Foresight Energy (FELP)

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FORESIGHT ENERGY

Company Overview

- Mines and sells thermal coal out of Illinois Basin (ILB) – largest pure play and 3rd largest overall producer in ILB
    - Operates four mining complexes: Williamson, Sugar Camp, Hillsboro, Macoupin
    - As of 2018, company had ~2.1bn tons of reserves sufficient for several production decades
- 2018 Revenue / Production Segments
    - Production (tons): Domestic (62%), Export – Europe (26%), Export, India / Middle East (12%)
    - Revenue Share: Domestic (53%), Export (47%)
- Key Customers
    - Domestic customers primarily electric utility and industrial companies in eastern U.S.
    - Top three customers compose 68% of revenue: Southern Company, Santee Cooper, Javelin Global Commodities
- Key Financials
    - 2019E EBITDA: $281mm
    - EBITDA Margin: 26.8%
    - 2019E UFCF: $179mm
        - Cash Interest: $114mm
        - Capital Expenditure: $84mm

Market Analysis / Macro Trends

- Illinois Basin coal faces formidable competition from other coal and alternative energy sources
  - Coal
    - Competes primarily within coal market with other ILB players as well as Northern Appalachia (NAPP) and Powder River Basin (PRB)
    - Domestic utilities overwhelmingly shifting to gas-powered plants in the last five years and poor economic conditions and lower energy needs past 2020 will likely accelerate decommissioning of coal plants and discourage installation of scrubbing equipment
    - Export competition defined by Indonesian and Russian coal producers as well as alternative energy sources
  - Alternative Energy
    - Seaborne coal markets feeling pressure from renewables as battery storage and renewables capacity triples. LNG production out of the US, Australia, and Russia will continue to prove problematic
- High cost of entry associated with mining equipment as well as high exit costs (minimum royalties and mine clean-up) leads to mines running unprofitably (zombie mines)
  - Substantial political pressure from current administration to maintain mining industry employment
  - Zombie mines continue to oversaturate coal supply
  - Poor performance of barge and other transport companies down the value chain instead of coal production numbers serve as better indicator of coal industry performance
- Buyers have significant power to choose among different coal sources depending on price, coal quality, and reliability
  - In addition, coal competes for overall electricity generation market share with low-cost natural gas and renewables
  - Contracts fail to lock in sufficient volume >3 years to provide for stable cash flows
- Mature declining industry implies fixed total addressable market with secular decline of coal market share
  - Profit in commodity market primarily by management of cost structure

Competitive Positioning

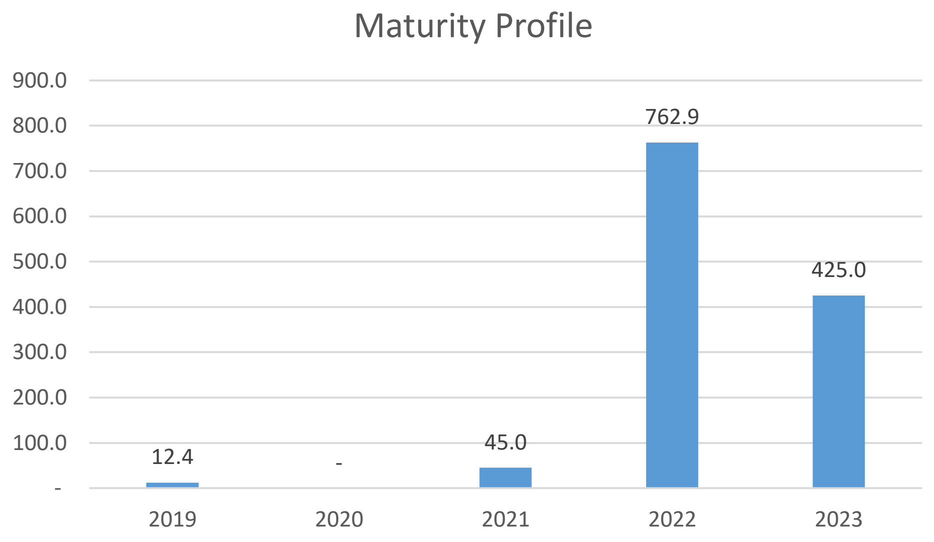
- Foresight is positioned as a high quality, low cost provider of high energy coal
- Product Differentiation
  - Coal
    - ILB produces high energy (BTU), high sulfur coal that was previously expensive and dirty to process
    - Build out of scrubbed generation capacity has decreased sensitivity to sulfur levels and increases demand for high energy ILB Coal
- Cost Structure
  - Cash Cost
    - ILB enjoys lower cash costs of mining due to favorable geology (thicker, uniform, contiguous coal seams)
    - ~$2bn of capital invested in longwall operations since establishment drive cash costs far below ILB average: FELP operates 3/4 most productive mines in the country
    - Non-unionized contract miners prevent headwinds from poor operating leverage
  - Transportation: delivered cost of coal in U.S. includes cost of transport to point of sale
    - Diversity of transportation options provide for higher netbacks (revenue per ton – transportation costs per ton).
    - Access to barge, rail, and truck services increase leverage to drive down supply of transportation. Previous investments in export terminal and barge-loading capacity avoid additional investment while allowing for export market optionality

Capitalization and Maturity Profile

($ in mm) Liquidity	As of 3/31/2019	Leverage	Maturity	Coupon	8/2/2019 Price	Yield
Cash and Cash Equivalents	3.5					
Revolver Availability	112.7					
Total Liquidity	116.2					
$170mm 1st Lien Revolver	45.0		3/28/2021	L+525		
1st Lien Term Loan	762.9		3/28/2022	L+575	72.00	30.7
5.780% Longwall Financing Arrangement	9.3		6/19/2019	5.78%		
5.555% Longwall Financing Arrangement	3.1		9/19/2019	5.56%		
Finance Lease Obligations	10.9					
Total 1L Debt	**831.2**					
2nd Lien Notes	425.0		4/1/2023	11.50%	38.87	48.2
Total Secured Debt	**1256.2**					
Market Capitalization	65.0					
Total Capitalization	1321.2					

LTM Operating Metrics	**LTM**	**YE2018**
Adj. EBITDA	314.107	313.584
Capital Expenditures	102.712	84.147
Est. Cash Interest	115.8	115.8

LTM Credit Metrics	**LTM**	**YE2018**
1L Debt / Adj. EBITDA	2.6x	2.7x
Secured Debt / Adj. EBITDA	4.0x	4.0x
Adj. EBITDA / Cash Interest	2.7x	2.7x
(Adj. EBITDA - Capex) / Cash Interest	1.8x	2.0x



Capital Structure Analysis

- Potential Triggers
  - First major maturity in 2022 - ~$760mm 1st Lien Term Loan, potentially difficult refinancing for 2021 revolving credit facility Financial projections assumes successful refinancing
    - Peers levered 1.0x – 2.0x imply that FELP 3.9x leverage in 2021 will damage access to capital markets
  - Business maintains adequate liquidity into 2022 before maturity
  - 30% EBITDA cushion before breach of covenant (3.5x 1L leverage, stepping down to 3.25x in 2021)
- History
  - 2L bonds previously were trading at ~70 mid 2019 and management expressed interest in buying back a portion
- Covenant Review
  - Subject to RP baskets and ECF sweep determined by leverage, FELP can buy back $65mm in market value of 2L Notes
  - Foresight could transfer assets to an existing unrestricted sub to raise up to ~$220mm of additional secured debt
    - Presents risk to 1L holders and opportunity for new money to capture portion of 1L value pool
- Takeaway
  - FELP will likely pursue a distressed buyback of 2L notes at discount (otherwise large premium) or a debt restructuring
  - Reorganization expectations / dynamics
    - 1st Lien trading at ~70 expecting impairment in reorganization or loss of collateral value / potential for pari-passu claim
    - 2nd Lien trading at ~40 on recovery value and potential for equity stake
    - Assuming reorganization instead of liquidation, 1L will likely seek partial reinstatement and majority ownership of company

Model Assumptions / Key Business Drivers

- Sales Growth
  - Revenue is driven by assumptions on production volume by segment and market share of ILB production
    - Assumes FELP captures increasing market share due to favorable cost structure and large cost reserves despite overall ILB basin production decreasing due to inclement weather, poor operating leverage, and oversaturation of coal
  - Assumes realized price per ton sold equals spot price
    - Pricing improves slightly into 2022 as demand for high BTU, high sulfur coal rises
  - Domestic / international share expected to shift towards 60:40 split
    - FELP able to take advantage of export loading capabilities to continue increasing exposure to export market at the expense of competitors
- Gross Margin
  - Cash cost (~50% of revenue) projected on a per mine per ton cash cost
    - Gross margin improvement driven primarily by shifting capacity back into low-cost Hillsboro operation and expectation that all longwall moves are in place. Slight drag versus 2018 due to assumed decreased tons sold versus tons produced due to current status of >30% of future volumes remaining uncontracted
- EBITDA Margin
  - EBITDA margin driven down 160bps from 2018 performance but recovering in the short term to 2018 levels
    - Transportation (~20% of revenue) primary driver of decreased margins due to increased share of export production
    - Flow down of gross margin serves as mitigating factor
- Capital Expenditure reflects return to pre-Hillsboro levels and expectation that only maintenance will be necessary on a go-forward basis

Financial Projections – Base Case

$ in mm	Historical			Projections		
	2016A	2017A	2018A	2019E	2020E	2021E
Financials						
Total Revenue	$876	$955	$1,105	$1,050	$1,044	$1,015
Growth		*9%*	*16%*	*-5%*	*-1%*	*-3%*
Gross Income	443	451	556	525	524	514
Gross Margin	*50.5%*	*47.2%*	*50.3%*	*50.0%*	*50.2%*	*50.6%*
Adj. EBITDA	308.80	294.50	313.58	281.64	290.47	279.60
EBITDA Margin	*35.3%*	*30.9%*	*28.4%*	*26.8%*	*27.8%*	*27.6%*
EBIT	23	22	85	73	107	102
EBIT Margin	*2.6%*	*2.3%*	*7.6%*	*7.0%*	*10.3%*	*10.0%*
Net Income	(179)	(215)	(62)	(41)	(2)	(2)
NI Margin	*NA*	*NA*	*NA*	*NA*	*NA*	*NA*
Credit Stats						
1L Debt / EBITDA	2.5x	3.1x	2.6x	2.7x	2.4x	2.3x
Total Debt / EBITDA	3.3x	4.1x	4.0x	4.2x	3.9x	3.9x
EBITDA / Interest Expense	2.7x	2.5x	2.7x	2.4x	2.5x	2.4x
Other Data						
Tons Sold	19,270	21,368	23,395	22,079	21,623	20,728
Coal sales realization per ton sold	$44.97	$43.84	$46.91	$46.76	$46.92	$47.57
Netback to mine realization per ton sold	$37.73	$36.36	$37.07	$37.34	$37.22	$37.87
Cash costs per ton sold	$22.32	$22.84	$22.85	$22.70	$22.64	$22.70
Liquidity						
Revolver Capacity				$170	$170	$170
Borrowings				8	0	0
L/Cs				12	12	12
Revolver Availability				149	158	158
Cash				10	81	152
Total Liquidity				159	239	309

Valuation

- DCF
  - Base case assumes ILB advantage and domestic coal dynamics drives both domestic and export pricing upwards. ILB production overall slows as higher cost producers are pushed out and FELP market share steadily rises. Tons sold as a percent of tons produced decreases initially as contracting proves difficult due to leverage but stabilizes thereafter
- Comparables
  - Selected sample of global coal peers trade between 2.5x and 4.2x EBITDA
    - I view other ILB producers and thermal coal companies in the Powder River and Appalachian basins as the closest competitors.
    - Alliance, a similar pure-play thermal producer with comparable gross margins but levered 1x trades at 4.23x
  - I believe FELP should trade at middle of peer group given reserve size and ILB location while also acknowledging abnormal leverage and lack of exposure to metallurgical coal
- Liquidation
  - Liquidation valuation assumes simple collateral waterfall with little to no recovery on non-current assets and 25% on PP&E

(% in mm)

	Low	Mid	High
DCF			
3 Year	$957,043	$1,175,629	$1,394,215
5 Year	1,055,185	1,260,581	1,465,976
Comparables			
2021E	838,805	978,606	1,118,407
2019E	844,920	985,740	1,126,560
Liquidation		642,256	

			Recovery %	
		DCF	**Comparables**	**Liquidation**
Total Value		$1,175,629	978,606	642,256
Claims				
Current Liab.	284,981	100%	100%	100%
1L Revolver	45,000	100%	100%	100%
1st Lien TL	762,900	100%	83%	40%
Longwall	9,300	100%	83%	40%
Longwall	3,100	100%	83%	40%
Finance Leases	10,900	100%	83%	40%
2L Notes	425,000	14%	No Recovery	No Recovery