The Deal

California Resources Amends Credit Agreement, but Restructuring Could Be on Horizon

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California Resources Corp. (CRC) and its lenders have reached an agreement to amend its debt, which includes reducing the borrowing base, increasing the interest rate and altering covenants.

The largest oil and gas company in California disclosed in a filing with the Securities and Exchange Commission on Wednesday, Feb. 24, that its borrowing base on its first-lien credit facility had been cut to $2.3 billion from $3 billion.

Lenders' commitment on a revolving credit facility was reduced to $1.6 billion, down from $2 billion in November, the SEC filing said. (California Resources also has a $1 billion term loan.)

According to Kim Brady, a senior managing director at advisory firm SOLIC Capital Management LLC, this amendment is a "Band-Aid" to give the company some additional time until the first quarter of 2017. He said the amendment allows the Los Angeles company some breathing room for the next year.

He predicted that unless the company can show improvements this year, it likely will need to get into some serious restructuring discussions in the second half of this year.

Brady said the company now has roughly $560 million available to borrow on its credit facility. JPMorgan Chase Bank NA is administrative agent on the first-lien financing, issued on Sept. 24, 2014, and due Oct. 1, 2019.

Before the amendment, the revolver and term loan were priced at either Libor plus 150 basis points to 275 basis points or an alternative base rate plus 50 basis points to 175 basis points. The amendment increased the interest rate to Libor plus 250 basis points to 350 basis points or ABR plus 150 basis points to 250 basis points.

It appears that the company has recently drawn down on its revolver, as it owed $1.7 billion on the revolver and term loan as of Jan. 31 and had $42 million in outstanding letters of credit. The company had $481 million outstanding on the revolver and $1 billion outstanding on the term loan as of Sept. 30.

Various covenants on its debt also were amended through the end of the year, including a minimum Ebitdax (earnings before interest, taxes, depreciation, depletion, amortization and exploration expenses) requirement, which is now $55 million through the first quarter, $130 million through the second quarter, $190 million through the third quarter and $250 million through the fourth quarter.

The company's minimum interest coverage ratio covenant was set at 2 for the end of the first quarter; 1.5 for the end of the second quarter; 1.25 for the end of the third quarter and 0.7 for the end of the fourth quarter; it will reset to 2 for the first quarter of 2017.

California Resources' first-lien senior secured leverage ratio covenant of 2.25 was suspended until the end of the first quarter of 2017.

Through the amendment, the company cannot pay dividends to its shareholders this year, nor can it make capital investments exceeding $100 million.

Brady said the capital investment limitation will mean the company's production and revenue will go down, putting the company into a "death spiral" but allowing it to kick the can down the road for another year.

The company must use any cash on hand it has, beyond $150 million, to repay the revolver balance. It also can use up to 40% of the proceeds from any asset sales to repurchase its bonds at a discount, with the remaining 60% going to the lenders to reduce their exposure.

In a report on Wednesday, KDP Investment Advisors Inc. said it believes the company will need to revisit both its interest coverage ratio covenant and its first-lien secured leverage ratio covenant before the end of the first quarter of 2017.

"We view this announcement as mixed. In general, credit facility redeterminations are a negotiation between the borrower and the lenders. Under this assumption, we presume that CRC is comfortable with the amended Ebitdax requirement, interest coverage ratio and suspended 1st-lien secured leverage ratio. However, our current projections do not forecast CRC being able to achieve the first-quarter Ebitdax requirement," KDP said in the report.

Brady also questioned whether the company would be able to meet its first-lien leverage covenant in the first quarter of 2017.

He said that if oil prices stayed where they are now, the company would continue to struggle to meet its covenants. He added that if it couldn't monetize its noncore assets, "it will be interesting to see if they can ultimately avoid a bankruptcy filing."

Brady said he believes California Resources is even worse off than Chesapeake Energy Corp. (CHK), which has $10.35 billion in long-term debt. He said Chesapeake has a lot more liquidity and better assets than California Resources. Brady also pointed out that Chesapeake has been successful in selling assets and can pay down debt that is maturing next year.

Moody's Investors Service Inc. had warned in a December report that California Resources would need to seek relief from its financial covenants, including its interest coverage and first-lien leverage covenants, under its credit agreement as early as the first quarter of 2016.

The ratings agency said it expected the company to generate negative free cash flow in excess of $150 million in 2016. The report said California Resources' attempts to monetize assets to reduce its debt would be difficult in the current commodity price environment.

The company, a subsidiary of Occidental Petroleum Corp. (OXY) before it was spun out in November 2014, had $11.91 billion in assets and $9.56 billion in liabilities as of Sept. 30, when the company had $4 million in cash on its balance sheet, according to SEC filings.

In addition to the credit facility, the company has $2.25 billion in 8% second-lien bonds due Dec. 15, 2022; $465.97 million in 5% senior unsecured bonds due Jan. 15, 2020; $828.76 million in 5.5% senior unsecured bonds due Sept. 15, 2021; and $891.2 million in 6% senior unsecured bonds due Nov. 15, 2024.

According to data provided by Bloomberg News, the 8% bonds last traded at 25.25 on Wednesday, down from

28.94 on Tuesday. Meanwhile, the 5% bonds last traded at 10.25 on Wednesday, the 5.5% bonds last traded at 14.75 on Tuesday and the 6% bonds last traded at 10.75.

On Dec. 15, California Resources retired $2.8 billion of its senior unsecured notes in exchange for the $2.25 billion of second-lien notes through an exchange offer.

All of the unsecured notes were issued on Oct. 1, 2014, with the Los Angeles oil and natural gas exploration and production company using $4.95 billion of the proceeds to make a cash distribution to former owner Occidental Petroleum.

Occidental still owns a roughly 18.5% stake in the company but plans to divest it. Last week, Occidental said it would spin off its remaining 71.5 million CRC shares to shareholders as a special stock dividend in March.

California Resources reported a $272 million net loss for the nine months ended Sept. 30.

The company's stock, which trades on the New York Stock Exchange, closed Wednesday at 29.8 cents, down 29.4%.

According to Brady, the stock is likely to be delisted soon, which will significantly diminish its ability to tap the capital markets.

A California Resources spokeswoman declined to comment because the company is in a "quiet period" before it announces its fourth-quarter earnings on Monday.

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