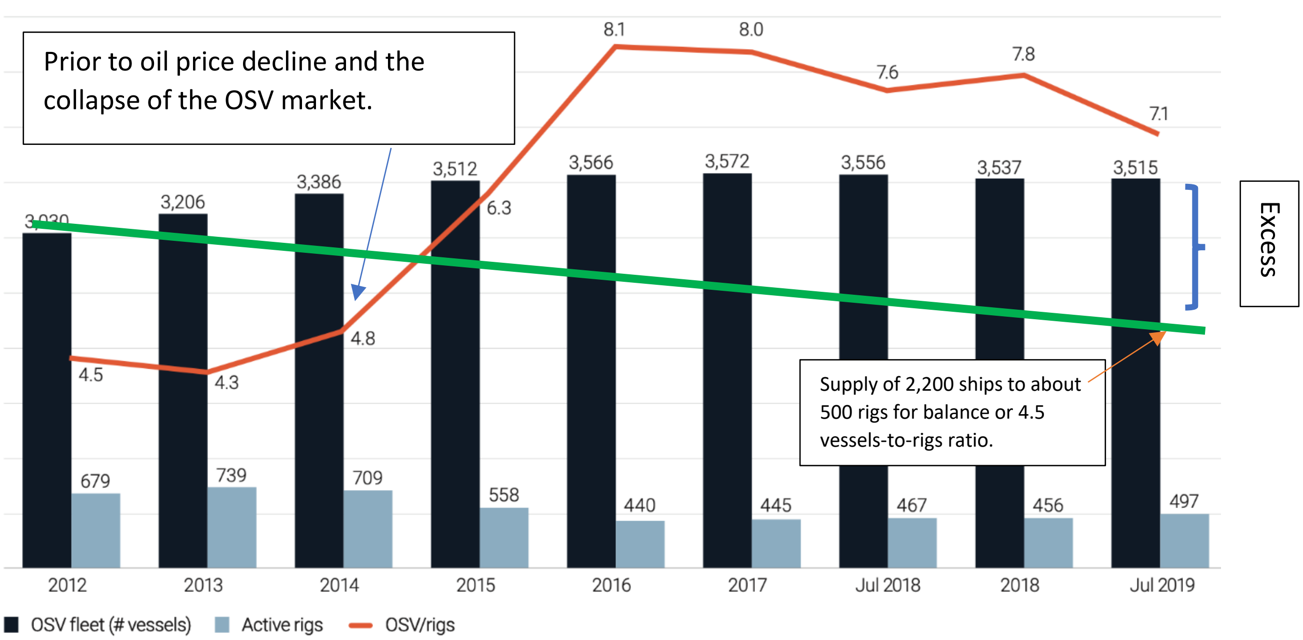
	2019	Pct	Est. 2020
Revenues:			
Vessel revenues		98.0%	$440,000
Other operating revenues	$9,534	2.0%	0.00
TOTAL REVENUES	$486,549	100.0%	$440,000
Costs and expenses:			
Vessel operating costs	$329,196	67.7%	$286,000
Costs of other operating revenues	$2,800	0.6%	$0
General and administrative	$103,716	21.3%	$82,000
Vessel operating leases	—		
Depreciation and amortization	$101,931	20.9%	$80,000
Gain on asset dispositions, net	-$2,263	-0.5%	
Impairment of due from affiliate	—		
Long-lived asset impairments and other	$37,773	7.8%	$0
TOTAL EXPENSES	**$573,153**	117.8%	$448,000
Operating loss	**-$86,604**	**-17.8%**	**-$8,000**
Other income (expense):		0.0%	
Foreign exchange gain (loss)	-$1,269	-0.3%	
Equity in net earnings (losses) of unconsolidated companies	-$3,152	-0.6%	
Interest income and other, net	$6,598	1.4%	$6,000
Reorganization items	—		
Loss on early extinguishment of debt	—		
Interest and other debt costs, net	-$29,068	-6.0%	-$21,000
TOTALS	**-$26,891**	**-5.5%**	**-$15,000**
Loss before income taxes	**-$113,495**	**-23.3%**	**-$23,000**
Income tax (benefit) expense	$27,724	5.7%	-$20,000
Net loss		0.0%	-$43,000
Less: Net income (losses) attributable to noncontrolling interests	$524	0.1%	
Net loss attributable to *Tidewater* Inc.		0.0%	
Basic loss per common share	-$4	0.0%	
Diluted loss per common share	(3.71)	0.0%	
Weighted average common shares outstanding	38,204,934	7852.2%	
Dilutive effect of stock options and restricted stock	—		
Adjusted weighted average common shares	38,204,934	7852.2%	

I calculate a loss of $8 million in operations on lower revenues of $440 million of contracted revenues while vessel operating costs decline from 67% to 65% of revenues because of fewer ships employed. Add back $80 million in depreciation then subtract $8 million in capital expenditures as per the guidance by Mr. Kneen to arrive at approximately $64 million in operating free cash flow. With the virtual shut-down of businesses in March and perhaps April and May, the above figure might be $50 or $60 million too high depending upon the effects of the recent economic turmoil. The market has already discounted the assets (market cap) by another 60% since February 2019. Provided the world does not go into a long-term depression, *Tidewater* should be at or above cash flow break-even in 4th quarter 2020.

The Supply and Demand Balance for Offshore Supply Vessels

The critical issue is whether the oversupply of vessels will improve. We know *Tidewater's* enterprise value of $315 million is far under its tangible book value of $990 million or its depreciated replacement cost of $3 to $4 billion. But assets are only worth the sum of their discounted cash flows. Utilization and charter rates depend roughly upon a balance between rig demand and the supply of vessels. See the ratio between vessels and drilling rigs below.

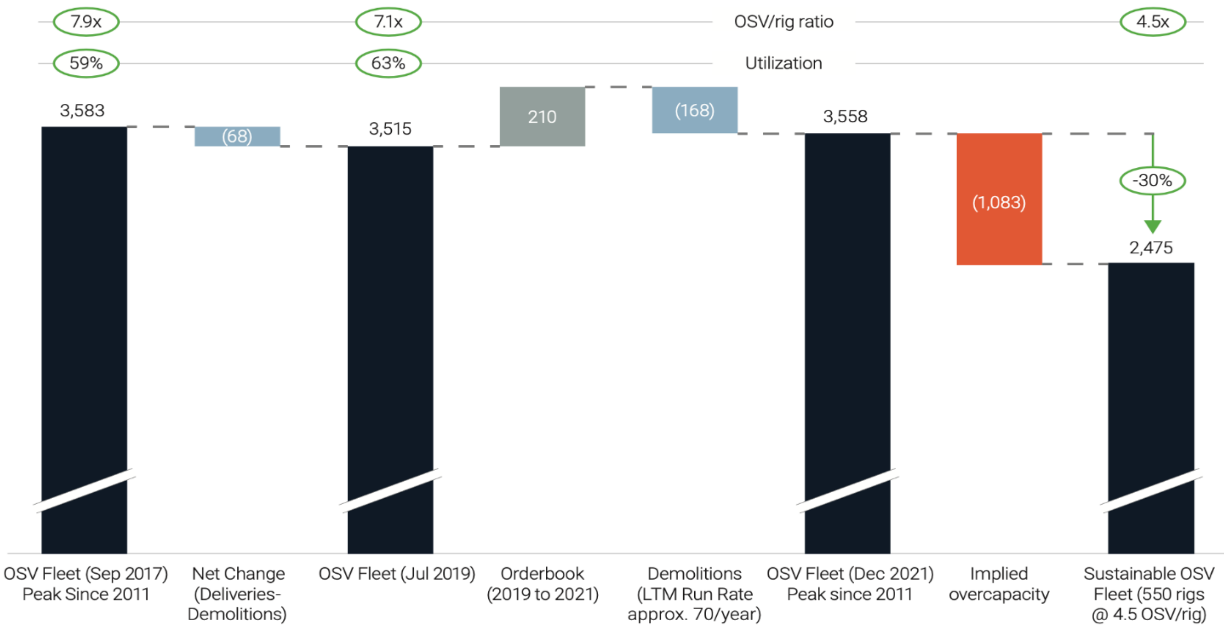
FIGURE 1: SUPPLY-DEMAND IMBALANCE SHOWS IMPROVEMENTS IN THE PAST 12 MONTHS BUT REMAINS THE BIGGEST DRAW ON OSV SECTOR



Source: Clarksons Offshore Intelligence Network, AlixPartners analysis
Note: OSVs include anchor-handling-tug-supply vessels of greater than 4,000 brake horsepower and platform supply vessels of greater than 1,000 deadweight tons

4.5 ratio of vessels to operating rigs implies a supply of **2236 vessels** (4.5 times 497 rigs as of July 2019) or (3,515-2,236 = 1,279 fewer vessels to be scrapped or leave the industry). Alix Partners estimated 1,100 vessels needed to leave the OSV market for market balance. See on the next page:

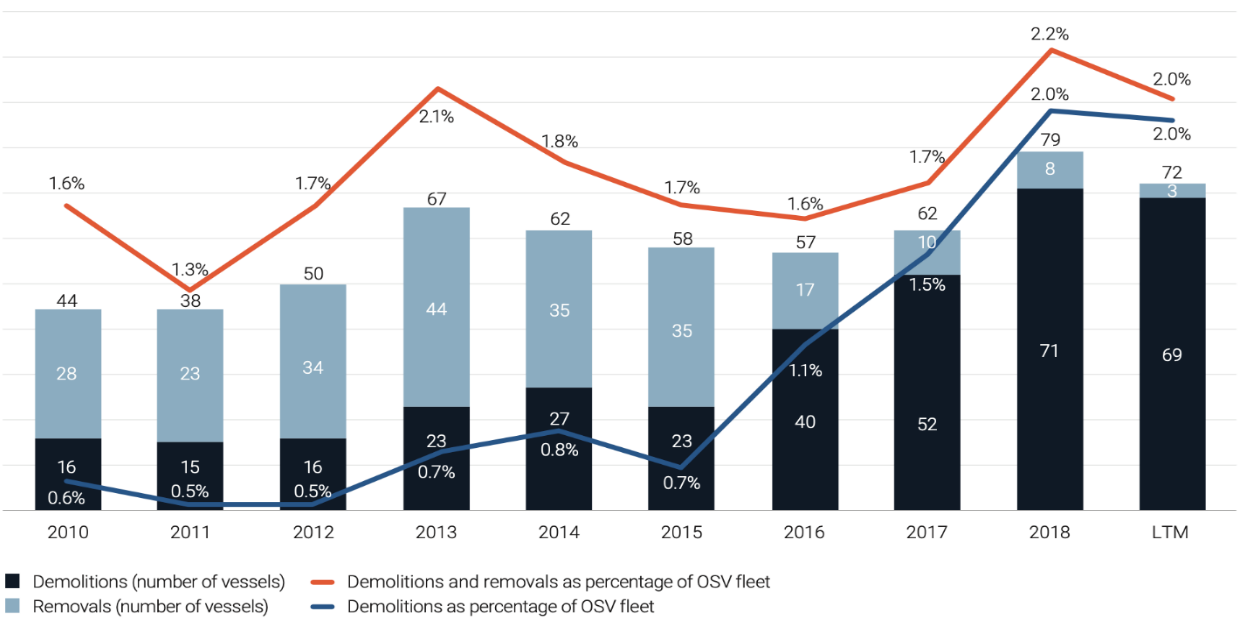
FIGURE 2: GLOBAL OSV MARKET IS STILL OVERSUPPLIED BY ABOUT 1,100 VESSELS



Sources: Clarksons Offshore Intelligence Network, AlixPartners analysis
Note: OSVs include anchor-handling-tug-supply vessels of greater than 4,000 brake horsepower and platform supply vessels of greater than 1,000 deadweight tons

Alix Partners points out that removals and demolitions are increasing but at 2% of the total fleet, sixteen years or more would have to pass at that rate to remove 1,100 vessels to be at a 2,400 fleet of operating vessels.

FIGURE 3: OSV DEMOLITION AND REMOVAL ACTIVITY RUNNING AT 60 TO 70 VESSELS PER YEAR



Sources: Clarksons Offshore Intelligence Network, AlixPartners analysis
Note: OSVs include anchor-handling-tug-supply vessels of greater than 4,000 brake horsepower and platform supply vessels of greater than 1,000 deadweight tons

The above graph would indicate that the rise out of this trough of vast oversupply of vessels is at least a decade and a half away! The time needed to balance the market appears to be too great for an investment in terms of the capital cycle.

Stacking and Scrapping

There is a large disconnect between the perceived vast oversupply of 1,100 to 1,200 vessels sitting in cold stack and what is the *true supply*. In other words, what vessels are economically viable to return to the OSV market?

First, the market for OSVs is bifurcating into higher charter rates of $14,500 per day for larger, higher spec platform supply vessels (PSVs) see slide 7. Utilization of 90% to 95% for 4,500 to 5,000 DWT ships vs. 73% average utilization rate, see slide 8. This means the type and class of vessel is important to meet customer specification. One would need to look at the types and age of vessels in stack. Currently, most large PSV are above 90% utilization.

Plattform Supply Vessel

An Anchor Handling Vessel

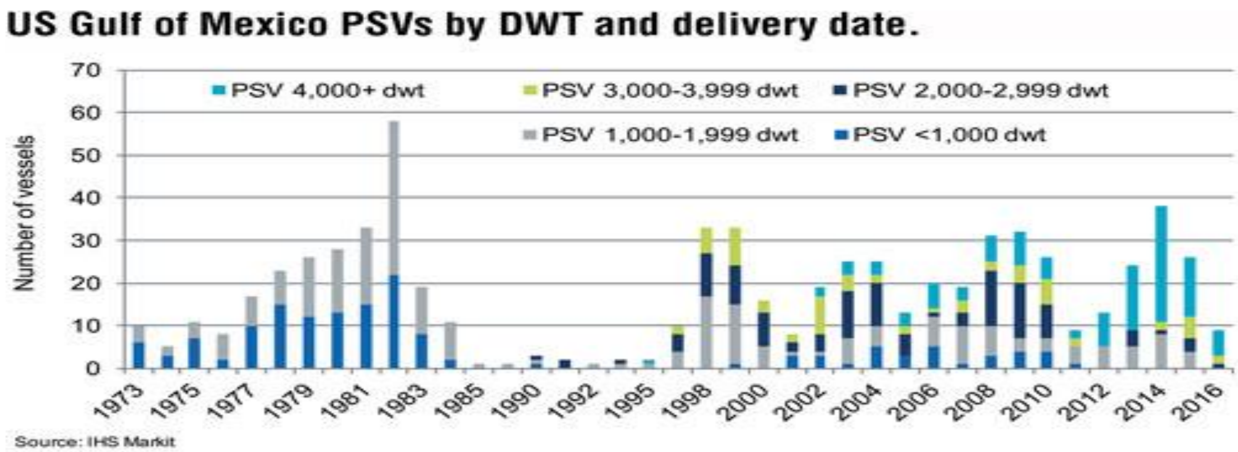
Operators say the benefits of vessel stacking are:

- Reduces operating expenses to between $500 and $1,500 per day per vessel or $360,000 per year.
- Able to defer cash outlays for vessel dry-dockings until market conditions improve
- Reduces the "wear and tear" on vessels and decreases incident rates and other operational risk
- Helps to rebalance the supply/demand equation by reducing excess tonnage
- Enhances vessel pricing and margins on the higher-spec actively marketed fleet (Source: *Hornbeck 2017 Presentation*).

The hulls of OSVs are often considered too small and contain too little steel to scrap profitably. Scrapping is occurring but most of the supply is leaving through natural obsolescence.

Let's hear what an industry expert has to say about supply:

Mr. Peter Laborde, CEO of Laborde Marine and son of John Laborde, said in 2018 that (See page 4) the last major down turn occurred with the overbuilding from 1979 to 1982. For example, there were seventy-five OSV operators in the Gulf of Mexico and 750 companies in the OSV industry. The trough took five-to-seven years before the upturn in 1990. There was overbuilding from 2009 to 2015 as shown in the diagram below. Seven years puts an upturn at 2016 to 2022 theoretically.



Mr. Laborde: "When the downturn began in 2014-2015, you saw vessels going to cold stack. **Once boats go through two cycles of five years each of not being dry-docked, you hit 2020, the likelihood of that boat coming back is not likely.** Boats can't return to the market unless they go through dry-docking and recertification, but how can owners afford to go through dry-docking because they don't have the money, or their debt is being restructured? The market may be assuming that most of the stacked fleet can return with increases in charter rates, but the reality is far different.

Also, world daily oil demand is 92 million barrels a day and with growth of 1% and replacement of depletion of 4% to 5%. Shale can't replace the oil needed, so the shift will inevitably be back to the offshore region. The market is underestimating future offshore activity not just in oil but also in offshore gas."

Please see slides 10-12 *Tidewater* September 2019 Presentation. Slide 10 shows that special surveys are required every five years costing $1 to $2 million or more and they often coincide with costly maintenance cycles. Costs increase with age due to technical obsolescence and likely increase in required overhauls. 450-active plus 204 stacked vessels should be due for a class certification (DNV, ABS, BV, etc.) in 2019. An additional 448 active plus 146 stacked vessels are due in 2020. Slide 12 estimates at least 850 vessels are candidates for demolition or removal from service because of the high cost to reactivate the vessel due to age and length of time stacked. More than five years as of 2019 have passed from the beginning of the market downturn which places most of the stacked vessels as uneconomic. Every day more vessels become too expensive to reactivate.

Remember that if you are an owner why would you return vessels to service without being able to recoup the investment in drydocking, recertification and maintenance ($2 million plus) while also operating the vessel. See my example of the calculations to return a stacked vessel to service on pages 6 and 7. The current charter rates of $9,000 to $10,000 would need to more than double. Also, with so many owners in financial distress (See page 29) with their debt far in excess of the market value of their fleets, why would they spend money to lose more money? If the current crisis has taught the bankers and private equity lenders anything, it is the rule that you do not lend money on assets without long-term contracts that cover operating and financial costs. The current market is unviable for every operator.

Before the Covid-19 crisis and Saudi/Russia price war, Mr. Kneen said, "Consolidation has been slower than anybody would prefer, because of all the facts and circumstances around people trying to hold onto their assets, a bit of self-preservation by management teams as well, but it seems to be coming to an end." Certainly, the recent plunge in equity, debt, and commodities prices will speed up the potential opportunities for *Tidewater* to purchase distressed assets or consolidate with the proper company.

Consolidation and more of a balance in terms of vessels required to meet customer needs provides tremendous upside leverage for *Tidewater*. See vessel revenues and operating costs on pages 32-36.

$477mil.	Revenues at $10,000 daily charter rates
-329	Op. Costs
-100	D&A
-47.5	G&A Ships
$0.250mil.	**Operating Profit**

Vessel revenues for 2019 were $477 million while operating costs were $329.2 million then deduct $100 million in depreciation and amortization and the $47.5 million general administrative expense for shore-based operations for each specific region, the profit is at cash break-even of $250,000. Of course, this does not cover the additional $35 million of corporate SG&A nor provide a return on capital for the risk taken to be invested. But at $20,000 daily rates--or $10,000 to $15,000 below the rates necessary to bring in new vessels or about double the current average rates *Tidewater's* vessels earn--the vessel operating cash flow would rise to $450 million or a 50% operating margin. You can see the high operational leverage in this high fixed-cost business. When business is bad it is very bad and vice a versa.

Tidewater **History to 2016**	**1998**	**1999**	**2000**	**2001**	**2002**
in $000's					
Revenues	$1,060,161	$968,992	$574,815	$616,679	$729,029
Net Earnings	$315,499	$210,719	$76,590	$86,143	$136,159
Capex			$57,362	$302,793	$317,907
LT Debt	$25,000	$0	$0	$0	$54,000
SE	$998,776	$1,067,707	$1,114,201	$1,178,340	$1,285,818
Debt/Equity	***2.50%***	***0.00%***	***0.00%***	***0.00%***	***4.20%***
Cash Dividends	$0.60	$0.60	$0.60	$0.60	$0.60
Mkt. Price	$43.81	$25.88	$31.81	$45.20	$42.35
Shs. Outstanding	60,552,315	57,189,946	55,546,832	55,741,624	56,054,797
Mkt. Cap.	2,652,797	1,480,076	1,766,945	2,519,521	2,373,921
Book Value	$16.49	$18.67	$20.06	$21.14	$22.94
Mkt. P/BV	2.6x	1.4x	1.6x	2.1x	1.8x
Net Cash from Ops.		$254,364	$235,062	$153,177	$194,390
Net cash from Ops/Eqty		***23.82%***	***21.10%***	***13.00%***	***15.12%***
Vessel Count			618	571	555
	2003	**2004**	**2005**	**2006**	**2007**
in $000's					
Revenues	$635,823	$652,630	$692,150	$877,617	$1,125,260
Net Earnings	$88,630	$41,662	$101,339	$235,756	$356,646
Capex	$269,620	$297,515	$207,391	$172,408	$235,182
LT Debt	$139,000	$325,000	$380,000	$300,000	$300,000
SE	$1,351,395	$1,366,110	$1,442,702	$1,659,121	$1,886,010
Debt/Equity	***10.29%***	***23.79%***	***26.34%***	***18.08%***	***15.91%***
Cash Dividends	$0.60	$0.60	$0.60	$0.60	$0.60
Mkt. Price	$28.72	$28.13	$38.86	$55.23	$58.58
Shs. Outstanding	56,413,856	56,563,328	56,854,282	57,372,815	55,914,998
Mkt. Cap.	1,620,206	1,591,126	2,209,357	3,168,700	3,275,500
Book Value	$23.96	$24.15	$25.38	$28.92	$33.73
Mkt. P/BV	1.2x	1.2x	1.5x	1.9x	1.7x
Net Cash from Ops.	$202,000	$129,049	$160,062	$293,254	$435,095
Net cash from Ops/Eqty	***14.95%***	***9.45%***	***11.09%***	***17.68%***	***23.07%***
Vessel Count	545	575	563	523	463
	2008	**2009**	**2010**	**2011**	**2012**
in $000's					
Revenues	$1,270,171	$1,390,835	$1,168,634	$1,055,388	$1,067,007

Net Earnings	$348,763	$406,898	$259,476	$105,616	$87,411
Capex	$354,022	$473,675	$451,973	$615,289	$357,110
LT Debt	$300,000	$300,000	$275,000	$700,000	$950,000
SE	$1,930,084	$2,244,678	$2,464,030	$2,513,944	$2,526,357
Debt/Equity	***15.54%***	***13.36%***	***11.16%***	***27.84%***	***37.60%***
Cash Dividends	$0.60	$1	$1	$1	$1
Mkt. Price	$55.11	$37.13	$47.27	$59.85	$54.02
Shs. Outstanding	54,259,495	51,364,237	51,447,077	51,221,800	51,165,460
Mkt. Cap.	2,990,241	1,907,154	2,431,903	3,065,625	2,763,958
Book Value	$35.57	$43.70	$47.89	$49.08	$49.38
Mkt. P/BV	1.55	0.85	0.99	1.22	1.09
Net Cash from Ops.	$486,842	$523,889	$328,261	$264,206	$222,421
Net cash from Ops/Eqty	***25.22%***	***23.34%***	***13.32%***	***10.51%***	***8.80%***
Vessel Count	460	430	304	378	342

	2013	**2014**	**2015**	**2016**
in $000's				
Revenues	$1,244,165	$1,435,103	$1,495,517	$979,062
Net Earnings	$150,750	$140,255	-$65,190	-$160,183
Capex	$440,572	$403,685	$364,194	$194,485
LT Debt	$1,000,000	$1,505,358	$1,524,295	Default
SE	$2,561,756	$2,679,384	$2,474,488	$2,299,520
Debt/Equity	***39.04%***	***56.18%***	***61.60%***	***NA***
Cash Dividends	$1	$1	$1	$0.75
Mkt. Price	$50.50	$56.00	$48.00	$5.00
Shs. Outstanding	49,550,391	49,730,442	47,029,399	47,067,715
Mkt. Cap. Full amt	2,502,294,746	2,784,904,752	2,257,411,152	235,338,575
Book Value	$51.70	$53.88	$52.62	$48.86
Mkt. P/BV	1.0x	1.0x	0.9x	0.10
Net Cash from Ops.	$213,921	$104,617	$358,713	$253,360
Net cash from Ops/Eqty	***8.35%***	***3.90%***	***14.50%***	***11.02%***
Vessel Count	328	294	289	

The above financial history can provide a rough outline of *Tidewater's* cyclicality and past debt and profit ratios. *Tidewater* has a substantially different fleet than 20 years ago and more of its customers have consolidated.

Vessel Utilization and Average Rates by Segment

SEGMENT STATISTICS:	Year Ended December 31, 2019		Year Ended December 31, 2018
Americas fleet:			
Utilization	54.40	%	46.10
Average vessel day rates	11,796		13,987
Average total vessels	58		51
Average stacked vessels	(21)		(22)
Average active vessels	37		29
Middle East/Asia Pacific fleet:			
Utilization	**63.80**	%	57.00
Average vessel day rates	7,458		7,482
Average total vessels	52		52
Average stacked vessels	(10)		(12)
Average active vessels	42		40
Europe/Mediterranean fleet:			
Utilization	**60.90**	%	64.30
Average vessel day rates	**12,052**		9,637
Average total vessels	46		25
Average stacked vessels	(13)		(6)
Average active vessels	33		19
West Africa fleet:			
Utilization	50.40	%	49.60
Average vessel day rates	9,338		9,196
Average total vessels	73		85
Average stacked vessels	(23)		(31)
Average active vessels	50		54
Worldwide fleet:			
Utilization	56.50	%	52.20
Average vessel day rates	10,046		9,809
Average total vessels	229		213
Average stacked vessels	(67)		(71)
Average active vessels	162		142

December 31,

2019

AVERAGE NUMBER OF VESSELS:

Americas fleet:	
Deepwater	31
Towing-supply	17
Other	4
Total	52
Stacked vessels	(15)
Active vessels	37
Middle East/Asia Pacific fleet:	
Deepwater	27
Towing-supply	28
Total	55
Stacked vessels	(10)
Active vessels	44
Europe/Mediterranean fleet:	
Deepwater	42
Towing-supply	3
Total	45
Stacked vessels	(15)
Active vessels	30
West Africa fleet:	
Deepwater	27
Towing-supply	19
Other	21
Total	67
Stacked vessels	(22)
Active vessels	45
Worldwide fleet:	
Deepwater	126
Towing-supply	68
Other	25
Total	219
Stacked vessels	(62)
Active vessels	157
Total active	157
Total stacked	62
Total joint venture and other vessels	4
Total	223

***Tidewater* Inc.**

Fleet Summary

as of September 30, 2019

Worldwide Fleet

Type	Active	Stacked	Total
AHTS	45	27	72
PSV	99	24	123
Other	16	9	25
Total	**160**	**60**	**220**

Total Vessels (Active + Stacked) by Category & Region

Region	Deepwater	Towing Supply	Other	Total
Americas	32	16	4	52
Middle East/Asia Pacific	24	26	0	50
Sub-Saharan Africa	30	20	21	71
Europe/Mediterranean	44	3	0	47
Total	**130**	**65**	**25**	**220**

Total Active Vessels by Category & Region

Region	Deepwater	Towing Supply	Other	Total
Americas	26	9	3	38
Middle East/Asia Pacific	18	21	0	39
Sub-Saharan Africa	23	13	13	49
Europe/Mediterranean	32	2	0	34
Total	**99**	**45**	**16**	**160**

		December 31, 2019	
(In thousands)			%
Vessel revenues:			
Americas	$	136,958	29%
Middle East/Asia Pacific		90,321	19%
Europe/Mediterranean		123,711	26%
West Africa		126,025	26%
Total vessel revenues	$	477,015	100%

(In thousands)		
Vessel operating costs:		
Americas:		
Crew costs	$	63,521
Repair and maintenance		12,076

Insurance		227
Fuel, lube and supplies		8,332
Other		12,086
		96,242
Middle East/Asia Pacific:		
Crew costs	$	37,164
Repair and maintenance		9,409
Insurance		1,921
Fuel, lube and supplies		9,053
Other		7,759
		65,306
Europe/Mediterranean:		
Crew costs	$	51,018
Repair and maintenance		13,416
Insurance		2,124
Fuel, lube and supplies		6,627
Other		10,652
		83,837
West Africa:		
Crew costs	$	35,896
Repair and maintenance		12,860
Insurance		1,857
Fuel, lube and supplies		12,347
Other		20,851
		83,811
Total:		
Crew costs	$	187,599
Repair and maintenance		47,761
Insurance		6,129
Fuel, lube and supplies		36,359
Other		51,348
Total Vessel Operating Costs	**$**	**329,196**

	Year Ended December 31, 2019 (A)		
(In thousands)			
Vessel operations general and administrative expenses:			
Americas (B)	$	14,028	10%
Middle East/Asia Pacific		9,618	11%
Europe/Mediterranean (C)		11,110	9%
West Africa		12,751	10%

Total vessel operations general and administrative expenses	**$**	**47,507**	10%

		Year Ended December 31, 2019	
(In thousands)			%
Depreciation and amortization expense:			
Americas	$	27,493	20%
Middle East/Asia Pacific		21,440	24%
Europe/Mediterranean		30,053	24%
West Africa		21,166	17%
Total depreciation and amortization expense	**$**	**100,152**	21%

Tidewater's most recent fleet status **https://investor.tdw.com/shareholder-services/online-investor-kit** It lists the type, age, and status of every vessel in its fleet.

Market Conditions and Outlook Prior to Covid-19 and Saudi/Russia oil price war

*Mr. Quintin Kneen and other OSV CEOs discuss the market in April **2016**.*

Mr. Quintin Kneen, CEO of *Gulfmark* and other OSV CEOs discuss the market in **May 2017**: https://www.marinemoney.com/speech/osv-owners-panel *The audio is important because the discussion focuses on the need to rationalize fleets and market* consolidation. The consolidation is expected to occur in regions.

Mr. Mr. Kneen and John Rynd of *Tidewater* on a OSV Panel 2018

Here is the outlook from a panel of owners in the OSV market (May 2019) Marine Money.mp3 There is oversupply, but improving prices.

NEWS SOURCES

1. workboat.com
2. Tradewindsnews.com

BOURBON CORPORATION

The presenter explains the difficulties faced before management filed for bankruptcy, liquidation, and transfer to new owners. Bourbon Corporation

http://bourboncorporation.com/wp-content/uploads/2020/01/facts-and-figures-2018.pdf'

As a reminder, all the assets and activities of Bourbon Corporation were sold to *Societé Phocéenne de Participations* (SPP), which became the new shareholder of Bourbon Maritime and owner of the BOURBON brands in 2020.

See slide 33 as an example of naïve extrapolation of market trends. The good times never last.

SIEM OFFSHORE

Siem Offshore 2018 Annual Report on the market outlook:

> The year 2018 has been another challenging year for the OSV market where almost all segments have struggled with low utilization and charter rates not sustainable to cover operating expenses and debt repayment. There are still too many vessels available in the market to make progress towards a balance in the supply and demand of OSV fleet. Several OSV owners decided to accept medium and long-term contracts with marginal EBITDA contribution, sometimes even at a negative level in order to maintain utilization. The consolidation efforts conducted over the past years have so far not contributed to a strengthened market, mainly due to such Owners' strategic focus on retaining utilization rather than using their improved market position to aid in increasing the obtainable rate levels.
>
> The positive trend we saw in the start of 2018 did not last throughout the year and, although the activity increased compared to 2017, the planning and operations were better organized by the operators, which gave the market less vessel days overall. We expect increased activity in the coming years, although there is still some path to cover before we see profitable rates obtainable for long term business after interest and debt repayment is covered. Continued and increased scrapping activity of obsolete tonnage is necessary in order to progress towards a balance situation for the OSV fleet. Financing banks and owners must take their responsibility and regulate players under their control in order to create a sustainable platform for the profitability of the industry.

STANDARD DRILLING

Standard-Drilling Presentation.pdf

41.1 mil cash and no debt see Standard-drilling financial-reports 2019 Q4-2019

The Company's results in 2019 show that the PSV market is moving in the right direction after several challenging years. Already into the winter season the Company's short-term focus is to secure winter coverage of the vessels and to take part in an expected upturn in the market in the North Sea Sector during the spring and summer season of 2020.

The Company has a sound financial position and the Board of Directors believe that the Company is well positioned to take advantage of opportunities that may appear in the PSV market in the North Sea Sector, the shipping industry and elsewhere going forward. This includes, but is not limited to, asset play or investment directly in other companies. The main drivers are maximizing the return and minimizing the risk.

See slides 11-13 discussing the potential for reactivating PSV in the North Sea https://www.standard-drilling.com/images/pdf/events/2019/SDSD-4Q-2019-Presentation.pdf

Hermitage

See slides 9 and 10 for signs of strengthening market in floaters Hermitage Company Presentation-3.07.19.pdf

EIDESVIK

Market

PSV • Increase in spot and term demand year on year has led to improved rates and utilization, for the larger PSVs. • Still oversupply of vessels, and the overall market remains challenging. • Maintain a positive view on the market for large and modern PSVs

DOF ASA

Outlook: The North Sea markets within supply (PSV and AHTS) have continued to prove better utilization, however, even with the modest improvement in rates and utilization for the AHTS fleet, the average earnings are not sustainable. As part of seasonal variations, the North Sea market activity has declined so far in 2020. In Brazil, the market is expected to be weak the next 12 months. The Group has several contracts up for renewal in 2020, which increases the risk regarding utilization and earnings in this region. Earnings for the Subsea IMR fleet have been better in the quarter compared to the same period last year and the Asia-Pacific and North America region have proven increased activity. However, there is still an oversupply of vessels and the Group expects reduced earnings in certain regions and especially in the North Sea during the winter season.

The Group will maintain its strategy to secure the fleet on term contracts and is actively working on keeping the firm employment of the fleet as high as possible. Most the Group's high-end vessels are committed on firm contracts and represent the largest portion of the Group's backlog. The OSV sector has the last few years experienced very challenging market conditions and the recovery has taken longer than expected. Nevertheless, the Group's backlog is still high.

A continuing weak market brings a risk of lower utilization and earnings of the Group's vessels and further increases the liquidity risk for the Group.

DOF/DOF ASA 20Q4 2020 Financial Report.pdf

SOLSTAD OFFSHORE

FINANCE In light of a difficult financial situation, a number of the companies within the Group have entered into agreements with a number of their key financial creditors for the suspension and deferral of payments until 31 March 2020.

The number of vessels that are in lay-up, globally, might put pressure on rate-levels. But, the <u>combination of</u> specification, age, condition and activation cost will make a substantial part of this fleet irrelevant for future contracts.

See the financial condition of public companies compared to *Tidewater*:

Company	Symbol	Stock Price	OS Shs. In mil.	MC in mil.	Cash Mil.	Debt Mil.	Net Debt	MC/Net Debt	News
Hornbeck	Hoss	$0.10	38	$3.80	136	$1,040	904	0.42%	Hornbeckoffshore
Siem Offshore	SIOFF	0.08	942	$75.36	73.2	1060	986.8	7.64%	Siem offshore
Bourbon	NA	NA	NA	NA	NA	Bankrupt	NA	Bankrupt	Bourbon Offshore
Standard Drilling	SDSD	$0.064	$576	$37	$41.1	NA	-41.1	No Debt	Standard Drilling
Hermitage Offsh	PSV	0.45	7.65	$3.44	12.6	142	129.4	2.66%	Hermitage Offshore
Eidesvik Offshore	EIOF.OL	$0	$63	$21	$408	$2,400	$1,992	1.07%	Eidesvik.no/
DOF ASA	DOF.OL	0.067	308	$20.64	146	1530	1384	1.49%	DOF.no
Seacor Marine* *1/2 non-recourse debt	SMHI	4.75	22	$104.50	84	380	296	35.30%	*Seacor* Marine
Solstad	SOFF	0.0442	291.4	$12.88	$96	$429	$333	3.87%	Solstad
Tidewater	TDW	5.5	42.4	$233.2	218	279	61	**382.30%**	*Tidewater*

Those are some of the largest competitors to *Tidewater*. **Note that *Tidewater* has almost 4 times the market cap to net debt even at today's panic prices** (Covid-19 Virus pandemic and oil price war with WTI crude near $23 on March 19th, 2020). Standard Drilling has net cash but only four PSVs and 25% ownership in nine other OSVs in addition to a 1/3 ownership in a VLCC tanker. *Seacor Marine* if you back out ½ their non-recourse debt has about 1 time its market cap to net debt. *Seacor Marine* with its fast boat fleet is in slightly different markets than *Tidewater* **but may offer a consolidation opportunity.** As per the 4th quarter 2019 earnings conference call, Quintin Kneen said there are nearly 600 participants and only four, including *Tidewater*, have more than 2.5% of the market.

MARKET EXTREMES

Note the current market extremes. **Should SDSD's fleet have a negative value?** *Click on Go to Standard-Drilling Investor Relations*

SDSD has a current market cap in USD (1 NOK = $0.085 USD) of $37 million with cash as of Dec. 31, 2020 of $41.1 million or a **negative enterprise value of $4 million dollars.** You are being paid to own its fleet:

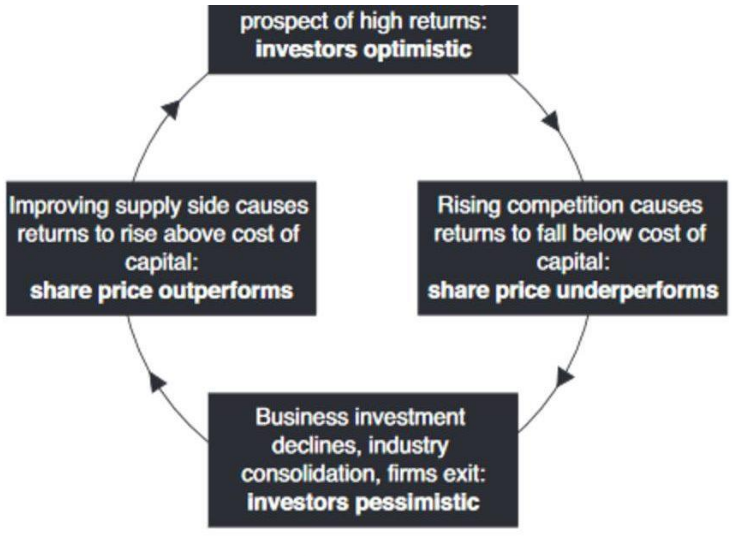
> Standard Drilling, through wholly owned Norwegian subsidiaries, has 100% control of four large PSVs, the Standard Viking, Standard Supplier Standard Princess and Standard Olymbus.
>
> And Standard Drilling has acquired in January 2020 a 33.3 % ownership in ZETA Owners Inc., a company register in Marshall Islands, which resulted in a part ownership in one VLCC tanker. Built in 2020, the VLCC with hull number 5469 is named "Gustavia S" and is a 300 000 TDW ECO Design Crude Oil Tanker built by Daewoo Shipbuilding & Marine Engineering Co and fitted with scrubber technology delivered by Wärtsila. TMS Tankers Ltd will act as technical and commercial manager.
>
> The cost of a new VLCC Tanker is about $100 to $120 million.
>
> So SDSD's ownership stake should be worth about $30 million. SDSD has other assets:
>
> Standard Drilling, through its wholly owned Norwegian subsidiary, WANAX AS, has an ownership of 25% in 9 mid-sized vessels, including FS Arendal, which is on a bare-boat contract.

Negative enterprise value indicates a distorted market, in my opinion, exacerbated by the liquidity needs of stressed investors during these times of market turmoil.

SDSD is cheaper than *Tidewater* but it is too small to consolidate the industry. But the price given to SDSD's fleet indicates the consolidation opportunities in front of *Tidewater*.

SUMMARY and CONCLUSION

"Try to buy assets at a discount rather than earnings. Earnings can change dramatically in a short time. Usually, assets change slowly. One has to know how much more about a company if one buys earnings."   - Walter Schloss



The goal of this case study is to help an investor think about how to invest in the capital cycle using Tidewater (TDW) as an example. The success of an investment in TDW requires a deep understanding of the capital cycle, faith in management's skill and experience to navigate through the cycle by lowering costs and allocating capital wisely, a strong balance sheet and solid assets to protect the equity value through the downcycle, and—most importantly—the patience and a strong stomach to weather the volatility and time needed for improving conditions to manifest. No one knows *when* the cycle turns. Please read Mr. Laborde's comments on pages 15-16 about the last major trough of 1987.

The Offshore Supply Vessel ("OSV") industry is at the bottom of its capital cycle as shown by the above diagram. Companies are consolidating; note *Tidewater's* merger with Gulfmark in 2018. There is no new building or ordering of vessels. Competitors have debt far exceeding the values of their fleets (See page 39). Firms like Bourbon are in default and being sold (See page 37). Companies are capital constrained (See page 39). Therefore, many older vessels, for example, 15 years and older that have been in stack will be too costly to return to service. The market perceives a greater supply—the 1,200 boats in stack--than is available to return. (See slide 13 as an example of a fleet rusting in place).

Investors are pessimistic as *Tidewater's* market cap and enterprise value trades at 1/8th to 1/10th replacement value which indicates the price of new supply entering the market. Since an asset is only worth its discounted cash flows at an appropriate cost of capital, charter rates currently at $10,000 per day would need to triple and be steady for any new building to occur or justify the significant investment to return older boats to service.

Tidewater's strong balance sheet of only $61 in net debt as of year-end 2019 relative to its competitors can allow management to consolidate further to drive out costs and be opportunistic in acquiring the proper assets to strengthen its fleet. Note the disconnect of prices to assets of *Standard Drilling* on page 40 where SDSD's enterprise value trades at a negative value to its fleet!

Tidewater's balance sheet, modern, high spec fleet and management (Mr. Rigdon, Chairman) who has gone through the last major cycle of 1982-1990 should allow Tidewater to emerge on the left side moving counter clockwise on the diagram where an improving supply side causes returns to rise above the cost of capital and the share price outperforms. Obviously, the TDW's share price is not rising and returns at cash flow break-even are far below the costs of capital. **However, there is a large gap between current cash flow break-even and returns high enough to bring in supply.** Charter rates of 10,000 per day would need to rise to $30,000 to $40,000 which would cause the share price to rise closer to replacement values of new vessels but that will take several years in my opinion. Prices given the high volatility have discounted extreme outcomes and offer an investor a chance to buy quality assets at a huge discount. Recent insider buying shows confidence in the future despite the recent uncertainty of Covid-19 and the Saudi-Russian oil price war.

All aspects of the investment thesis need to work for a successful outcome. A strong Tidewater balance sheet coupled with financially stressed competitors allow greater odds for consolidation and opportunistic purchases of assets while time causes further erosion of supply. An experienced management team that is focused on returns rather than growth and having been through the last major downturn of 35 years ago increases the odds of success. Prior to the recent upheaval, rising utilization and charter rates showed slowly improving fundamentals.

The risk is that financial subsidies to either oil drillers and/or OSV operators may prolong this downcycle which ultimately might impair Tidewater. Though Tidewater may be at cash flow break-even or slightly improving its free cash flow, its charter rates need to double or triple for the company to earn its cost of capital or for management to set aside adequate cash to replace its fleet over time. My expected values are below but reach your own conclusions. An investor buys asset in distress for a move to normalization.

$6.00 current share price on March 19th, 2020		
Expected values	**Probability**	**Target**
-$0.60	10%	-$6 bankruptcy (total loss) within five years
-$0.75	25%	-$3 a decline of 50% as low rates persist for longer
$1.50	25%	$6 (price doubles) as a lessening of fear and uncertainty 2H 2020
$2.80	20%	$14 a lessening of fear, stabilizing rates 2021
$1.90	10%	$19 improving rates in 2022/23
$4.40	10%	$44 further improving rates in 2023/24
$9.25	**100%**	***9%* compounded annual return over five years.**

Additional Notes

Private Equity Firms exiting the shipping market Marine Money Hamburg 2020

Second hand debt of shipping firms Marine Money Hamburg 2020

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The goal is to inve3st in companies from sectors where capital was being withdrawn and to avoid companies in industries where assets were increasing rapidly.

The insight being that both profits and valuations should generally rise after capital has exited an industry and decline after capital has poured in.   Capital cycle analysis was all about the drivers of mean reversion

W

Don't buy stocks which are cheap on accounting measures (P/E, price-to-book, etcv.) and to avoid those which are expensive on the same basis, but rather to look for investments trading at low prices relative to the investor's estimate of their intrinsic value.

A growth stock usually becomes a value stock after excess capital, lured ibn by large current profitability, btrings about a decline in returns.

Value traps.

Stocks should be viewed not as "growth" or "value" opportunities, but rather from the perspective of whether the market is efficiently valuing their future earnin prospects.

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Even if one has developed the anbalytical skills to spot the winner, the psychological disposition necessary to own shares for prolonged periods is not easily come by.

There is less competition out there for the really valuable bits of information.

Price is what you pay and value is what you get. By this definition, every serious investor must be a value investor.

Investors like modelling because it appears scientific.   Investment models, however, encourage anchoring.   Detailed forecasting adds little value.

Traditional valuation measures say nothing about the specific context of an investment—for instance, a company's business model, its industry structure, and management'[s ability to allocate4 capital—which determines future cash flows.

END