Tidewater Inc [NYSE: TDW]

Long on 3-5 Year Time Horizon | Upside: 45.3%

March 6th, 2025

FI 423 Investment Research

Tidewater Inc: (Off)shoring Up Profits

Tidewater Inc (NYSE: TDW) is a leading global contractor of offshore support vessels (OSVs) and marine services to the offshore energy industry. After a ten-year offshore services bear market, worsening shale economics coupled with a realistic view of the timeline of the energy transition creates an increased demand for oil that can only be met by offshore projects. Despite increased demand, new offshore drilling supply is not economically viable. We believe that OSV operators provide a picks and shovels opportunity to play the offshore trade without having to predict the success of one contract drilling company over another. Finally, trading at a severe discount to its replacement value, TDW is the best OSV player, boasting the youngest fleet, global reach, and a superior balance sheet.

Offshore Services Industry Introduction

Offshore drilling is the process of drilling into the ocean floor to extract pockets of oil and natural gas that lie under the surface. There are several stages in the offshore drilling process, and a single location can take anywhere between 7-10 years on average from project initiation until the first barrel is extracted. The first step is selecting and evaluating potential drilling sites. Geologists and engineers use tools like seismic surveys to identify promising locations for oil and natural gas deposits. Once potential sites are identified, companies complete additional evaluations to minimize the risk that drilling efforts are wasted on an unviable project. After selecting a suitable project site, the second step is to establish a drilling platform. There are multiple types of drilling platforms that vary in effectiveness depending on the depth of the water you are trying to drill in. Fixed platforms provide stability by being sunk to the ocean floor and filled with concrete, effectively extracting oil in shallow waters. Floating platforms, like semi-submersible rigs and drillships, are used to drill in deeper water and are not supported by the ocean floor. Finally, Jackup rigs are a hybrid between the two, raising themselves above the water level by extending legs down to the seabed, essentially standing up on the ocean floor to extract oil from medium-depth project sites. Depending on the project depth, the chosen platform is transported to the drilling location and positioned accurately using anchors. Once in place, the platform serves as a home base for all drilling operations, equipment, crew, and safety systems. The third phase, drilling, involves creating a wellbore to reach the oil reservoirs deep beneath the seafloor. As drilling progresses, casing pipes are added to stabilize the wellbore, and blowout preventers are installed to control pressure and minimize the risk of blowouts. Once drilling confirms the presence of hydrocarbons, we enter the final stage of the offshore process, production. Production tubing is inserted into the wellbore to allow the newly discovered oil to float to the platform, where it is separated, processed, and stored. The finished oil is transported to onshore facilities through pipelines or tanker ships. Putting the evolution of technology aside, this process has remained mostly unchanged from the first offshore project in 1896, growing steadily until 2010, when offshore oil production accounted for approximately 31% of the global oil supply.

The Shale Revolution Caused A 10Y Offshore Bear Market

In the late 2000s and early 2010s, shale began to encroach meaningfully on offshore drilling's share of the global oil supply. We have identified three primary factors that lead to this outperformance. First, on April 20, 2010, a blowout at BP's Deepwater Horizon well in the Gulf of Mexico caused the largest accidental marine oil spill in the history of the oil industry. The NOAA estimates that over 4 million barrels gushed into the ocean over the nearly three

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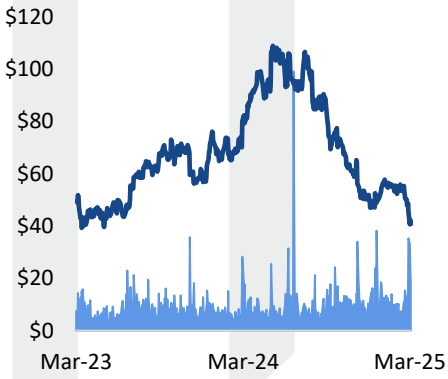
Figure 1: TDW 2 Year Stock Chart



Source: S&P Capital IQ, Market data as of 3/5/2025.

Price	$40.77
Dividend Yield	—
Intrinsic Value	$59.23
Upside	45.28%
3-Year PT	$88.22
Implied IRR	24.60%
52-Week Range	$38.65 — $111.42
Dil Shrs Outstand	51.5M
Mkt Cap	$2.18B
Ent Value	$2.41B
NTM P/E	10.84x
NTM EV/EBIT	7.99x
NTM EV/EBITDA	4.43x
FCF Conversion %	55.12%
% of Float Short	12.03%

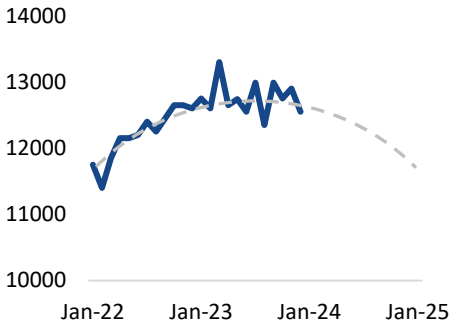
Source: S&P Capital IQ, Market data as of 3/5/2025.

months before the leak was sealed. This disaster not only gave the offshore industry major bad press as the ESG movement was beginning to rapidly grow in popularity but also resulted in the Obama administration halting all deepwater lease sales for six months, forcing oil executives to turn to shale despite inferior returns.

Second, while they now face criticism for underdelivering, looking back to the 2010s, shale executives seem to have severely overpromised the economies of scale that shale production could provide when ramping production up or down in response to oil prices. From 2010-2014, due to a mix of high oil prices and the invention of horizontal drilling, shale led to a doubling of U.S. oil production, culminating in the U.S. surpassing Saudi Arabia to become the world's largest oil producer. However, as the industry grew to scale, breakeven prices never fell below those of offshore projects. Today, most of the "best" shale reserves have been depleted, resulting in each incremental new barrel of shale oil having worse economics. In a recent commentary, Goehring & Rozencwajg said that they believed that U.S. shale production peaked in late 2023 and is now declining (Figure 2). Furthermore, they attribute this decline to geological depletion, not market dynamics. This hypothesis is further supported by the elevated volume of domestic shale M&A transactions, with a specific concentration in the Permian Basin (Figure 3). The onshore drilling industry is rapidly becoming a game of scale, leaving only the largest and most efficient players able to compete for diminishing returns in the long term.

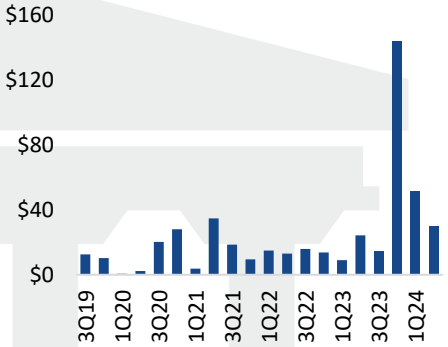
The third and final reason that shale players have taken share in the last century is the incorrect belief that many executives and world leaders had that the energy transition was not only inevitable but would lead to peak oil consumption during the 2020s. This belief implied that long-cycle energy projects, like offshore, were economically unviable. All three of these factors contributed to a century of dramatically reduced offshore spending and bankrupted almost all of the players in the sector.

Figure 2: Adjusted US Crude Production Estimate (kbpd)



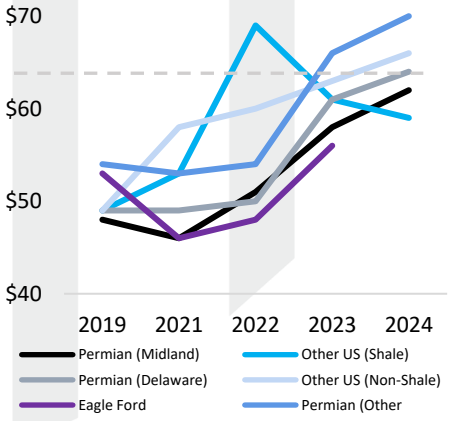
Source: EIA, Goehring & Rozencwajg.

Figure 3: Quarterly Cumulative U.S. Shale Deal Value (Billions)



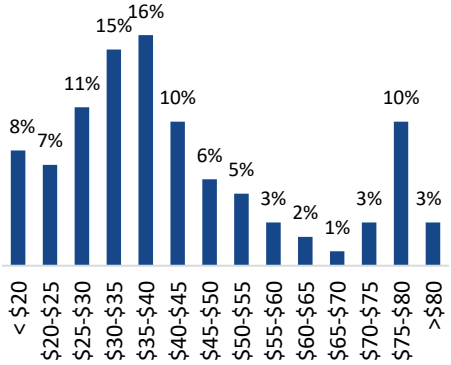
Source: Enverus Intelligence.

Figure 4: WTI Price to Profitably Build a New Well vs. 3/5/25 WTI Price ($66.46)



Source: Federal Reserve Bank of Dallas.

Figure 5: Offshore Project Breakeven Prices (Crude Oil Price/Barre



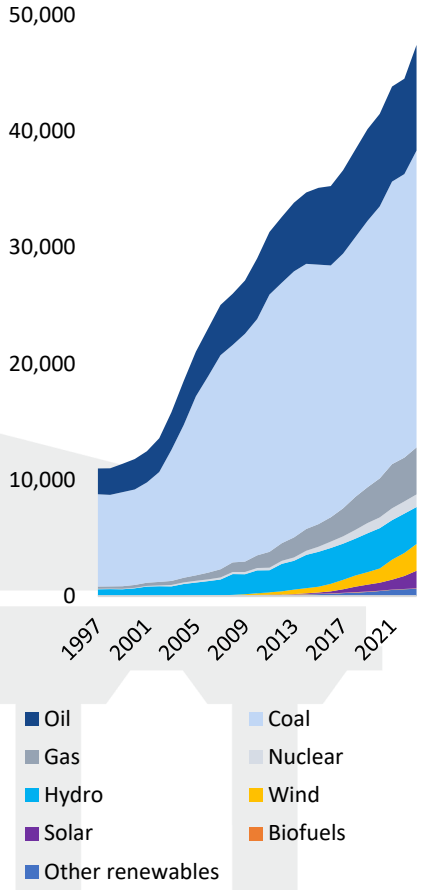
Source: Rystad Energy.

Why Offshore Will Retake Lost Share From Shale

There are two primary reasons that offshore production share gains seem inevitable: positive economics and volume requirements. First, the economics of offshore production have improved meaningfully through the past decade's bear market. Advancements in undersea pipelines and production storage equipment not only speed up production but also make the larger operation much more dynamic, allowing much more of the total equipment necessary to be upended and transported, reducing the sunk costs associated with each project. There have also been significant improvements in the seismic technology used to evaluate well sites, reducing the likelihood of losses from finding "dry wells." Finally, and perhaps most importantly, a new development in blowout preventer technology severely minimizes the likelihood of another Deepwater Horizon occurring. All of these developments contribute to significantly improved economics, from already attractive levels, and have gone largely unappreciated by the market as offshore broadly fell out of favor. Combine this dynamic with the fact that many of the best shale basins in the U.S. are now mature, with declining production and worsening economics, shale projects simply aren't attractive at year-end WTI prices around $70 (Figure 4). While some of the best basins may still make acceptable returns at today's prices, the economics deteriorate rapidly with slight price declines. In contrast, 84% of offshore projects have breakeven prices at or below current WTI prices, with 73% of projects having breakeven prices below $50/barrel, and 57% of projects having breakeven prices below $40/barrel (Figure 5). In a scenario where oil prices plummet, shale would be forced to surrender millions of barrels of daily production to offshore. However, even if oil prices maintain current levels or increase, we believe that there is still upside in offshore projects for our second reason: volume requirements. As even the ESG movement's staunchest supporters begin to become more realistic, many government agencies have begun to revise their estimates of where "peak oil" is. In 1938, geologist King Hubbert coined the concept of peak oil, which is defined as "having extracted half of the recoverable, conventional oil reserves." Many geologists, scientists, and IEA officials believed that the energy transition would result in the world reaching peak oil in the 2010s, with oil dependency gradually tapering off from there as the global economy began to rely more on more environmentally friendly sources of power. Currently, the IEA predicts peak oil demand in 2030, the EIA predicts a peak in 2050, and OPEC predicts a peak in 2045. As the world comes to terms with the fact that the energy transition is much farther out than we initially thought, oil seems to be the only answer for the increase in energy demand driven by new technological developments like data centers. Additionally, even in economic downturns like

what has been happening to China's economy over the last decade, China's oil use has increased by 3% annually (Figure 6). With diminishing economics and reserves, we believe that producers will be forced offshore to meet upcoming energy demands.

Figure 6: Chinese Energy Demand Over the Last Three Decades (TWh)

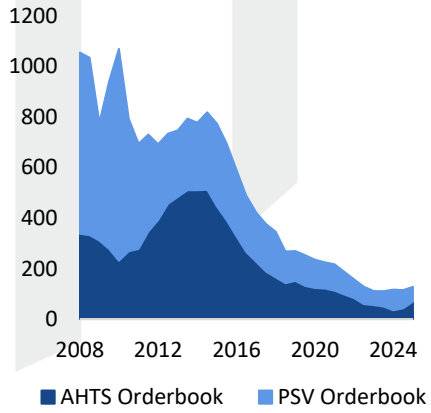


Source: *Our World in Data.*

Why New Supply Is Impossible

Despite the fact that oil demand's right tail is extending far beyond many scientists' predictions, the oil industry still has valid terminal value concerns. Primarily, it is hard to justify the extremely large capex spend to build a new fleet when *eventually*, the energy transition will occur. However, it is not unheard of for company executives to spend irrationally when facing large increases in demand for their product, so instead of focusing on why executives ***won't*** build more rigs, let's instead explore why they ***can't***. In the past, oil rigs have been rendered obsolete every decade or so, due to increases in technology that allow new ships to drill deeper, safer, and faster. After the deepwater horizon accident (5th generation rig), the industry moved to the 6th generation, which makes up two-thirds of global capacity today. As we entered the most recent bear market for offshore drilling, the 7th generation rigs were invented, but only 57 (1/3 of global capacity) of them exist, primarily due to some players in the industry not being in the financial position to upgrade. Unlike the offshore industry, (which nearly ground to a halt from 2014 to 2023) technology continued to progress, and we are now on the 8th generation of vessels. There are three 8th-generation vessels in the world, and unfortunately for manufacturers, it looks like that number will remain at three forever. An 8th generation rig costs 3 years and ~$1 billion to build, which from an IRR perspective, only makes economic sense at $1 million / day rates (reminder: we are currently ~$500k / day and peak inflation-adjusted day rates from the last cycle are $750k-$800k). As a result of this, we believe that new supply, which would usually signal the beginning of the end of peak cycles, is not a risk. Since drilling activity is a key driver of OSV production, the number of new OSVs and OSV orders has also been declining steadily over the last decade (Figure 7). Furthermore, customers are not going to contract out OSVs if they also do not have the capability to contract out drillships, effectively fixing OSV supply as well.

Figure 7: OSV Orderbook Since 2008 (# of ships)

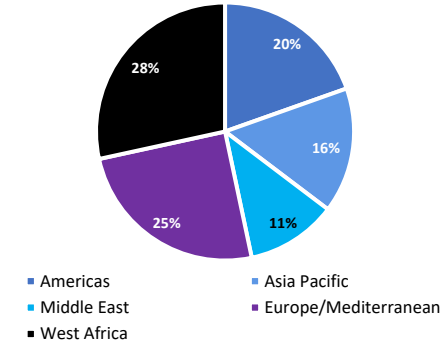


Source: *Company Filings.*

OSV Operators Provide a Picks And Shovels Opportunity To Play The Offshore Trade

While the potential returns of investing in an offshore drilling contractor may tempt the hand of some investors, as value investors we are in constant pursuit of a margin of safety, and we believe that we can de-risk this trade by instead investing in Offshore Support Vessels (OSVs). OSV operators are the "picks and shovels" play for every stage of offshore oil production. They own and operate fleets of specialty ships that support the exploration, construction, operation, and decommissioning of an offshore project. Similar to contract drillers, OSV operators are paid by charter or long-term contract for the use of their ships, making revenue essentially guaranteed for ten years at a time. Cancellation of these contracts requires a 90%+ face value payment. However, unlike their drilling counterparts, OSV operators assume no direct financial risk if projects are unsuccessful and serve multiple companies within the value chain instead of just E&P operators, diversifying revenue and minimizing the negative effects of downturns.

Figure 8: FY24 Revenue by Geography



Source: *Company Filings.*

Fighting Out Of The Blue Corner: TDW Overview

Tidewater Inc., along with its subsidiaries, owns and operates one of the largest OSV fleets in the world. Incorporated in 1956 and headquartered in Houston, Texas, TDW's 191 high-quality OSVs serve a diverse offshore energy customer base in over 30 countries. TDW reports revenue in five geographic segments: Americas, Asia Pacific, Middle East, West Africa, and Europe/Mediterranean (Figure 7). Of their 191 OSV vessels, 139 are Platform Supply Vessels (PSVs). These ships are used to transport essential equipment, supplies, crew, and cargo to and from offshore oil and gas rigs and other offshore installations like wind. In FY24, TDW operated 70 Medium PSVs, classified as having between 500 and 900 square meters of deck space, and 69 Large PSVs, classified as having greater than 900 feet of deck space. Combined, the PSV fleet contributes approximately 75% of vessel revenue. The remaining vessels in the OSV fleet are Anchor Handling Towing Supply (AHTS) Vessels. These ships are used to serve

offshore rigs during mooring and towing operations in a variety of sea conditions. TDW classifies AHTS vessels by brake horsepower (BHP) and has 20 Small AHTS vessels that have up to 8,000 BHP, 21 Medium AHTS vessels that have between 8,000 and 16,000 BHP, and 11 Large AHTS vessels that have over 16,000 BHP. Together, the 52 AHTS vessels contributed approximately 21% of vessel revenue. From a customer perspective, TDW derives a significant portion of its revenue from a relatively small number of customers. In FY24, Eni S.p.A accounted for 12.3% of revenue, and our research revealed that Chevron Corp and the Saudi Arabian Oil Company also account for just under 10% of revenue each. Revenue troughed from FY16 to FY21 and has increased consistently each year since, reaching $1.35B in FY24 (Figure 10).

Why TDW Is The Best OSV

We believe that TDW is the best bet in the OSV industry. Not only do they command the largest fleet (57% larger than Edison Chouest Offshore, the second largest player), but they have one of the younger fleets in their peer set. Additionally, 68% of TDW's fleet is specialized for deepwater projects, representing the largest deepwater fleet in the world. Wood Mackenzie projects a 60% increase in deepwater production by 2030 and notes that 70% of 2025-27 offshore commitments are for deepwater exploration, so we believe this exposure provides a meaningful competitive advantage for TDW going forward. Additionally, when considering other key competitive advantages in the OSV industry, TDW is the only company that checks all our boxes. Finally, acquisitions of Swire Pacific Ltd. and Solstad Offshore at 7% and 20% of replacement value respectively have only extended TDW's scale lead (Figure 9). With the best balance sheet in the industry, TDW is also positioned to continue to grow inorganically, as the market continues to punish any company adjacent to offshore drilling.

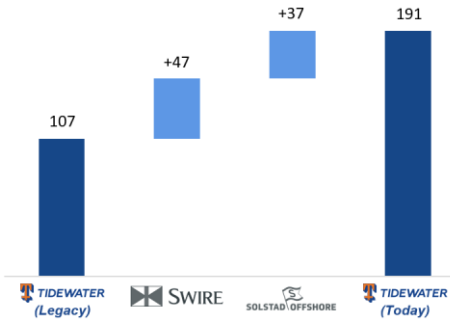
Sell Side Analysts Remain Blinded By Short-Termism

TDW's share price has fallen ~62% in the last eight months, primarily due to falling utilization rates and whitespace fears in the near term. One contributing factor to this whitespace not being discussed by the street is the current issues with FPSOs. Floating, Production, Storage, and Offloading (FPSO) vessels are designed to receive hydrocarbons produced by themselves or nearby platforms, process them, and store oil until they can be offloaded into a tanker or pipeline. As new offshore projects were brought online over the last year, FPSO demand skyrocketed, and supply chains tightened as only a few companies could bring these ships online. This was combined with several notable FPSO issues, including the Jotun FPSO delay, which resulted in IOCs having to delay offshore projects. Limited sell-side covering analysts currently give TDW no grace for the current slowdown, instead valuing the company as if the cycle has fully inflected downward. Additionally, the market is taking these analysts' words at face value, despite TDW not being under coverage by a single bulge-bracket research department. We believe that this creates a buying opportunity for patient investors who have longer time horizons and can look past what could be an unassuming next few quarters.

Valuation

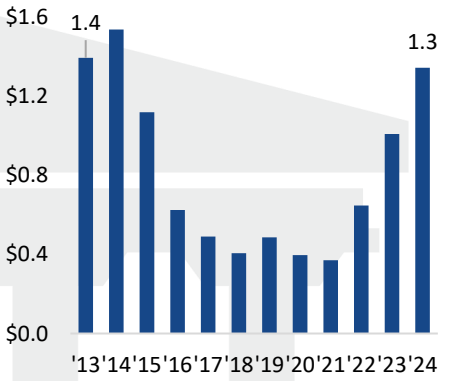
We modeled fleet revenue by multiplying working days (a direct function of fleet size and utilization rates) with day rates. We expect utilization rates to remain close to today's ~80% rate through the rest of 2025 and then accelerate by 800bps in 2026. We see utilization rates eclipsing 92% by 2028, representing a 1200bps expansion. We expect day rates to hold steady through 2025 into a mid-teens acceleration through 2028, with day rates peaking in 2029 at ~$32,500 (Figure 11). We hold our estimates of fleet size flat to avoid mismodeling unpredictable capital allocation moves. We believe this serves as the most directionally accurate picture of TDW's cash flow/earnings potential. With respect to our cost build, we expect TDW's vessel and operating costs to grow slower (MSD) than fleet revenue, creating significant operating leverage. We forecast gross margins reaching ~60% by 2027, with EBITDA margins closely trailing at ~55%. Our model contemplates the cycle inflecting to the downside beginning in 2030, but given our time horizon, our valuation is focused on 2025-2029. We expect free cash flow generation to reaccelerate in 2026 and reach cycle highs by 2028/2029, with free cash flow exceeding $900M annually.

Figure 9: TDW Inorganic Fleet Growth (# of ships)



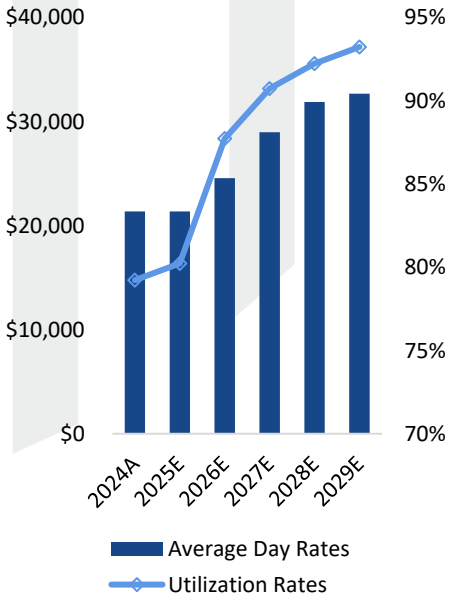
Source: Company Filings.

Figure 10: TDW Annual Revenue (Billions)



Source: Company Filings.

Figure 11: FI 423 Day Rate, Utilization Estimates



Source: Company Filings, FI 423 Estimates.

	2024A	2025E	2026E	2027E	2028E	2029E
Total Revenue	1,345.8	1,365.0	1,714.3	2,090.3	2,336.4	2,420.5
Gross Profit	649.2	633.0	934.2	1,254.8	1,441.0	1,475.2
EBITDA	538.4	533.8	830.4	1,146.2	1,327.4	1,356.3
Operating Income	295.7	278.9	562.7	865.2	1,032.3	1,046.5
Net Income	180.7	166.5	390.8	629.7	761.7	772.9
EPS	$3.40	$3.14	$7.36	$11.86	$14.35	$14.56

Utlization Rates	79%	80%	88%	91%	92%	93%
Average Day Rates	$21,352	$21,352	$24,555	$28,975	$31,872	$32,669
Gross Margin	48.2%	46.4%	54.5%	60.0%	61.7%	60.9%
EBITDA Margin	40.0%	39.1%	48.4%	54.8%	56.8%	56.0%
FCF Conversion	180.1%	186.3%	137.7%	124.0%	120.4%	120.6%
FCF	**325.5**	**310.2**	**538.1**	**780.9**	**917.0**	**932.4**

We base our valuation on an EV/FCF yield against our estimates for FCF through 2025-2029, with 2028 as our focus year. Against today's enterprise value, we expect TDW to generate a >30% FCF yield from 2027-2029. We believe the market will have to close this valuation gap by assigning a lower required yield on FCF. At a conservative 16.7% FCF yield, representing a 6x FCF multiple, TDW would trade at ~$103/share by EOY 2028, representing a return of ~154% from today's valuation. We use a 15% discount rate to discount this price target back to its intrinsic value. This approach yields an intrinsic value of $59.23, representing a 45.28% upside to today's price, an adequate margin of safety. Consequentially, our estimates imply a ~22%-25% IRR if we were to exit the position in 3-4 years. We sanity-checked our assumptions by evaluating TDW's implied EV/Replacement Value. At our peak cycle estimates, TDW would be valued at 0.7x replacement value, which we view as conservative for a stock like TDW at peak cycle.

TDW	Yield	2025E	2026E	2027E	2028E	2029E
	12.5%	2.5%	33.3%	37.2%	31.9%	25.2%
	14.3%	-10.4%	24.7%	31.2%	27.6%	21.9%
IRR If FCF Yield =	*16.7%*	-23.2%	15.5%	24.6%	22.8%	18.2%
	20.0%	-36.0%	5.4%	17.3%	17.3%	14.0%
	25.0%	-48.8%	-5.7%	8.9%	10.9%	9.0%

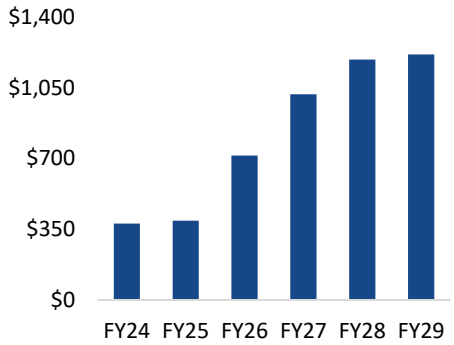
We see additional upside if day rates reach past cycle highs. On estimates of ~$35,000 day rates and 93% utilization rates, we expect free cash flow to reach ~$1,100M. On a 15% FCF yield, TDW would trade at ~$138/share by EOY 2028, representing a ~240% return and a ~32% IRR. We also modeled a static case where we assume that day rates and utilization rates remain at their current levels. In this case, we would expect TDW stock to trade at 5x EBITDA, resulting in a 2028 PT of $34.08, a 16.4% decline in the stock price. We acknowledge this does not reflect cases where long-term oil demand forecasts are significantly lowered or tail risks such as an oil spill occur. In the event of either, we would assess the bankruptcy risk and adjust our view on the valuation and long-term potential from there. However, we expect we will have multiple off-ramps to exit the stock if we notice a change to our thesis, before experiencing significant price declines. Ultimately, given our extended time horizon, we believe the market is presenting an asymmetric opportunity to bet on the offshore oil industry through one of the most well-positioned, high-quality operators in the space.

TDW	2025E	2026E	2027E	2028E	2029E
Price Target	**$35.04**	**$60.79**	**$88.22**	**$103.59**	**$105.34**
Cumulative Return	**-14.1%**	**49.1%**	**116.4%**	**154.1%**	**158.4%**

Current Price Target	**$30.47**	**$45.96**	**$58.00**	**$59.23**	**$52.37**
Upside (%)	**-25.3%**	**12.7%**	**42.3%**	**45.3%**	**28.5%**

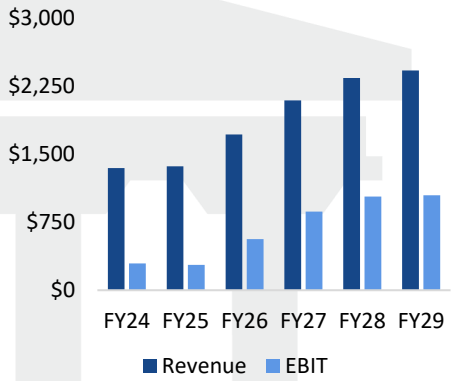
Model Summary:

Figure 12: Vessel Level FCF (Millions)



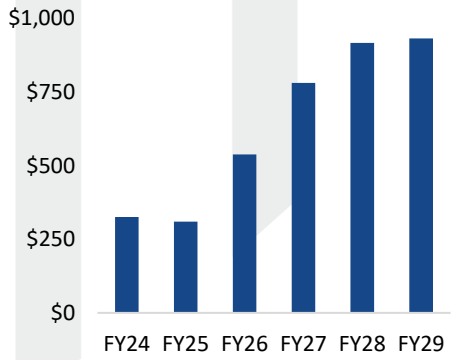
Source: Company Filings, FI 423 Estimates.

Figure 13: Revenue and EBIT (Millions)



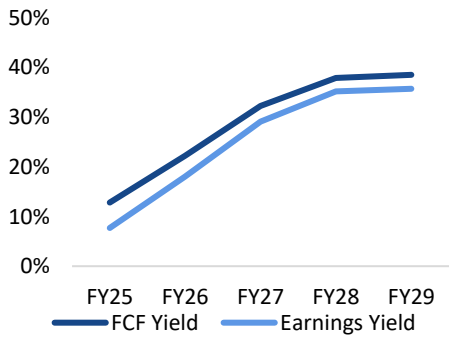
Source: Company Filings, FI 423 Estimates.

Figure 14: Free Cash Flow (Millions)



Source: Company Filings, FI 423 Estimates.

Figure 15: FCF and Earnings Yield



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