Financial Report For the Period Ended December 31, 2016

This Financial Report is presented for Shelf Drilling Holdings, Ltd (the "Company"). The financial and operational data included in this report covers the three and twelve months ended December 31, 2016.

Introduction

This report comments on the financial performance of the Company and on the table of results set out on page 4. A complete listing and description of defined terms and the methodology of calculating EBITDA and Adjusted EBITDA are set out in the Explanatory Notes.

"Q4 2016" and "Q4 2015" are used to refer to the three month periods ended December 31, 2016 and 2015, respectively.

Highlights

- Total revenue of $156.1 million in Q4 2016 decreased by $42.7 million (21.5%) compared to Q4 2015 primarily due to the decrease in average dayrates
- Total operating expenses decreased by $18.0 million (19.0%) in Q4 2016 compared to Q4 2015 mainly reflecting cost savings achieved by the Company as well as a reduction in the number of marketable rigs
- Selling, general and administrative expenses decreased by $2.1 million (10.2%) in Q4 2016 compared to Q4 2015 reflecting cost reduction initiatives
- Provisions for doubtful debt of $7.4 million and $48.0 million were recorded in Q4 2016 and Q4 2015, respectively, related to the uncertainty of collectability for specifically identified accounts receivable
- Adjusted EBITDA in Q4 2016 of $53.9 million increased by $21.1 million (64.3%) compared to Q4 2015 mainly due to lower provision for doubtful debt and cost savings in operating expenses, partly offset by lower average dayrates
- Q4 2016 Capital and Deferred Expenditure totaled $50.7 million compared to $58.8 million in Q4 2015. This included $31.7 million related to the construction of the two newbuilds (Q4 2015: $12.0 million)
- The Company's first newbuild started its five-year contract with Chevron in Thailand on December 1, 2016 after completing final customer acceptance requirements
- $1.7 billion in contract backlog at December 31, 2016 across 25 contracted rigs (including one newbuild rig under construction) with a weighted average backlog dayrate of $96.7 thousand

Revenues

Total revenue was $156.1 million in Q4 2016 compared to $198.8 million in Q4 2015. The decrease in total revenue was largely due to the 24.5% decrease in average dayrates from $94.0 thousand in Q4 2015 to $70.9 thousand in Q4 2016, and the decline in average marketable rigs from 35.0 in Q4 2015 to 31.3 in Q4 2016. This was partially offset by a higher marketed utilization of 71% in Q4 2016 compared to 61% in Q4 2015.

Total revenue for the twelve months ended December 31, 2016 was $684.3 million compared to $1,030.3 million for the same period in 2015. The decrease in total revenue was largely due to the 28.0% decrease in average dayrates from $104.3 thousand in 2015 to $75.2 thousand in 2016, and the decline in average marketable rigs from 34.5 in 2015 to 31.2 in 2016. This was partially offset by a higher marketed utilization of 74% in 2016 compared to 72% in 2015.

Within the marketable rig fleet, nine rigs were idle awaiting marketing opportunities at the end of Q4 2016 compared to four rigs at the end of Q4 2015. During Q4 2016 one rig was undergoing a major project compared to seven rigs in Q4 2015. There were 32 marketable rigs and one rig under a three year bareboat charter contract at the end of December 31, 2016.

Operating Expenses

Total operating expenses decreased by $18.0 million (19.0%) in Q4 2016 to $76.5 million compared to $94.5 million in Q4 2015. This decrease was mainly due to lower expenses for rigs which were seeking marketing opportunities in Q4 2016 compared to Q4 2015 ($9.0 million), cost savings generated by the Company across the fleet ($4.1 million), lower expenses for rigs which were stacked in Q4 2016 compared to operating in Q4 2015 ($3.7 million) and lower maintenance and shipyard expenses ($0.9 million).

Total operating expenses for the twelve months ended December 31, 2016 decreased by $164.8 million (34.2%) to $317.5 million compared to $482.3 million for the same period in 2015. This decrease was mainly due to cost savings generated by the Company across the fleet ($54.8 million), lower expenses for rigs which were seeking marketing opportunities in 2016 compared to 2015 ($54.2 million), lower expenses for rigs which were stacked in 2016 compared to operating in 2015 ($26.5 million) and lower maintenance and shipyard expenses ($25.3 million).

Selling, General and Administrative Expenses

Selling, general and administrative expenses were $18.5 million in Q4 2016 compared to $20.6 million in Q4 2015 largely due to cost savings in all expense categories.

Provision for doubtful debt, which relates to the uncertainty of collectability for specifically identified accounts receivable, was $7.4 million in Q4 2016 compared to $48.0 million in Q4 2015.

Selling, general and administrative expenses decreased by $21.2 million (21.6%) to $77.1 million for the twelve months ended December 31, 2016 compared to $98.3 million for the same period in 2015, largely due to cost savings in all expense categories.

Provision for doubtful debt, which relates to the uncertainty of collectability for specifically identified accounts receivable, was a net favorable impact of $0.4 million in 2016 following customer collections compared to an unfavorable impact of $87.4 million in 2015.

Adjusted EBITDA

Adjusted EBITDA for Q4 2016 was $53.9 million compared to $32.8 million for Q4 2015, an increase of $21.1 million, or 64.3%. The Adjusted EBITDA margin for Q4 2016 was 34.5% compared to 16.5% in Q4 2015.

Adjusted EBITDA for the twelve months ended December 31, 2016 was $295.5 million compared to $372.2 million for the same period in 2015, a decrease of $76.7 million, or 20.6%. The Adjusted EBITDA margin for the twelve months ended December 31, 2016 was 43.2% compared to 36.1% for the same period in 2015.

Capital and Deferred Expenditure

Capital and Deferred Expenditure can vary significantly from quarter to quarter and year over year depending on the timing of required work on rigs for special periodic surveys, underwater inspections, periodic major overhauls of equipment, contract preparations, refurbishments and upgrades required under new contract specifications as well as the timing of any rig reactivations or newbuilds under construction.

Capital and Deferred Expenditure was $50.7 million in Q4 2016 compared to $58.8 million in Q4 2015. Capital and Deferred Expenditure decreased by $8.1 million due to the significant decline in non-newbuild capital and deferred expenditure from $46.8 million in Q4 2015 to $19.0 million in Q4 2016, partly offset by the increase of $19.7 million attributable to the two newbuild rigs under construction, from $12.0 million in Q4 2015 to $31.7 million in Q4 2016.

Capital and Deferred Expenditure was $257.3 million for the twelve months ended December 31, 2016 compared to $323.2 million for the same period in 2015. Capital and Deferred Expenditure decreased by $65.9 million due to the significant decline in non-newbuild capital and deferred expenditure from $227.9 million in 2015 to $67.4 million in 2016, partly offset by the increase of $94.7 million attributable to the two newbuild rigs under construction, from $95.3 million in 2015 to $190.0 million in 2016.

Following the delivery of the Company's first newbuild on September 29, 2016 from Lamprell, Plc. in the UAE, the rig started its five-year contract with Chevron in Thailand on December 1, 2016 after completing final customer acceptance requirements. The second newbuild is scheduled for delivery in the second quarter of 2017.

Outlook

Demand for the Company's fleet of shallow water drilling rigs is driven by customer spending, which can experience fluctuations depending on current commodity prices and market expectations of future price levels. The business environment for offshore drillers remains very challenging, as operators have announced declines in spending and cancelled or deferred projects over the last two years in light of the precipitous drop in crude oil prices. Although crude oil prices have begun to recover and stabilize in recent months, we believe that the market outlook continues to be more challenging compared with previous years due to the current lower levels of rig demand, combined with a significant oversupply of available jackups.

While the shallow water market has been more resilient than the deepwater market, dayrates and utilization for all offshore rigs have been significantly impacted. The competition on operating dayrates has, in certain cases, resulted in rates that approximate direct operating expenses. We are starting to see an increase in potential contract opportunities, but we expect to see continued pressure on dayrates for existing and new contracts in the near term.

The Company believes that its contract backlog of $1.7 billion at December 31, 2016 across 25 contracted rigs (including new build rig under construction) is indicative of our relatively positive position compared to our competitors. The Company remains focused on delivering safe and efficient operations, as well as realizing cost savings and efficiency gains across all levels of the organization.

Financial Report For the Period Ended December 31, 2016

	Three Months Ended December 31, 2015	Three Months Ended December 31, 2016	Twelve Months Ended December 31, 2015	Twelve Months Ended December 31, 2016
Statement of Operations:				
Total Revenue (1)	$ 198.8	$ 156.1	$ 1,030.3	$ 684.3
Operating expenses:				
Labor expenses (2)	59.0	41.0	292.2	188.7
Rig maintenance expenses (2)	39.4	28.4	188.4	95.0
Other operating expenses (2)	(4.0)	7.1	1.6	33.8
Total operating expenses	94.5	76.5	482.3	317.5
Gross Profit	104.3	79.6	548.1	366.8
Loss / (gain) on insurance recovery	2.5	-	(25.4)	-
Selling, general, and administrative expenses	20.6	18.5	98.3	77.1
Provision for / (Reversal of) doubtful accounts, net	48.0	7.4	87.4	(0.4)
EBITDA (3)	$ 33.2	$ 53.7	$ 387.7	$ 290.1
Adjustments:				
Exclusion of non-income tax related costs	(2.9)	0.1	(0.8)	0.7
Rig reactivation costs	-	-	4.1	-
Rig preparation and relocation costs	-	-	6.4	-
Severance costs	-	-	-	4.7
Loss / (gain) on insurance recovery	2.5	-	(25.4)	-
Other	-	0.1	0.1	-
Total adjustments	(0.4)	0.2	(15.5)	5.4
Adjusted EBITDA (3)	$ 32.8	$ 53.9	$ 372.2	$ 295.5
Operating Data:				
Average marketable rigs (4)	35.0	31.3	34.5	31.2
Average stacked rigs (5)	2.0	3.0	2.4	3.6
Average stacked rigs under reactivation (6)	0.0	0.0	0.8	0.0
Average rigs under bareboat charter (7)	0.0	1.0	0.0	0.9
New build rigs under construction	2.0	1.7	2.0	1.9
Total rigs	39.0	37.0	39.7	37.6
Average dayrate (in thousands) (8)	$ 94.0	$ 70.9	$ 104.3	$ 75.2
Marketed utilization (9)	61%	71%	72%	74%
Capital and Deferred Expenditure:				
Regulatory & Maintenance (10)	$ 31.2	$ 12.0	$ 127.7	$ 38.0
Contract preparation (11)	13.4	2.0	65.2	22.3
Marketable Rigs	44.6	14.0	192.9	60.3
Fleet spares and others (12)	2.2	5.0	11.6	7.0
Reactivation projects (13)	-	-	23.4	-
Sub-Total (excluding Newbuilds)	46.8	19.0	227.9	67.3
Newbuilds (14)	12.0	31.7	95.3	190.0
Total	$ 58.8	$ 50.7	$ 323.2	$ 257.3

(In US$ millions, except rig numbers, average dayrate and marketed utilization)

(percentages and figures may include rounding differences)

Explanatory Notes

The above Statement of Operations is presented on a Pro Forma presentation basis rather than on a United States Generally Accepted Accounting Principles ("US GAAP") financial statement presentation basis. The Pro Forma Statement of Operations is presented as defined in the Confidential Information Memorandum of the Bond offering.

(1) ''Total Revenue'' includes all revenues earned over the period including drilling service contract dayrates, mobilization and contract preparation fees amortized over the firm contract term, lump sum demobilization and contract termination fees. Revenue excludes any fair market value amortization of drilling contract intangibles.

(2) ''Labor expenses'' are defined as all personnel remuneration related expenses directly attributable to operating the rig fleet. ''Rig maintenance expenses'' are defined as all non-capitalized or deferred expenses related to maintaining a rig and fall into two categories: ordinary and extraordinary expenditures. Ordinary expenditures include all maintenance expenses less than $50,000. Extraordinary expenditures include all maintenance expenditures that are greater than $50,000 and that do not qualify as capital or deferred expenditures by virtue of not directly extending the life, or increasing the functionality of the rig. Rig maintenance expenses before adjustments also include rig reactivation costs which are required to be accounted for as operating expenditures under US GAAP. ''Other operating expenses'' are defined as all remaining directly attributable operating expenses and include costs relating to insurance, professional services, equipment rental and other miscellaneous costs.

(3) ''EBITDA'' as used herein represents revenue less: operating expenses, selling, general and administrative expenses and provision for doubtful debt, excluding interest, sponsors' management fees, income taxes, depreciation and amortization. ''Adjusted EBITDA'' as used herein represents EBITDA as adjusted for the exclusion of non-recurring items: tax related costs, rig reactivation operating costs which are required to be accounted for as operating expenditures, rig preparation and relocation costs, severance costs, transaction costs, inventory acquisition costs and gain on insurance recovery. These terms, as we define them, may not be comparable to similarly titled measures employed by other companies and are not a measure of performance calculated in accordance with US GAAP. EBITDA and Adjusted EBITDA should not be considered in isolation or as a substitute for operating income, net income or other income or cash flow statement data prepared in accordance with US GAAP.

We believe that EBITDA and Adjusted EBITDA are useful because they are widely used by investors in our industry to measure a company's operating performance without regard to items such as interest expense, income tax expense (benefit), depreciation and amortization and non-recurring expenses (benefits), which can vary substantially from company to company. EBITDA and Adjusted EBITDA have significant limitations, such as not reflecting our cash requirements for Capital and Deferred Expenditure, contractual commitments, working capital, taxes or debt service.

Our management uses EBITDA and Adjusted EBITDA for the reasons stated above. In addition, our management uses Adjusted EBITDA in presentations to our Board of Directors to provide a consistent basis to measure operating performance of management; as a measure for planning and forecasting overall expectations; for evaluation of actual results against such expectations; and in communications with equity holders, lenders, note holders, rating agencies and others concerning our financial performance.

We reconcile EBITDA to Adjusted EBITDA in the table on page 4 as follows:

(a) ‘‘Exclusion of non-income tax related costs’’ represents certain charges incurred by the Company whereby a fee of a percentage of an Egyptian entity’s consolidated revenues is levied bi-annually by the Egyptian General Authority for Investment. For U.S. GAAP reporting purposes the Company recognizes these costs as operating and maintenance expenses.

(b) ‘‘Rig reactivation costs’’ represents the expenditure accounted for as operating expense in accordance with U.S. GAAP incurred by the Company on the re-activation of stacked rigs.

(c) “Rig preparation and relocation costs” correspond to the one-time costs incurred in relation to the rig which was mobilized in replacement of the rig which became non-operational following a fire incident in 2015 and which was declared Total Constructive Loss by the Company’s insurance underwriters.

(d) “Severance costs” represents one time employee termination costs.

(e) “Loss / (gain) on insurance recovery” corresponds to the realized one-time net gain resulting from insurance proceeds for a rig that was declared by the Company’s insurance underwriters in 2015 as Constructive Total Loss following a fire incident.

(4) ‘‘Marketable rigs’’ are defined as the total number of rigs excluding: (i) stacked rigs, (ii) stacked rigs under reactivation, (iii) rigs under bareboat charter and (iv) newbuild rigs under construction.

(5) ‘‘Stacked rigs’’ are defined as rigs that have been taken out of service and placed in long-term storage. It can also include rigs that have been taken out of service as a result of natural disaster or operational event such as a fire incident. Stacking a rig involves a total reduction of the rig crew and “storing” the rig in a harbor or designated area offshore. Steps are typically taken to protect the rig including installing dehumidifiers, applying protective coatings to fight corrosion and filling engines and machinery with protective fluids. Total rig costs are generally reduced to minimum levels during stacking periods.

(6) ‘‘Stacked rigs under reactivation’’ are defined as stacked rigs which are undergoing a reactivation project. These rigs may or may not have a firm customer contract. The costs associated with reactivation are classified as Capital, Deferred Expenditure or charged to operating costs in accordance with the Company’s policies.

(7) ‘‘Rigs under bareboat charter’’ are defined as rigs operating under an arrangement between the owner and charterer of a rig whereby rig operating costs are borne by the charterer as part of the agreement.

(8) ‘‘Average dayrate’’ is defined as the average contract dayrate earned by marketable rigs over the reporting period excluding any mobilization fees, contract preparation and capital expenditure reimbursements.

(9) ‘‘Marketed utilization’’ is defined as the actual number of calendar days during which marketable rigs generate dayrate revenues divided by the maximum number of calendar days during which those same rigs could have generated dayrate revenues. Marketable rigs exclude rigs we consider stacked.

(10) “Regulatory & Maintenance” Capital and Deferred Expenditure includes major overhauls, regulatory costs, general upgrades and sustaining capital expenditures on rigs in operation.

(11) “Contract preparation” Capital and Deferred Expenditure includes specific upgrade, mobilization and preparation costs associated with a customer contract. It excludes contract preparation costs associated with reactivation projects (such amounts are included under “Reactivation projects”).

(12) “Fleet Spares and Others” Capital and Deferred Expenditure includes: (i) acquisition and certification costs for the rig fleet spares pool which is allocated to specific rig expenditure as and when required by that rig which will result in an expenditure charge to that rig and a credit to Fleet spares and (ii) office and infrastructure expenditure.

(13) “Reactivation projects” include all Capital and Deferred Expenditure associated with reactivation projects including Regulatory & Maintenance and Contract Preparation.

(14) “Newbuilds” include all payments made under the construction contracts with Lamprell shipyard for the two newbuild jackup rigs, internal costs associated with project management, machinery and equipment provided to the project by the Company and capitalized interest.