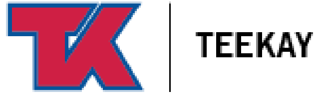

TEEKAY SHIPPING LTD.

Moderator: Bjorn Moller
July 23, 2003
10:00 a.m. CT

Operator: Ladies and gentlemen, thank you for standing by. Welcome to the Teekay Shipping Corporation's second quarter 2003 earning results conference call.

During the presentation all participants will be in a listen-only mode. Afterwards, you will be invited to participate in a question-and-answer session. At that time, if you have a question you will need to press star one. As a reminder, this conference is being recorded.

Now for opening remarks and introductions, I would like to turn the conference over to Mr. Bjorn Moller, President and Chief Executive Officer of Teekay Shipping Corporation. Please go ahead, sir.

Jerome Holland: Before Mr. Moller begins, please allow me to remind you that various remarks we may make about future expectations, plans and prospects for the company and the shipping industry constitute forward-looking statements for purposes of the Safe Harbor provision under the Private Securities Litigation Reform Act of 1995. Actual results may differ materially from those indicated by these forward-looking statements as a result of various important factors, including those discussed in our annual report on Form 20-F dated March 31, 2003, which is on file with the SEC.

I'll now turn it over to Mr. Moller to begin.

Bjorn Moller: Thanks, Jerome, and good morning, ladies and gentlemen. Thank you for joining us on today's call.

We're pleased to report on another very good quarter for Teekay Shipping. For the quarter ended June 30, 2003 we reported net income of $96.9 million or $2.39 per share, our third highest quarter ever. Our results were boosted by the Navion acquisition, which was completed early in the quarter, and whose figures are included for the first time. Navion contributed to our net income with $28.8 million or 71 cents per share.

This morning I will provide an overview of key dynamics in our two business segments, that is, our spot tanker business and our long-term fixed rate business. Peter Evensen, our new chief financial officer, will take you through our financial results. And Vince Lok, Vice President of Finance, will join us for the question-and-answer session.

I'll begin this morning's discussion with an overview of Teekay's conventional spot tanker segment. With the addition of Navion, our spot tanker fleet grew during the quarter from 75 to 100 ships, including vessels on order. Our 70-ship Aframax tanker fleet remains the cornerstone of our spot market franchise, but Navion has expanded Teekay's involvement in larger crude oil carriers and in the product carrier market. Our spot business benefited from strong tanker charter rates in the quarter, producing $126 million in EBITDA compared to $36.4 million in the previous quarter.

I'll briefly review the demand and supply dynamics that influenced our spot business in the quarter and the resulting trade market. Turning first to tanker demand, oil demand growth and underlying driver of tanker demand slowed in the second quarter after a strong first quarter. According to the IEA global oil demand declined from the March quarter in line with typical seasonal demand patterns, but was up .8 percent from figures one year ago. Global oil supply,

the most direct driver of tanker ton-mile demand, gradually declined during the quarter, resulting in an average supply of 78.1 million barrels per day, down .9 percent from the previous quarter. Most of the decline was the result of OPEC and in particular Saudi Arabia reigning in production to comply with lower quotas.

Having come through the June quarter, which is typically the weakest part of the year in terms of oil demand, we look ahead to the next three quarters for which the IEA forecasts average oil demand of 2.5 million barrels per day or 3.2 percent above June quarter figures. With global inventories still well below normal levels, this pick up in oil demand will require equivalent production increases. The leverage factor normally used to translate oil demand to tanker demand points to an increase in tanker demand of around five percent from levels in the June quarter. And with Middle East OPEC countries likely to supply the majority of this incremental oil from their significant spare capacity, tanker demand would grow even more. We believe that the stage is set for strong tanker demand beginning late in the third quarter and extending through to the first quarter of 2004.

Turning to tanker supply, the June quarter provided a surprisingly positive result, namely a decline in the world tanker fleet. According to Clarkton, the world fleet declined by .4 percent in the quarter. Deliveries of new tankers slowed to 6.7 million tons, while scrapping and other deletions increased to 7.9 million tons. At an annualized pace of 10 percent of the world tanker fleet, the amount of tonnage scrapped in the quarter was remarkable in and of itself. Even more remarkable is that this level of scrapping occurred during a strong trade market. Although assisted by the current very high prices for scrap steel, this does underline the impact on ship owners of the pending regulatory phase out of old ships and the effect of charge for discrimination on the cash flow of such ships.

New tanker ordering slowed in the quarter to 10.7 million tons from 14.8 million in the prior quarter. The total order book at the end of June stood at 69 million tons or 22 percent of the

existing fleet, up from 21 percent three months ago. In the Aframax sector, the fleet grew by three ships to 663, with 14 ships delivering and 11 being deleted. New orders were placed for 20 Aframaxes in the quarter, bringing the order book to 132 units or 20 percent of the existing fleet, up from 19 percent three months earlier.

The tanker supply outlook is shaping up to be very interesting as a result of the regulatory developments over the past month. As widely anticipated, in June the EU parliament passed laws that accelerated phase out of single hull tankers from European waters and creates strict inspection regimes for older ships. These laws are expected to take effect later this year.

Last week the IMO, the Global Maritime governing body, agreed to accelerate the phase out of so-called category one tankers, in essence tankers built prior to 1982, thereby following the EU's lead. In addition, the IMO considered an accelerated phase out of the world's remaining single hulled tankers, known as categories two and three, but in the end deferred this decision - its decision on this issue until its meeting next December in order to more carefully consider alternative time schedules for this phase out.

As a result of the July IMO decision, approximately 37 million tons or 12 percent of the world fleet will become obsolete and require replacement by mid-2005. Assuming annual growth in tanker demand of 2.5 percent, the market will require an additional 16 million tons of tanker capacity by mid-2005. And this adds up to a total requirement for 53 million tons of tonnage replacement by mid-2005 in order to maintain status quo in the fleet. With scheduled deliveries between now and mid-2005 locked in at 55 million tons, the prospect of sizable fleet growth in the near term, which some observers were predicting future size for the tanker order book, now seems less likely. In our view, the new IMO regulations have set the stage for a continuation of the tightly balanced tanker supply picture for at least two more years.

Looking beyond the IMO phase out in mid-2005, a further 30 million tons of category two tankers will be in the scrapping zones with an average age of over 22 years by the end of 2006. This is particularly relevant because of the tighter inspection regimes soon to come into effect for older tankers. Already, before the condition assessment scheme has come into effect, almost one-third of tankers sold for scrap this year were under 25 years old. This additional large block of old ships has the potential to offset new tanker deliveries through 2006.

The lead-time for new building berth availability has grown during the past six months and is now three years or more, with berth space becoming tight before mid-2006. Shipyard capacity is being rapidly absorbed by very strong demand for container ships, L&G carriers and other types of ships being ordered to meet growing international sea bound trade. This is placing a limit on the space being allocated to the construction of tankers.

Turning to the freight market, the tanker freight rates were relatively strong in June - in the June quarter, albeit below the first quarter's very high levels. Rates did however gradually slide downwards throughout the quarter, mainly due to the ripple effect of production cuts in the Middle East. Aframax rates in the India Pacific were representative of this, beginning the quarter at $38,000 a day but dropping to $19,000 per day by the end of June.

During the first three weeks of July we've seen a further weakening in rates across all sectors of the crude oil market. Rates are not expected to recover until oil production levels grow, which, as stated earlier, we expect to occur later in the quarter.

In past quarters earnings conference calls, we have discussed our Aframax day rates against Clarkson AG East and Carrier U.S. Gulf numbers. With our more diverse fleet composition and its broader geographic distribution, after the addition of the Navion fleet, this comparison has become less relevant as a rule of thumb, particularly during periods of high volatility and charter rates. As we become more familiar with the impact on our earnings of the Navion spot business,

we shall develop a revised guideline that could be used by you to estimate Teekay's earnings based on changes in the open tanker market.

Just touching briefly on changes in our spot tanker fleet in the quarter, there are a number of changes, which were all part of our ongoing fleet renewal. We exercised options before Aframax newbuildings, with delivery in 2005, bringing this series of ships to eight. We took delivery of two in-chartered newbuildings, an Aframax and a VLCC. We entered into two additional Aframax in chart transactions of two to three year duration due to commence later this year. And we exercised options to extend existing in-charters on two Suez Max tankers and one large product tanker. These additions to our fleet will support our increased tonnage requirement arising from the Navion acquisition.

During the quarter we sold three older vessels built between 1983 and 1987. Earlier in the third quarter we sold a further three Aframaxes built in 1985, '86, and two of these ships have already delivered to the buyers, and the third vessel will change hands in September.

Next, I'll provide a brief update on our long-term fixed rate contract segment. During the quarter this segment produced $56.2 million of EBITDA compared to $22.9 million one year ago. Our shuttled subsidiary, UNS, successfully completed the conversion of two Suez Max shuttle tankers, which have since delivered on 15-year contracts to Brazil. Between August 2003 and January 2004 we expect six new ships with long-term employment to join the fleet, a Suez Max shuttle tanker delivering into the UNS fleet in August and three Suez Max and two Aframax tankers conventional tankers delivering on 12 year charters to Conoco Philips between September and January. EBITDA from these ships is expected to be $35 million per year and brings the number of ships in this segment to 51. We're currently forecasting $260 million of EBITDA from our long-term contract segment in 2004. We continue to pursue interesting new projects and expect to add to this contract portfolio going forward.

I'll now hand it over to Peter to discuss our financial results - Peter.

Peter Evensen: Thanks, Bjorn. Our second quarter was a very good quarter, both measured with and without the acquisition of Navion. As previously mentioned, Teekay completed its acquisition of Navion in April, and our results include a full quarter of Navion from April 1st.

Net income for the quarter was $96.9 million or $2.39 per share, which includes the $3.8 million write down in the carrying value of three of our older vessels that were sold in July. Excluding this write down, net income was $100.7 million or $2.48 per share. Teekay generated $182.2 million of EBITDA during the quarter, of which $56.2 million was from long-term fixed rate contracts.

Navion's strong performance for the quarter resulted in approximately $28.8 million or 71 cents per share earnings accretion to the company's consolidated results. Of this, $13.0 million or 32 cents per share was attributable to Navion's shuttle tanker business and $15.8 million or 39 cents per share was attributable to Navion's conventional tanker business.

You will note that we have revised the format of our earnings release to incorporate Navion and, as a consequence, we have redefined our segments based upon their cash flow characteristics. The spot tanker fleet revenues are more variable, reflecting the inherent volatility of the spot tanker market, while the long-term fixed rate contract fleet revenues are stable and much more predictable given the attributes of these contracts.

In looking at the segment results for the quarter and comparing them to the second quarter of 2002, I will refer to the operating results section beginning on the second page of our press release. Our long-term fixed rate contract fleet segment includes the company's shuttle tanker operations, both Navion and Nordic Shipping, FSO vessels and LPG carrier and certain conventional crude oil and product tankers on long-term fixed rate contracts. This segment

generated, as Bjorn said, $56.2 million in EBITDA during the second quarter compared to $22.9 million in the second quarter of 2002, primarily due to the inclusion of Navion's shuttle tanker fleet.

Navion shuttle tanker business, which earned 32 cents in the second quarter, was more profitable on a net income basis than our previous guidance of 25 cents per quarter because of higher utilization of the shuttle tanker fleet caused by favorable seasonal factors. As Bjorn mentioned, our long-term contract fleet will increase by early 2004 with the delivery of five conventional crude oil tankers to Conoco Philips and one UNS Suez Max shuttle tanker.

Turning to the spot tanker fleet segment, the acquisition of Navion added 2,366 calendar days to our spot tanker fleet. With the exception of two owned vessels, the Navion conventional tanker fleet consists of charted in vessels at different rates for different periods and may vary depending upon the requirements of our customers. The additional calendar days were partially offset by a reduction in days from the sale of two Aframax vessels during the beginning of the second quarter. Our Aframax fleet generated a 365-day time charter equivalent, or TCE, of 27,327 per day in the second quarter compared to 28,761 per day from the first quarter. This drop in our average TCE rate reflects the decline in market rates from the high levels seen in the previous quarter, for the reasons Bjorn cited earlier.

The calendar ship days for the OBO fleet decreased in the second quarter due to the sale of one vessel in this fleet in April. The OBO fleet continued to earn strong tanker rates, generating a 365-day TCE of 17,209 per day in the second quarter compared to 17,775 in the first quarter.

Turning next to our income statement on the sixth page of the press release and running down June 30th quarter figures and comparing them to the March 31st quarter, net voids revenues increased by $140 million over the prior quarter to $353 million. Navion added approximately $157 million in net voids revenues, which were partially offset by lower spot tanker rates this

quarter. Our op ex was up by about $13 million from the first quarter, due primarily to the addition of Navion's own fleet. Otherwise, op ex was substantially unchanged from the prior quarter. Our time charter expense grew significantly by almost $80 million to $93.5 million due to the acquisition of Navion.

Depreciation and amortization increased by $10.6 million from the first quarter to $49.8 million, again mainly due to Navion. Included in depreciation expense is $6.7 million in dry docked amortization in the second quarter compared to $6.4 million in the first quarter. G&A expenses increased to $21.9 million in the second quarter compared to $14.7 million in the first quarter, due primarily to the acquisition of Navion. Also included in the second quarter is a one-time cost of $1.4 million relating to the merger of our offices in Australia.

Net interest expense increased to $20.4 million from $13.5 million in the first quarter due to the debt financing taken on with the acquisition of Navion. And EBITDA to interest coverage decreased slightly from 9.5 times cover in the first quarter to 8.1 times in the second quarter. The results for the second quarter included a $3.8 million write down in the carrying value of three of our older vessels sold in July. When we took the larger write down in the first quarter, it was not anticipated that one of these vessels would be sold. And that vessel accounted for the bulk of the extra write down this quarter.

Deferred income taxes has increased to $13.9 million from $3.3 million in the previous quarter due to the tax on Navion's results of operations for the second quarter. Other income of $2.5 million relates mainly to income from joint ventures, dividend income and foreign exchange gains partially offset by minority interest expense and a number of miscellaneous items.

Looking at the balance sheet, treating the mandatory exchangeable preferred issue as equity, net debt to capitalization increased to only 41 percent at the end of the second quarter, up from 35 percent at the end of the first quarter. The acquisition of Navion was initially 100 percent debt

financed, with a 364 day, $500 million debt facility, together with existing cash and credit lines. The one-year debt facility was subsequently replaced this quarter with a five year, $550 million revolving credit facility. Through significant internal cash flow generation and the issuance of the $144 million mandatory exchangeable preferred issue, we have already made substantial progress in both de-levering the balance sheet and increasing our liquidity by freeing up capacity on our corporate revolving credit. Our liquidity, consisting of cash, cash equivalents and undrawn availability under revolving credits, totals over $700 million.

Capital expenditures for the second quarter, excluding the acquisition of Navion, totaled $62 million, including $39 million in newbuilding installments, $9 million in dry-docking costs, and the remainder relating to vessel conversions and upgrades. Forecasted cap ex excluding maintenance cap ex for the next two-and-one-half years is roughly $125 million for the remainder of 2003, $190 million in 2004 and $120 million in 2005.

As Bjorn mentioned, in terms of earnings guidance going forward, we have in the past asked you base earnings based on 60 percent spot Aframax rates in the Pacific and 40 percent spot rates in the Atlantic. The addition of Navion's conventional spot tanker business has made precise guidance, using Aframax rates more difficult. While we develop a more effective formula, we would guide you to use 13,500 a day as the company's net income break even Aframax TCE rate for 2003, with every $1,000 a day increasing Aframax rates based on Pacific and Atlantic rates contributing and incremental 65 cents to 70 cents in EPS.

I will now turn the mike back to Bjorn to conclude.

Bjorn Moller: Thanks, Peter.

To conclude, over the past several years we have focused on a dual strategy - building our spot tanker franchise and customer service organization, and leveraging our position in that business

into a large portfolio of premium, stable contract business in some of the most complex trades in the industry. The financial strength that this strategy has brought about is evident from the acquisition of Navion, through which we have grown our company by 30 percent.

Navion was an all debt financed transaction, yet, as Peter said, has had a limited effect on our financial leverage, has had no adverse effect on our credit ratings, and has left our significant liquidity largely intact. We are pleased to be able to demonstrate to you this quarter the positive financial effect of this strategy, and we're excited about the capacity that it has created for future profitability and growth of the Teekay franchise.

Just before I open it up to questions, let me just go back and restate my tanker demand information. I think I got it a little bit confusing for you. Just what I wanted to restate is that the IEA is forecasting that average oil demand for the next three quarters will be 2.4 million barrels a day or 3.2 percent above June quarter figures. Just want to clarify that.

So we're going to be opening up to your questions now. Thank you very much.

Operator: Thank you, Mr. Moller. Today's question-and-answer session will be conducted electronically. If you would like to ask a question, you may do so by pressing the star key followed by the digit one on your touch-tone telephone. We ask that anyone who is using a hands-free phone or speakerphone to please pick up the handset when asking your question. Additionally, please make sure your mute function is turned off to allow your signal to reach our equipment. We'll take as many questions as time permits today. Once again, press star one for a question.

And once again, if you do have a question at this time you may press star one. We'll take our first question today from Magnus Fyhr with Jeffries & Company.

Magnus Fyhr: Thank you. Good morning. Congratulations to a great quarter. A couple of questions, starting - just following-up on the Navion acquisition. Halfway through the third quarter would you give us - can you give us some guidance on the comfort level you had with achieving similar results to what you did in the second quarter, or are you still sticking with the 25 cent guidance that you have given earlier?

Bjorn Moller: You're referring to the shuttle business?

Magnus Fyhr: Yes, the shuttle tanker business.

Bjorn Moller: Well, I think it's - what happens in the shuttle business is that, as you probably know, during the summer periods there is field maintenance. And that causes some shut in on capacity and typically leads to lower utilization of the Navion shuttle fleet during summer months. I guess June, which is in the second quarter, would have captured some of that. But I would suspect that the utilization is typically budgeted to be lower in the third quarter than the second quarter. So I think if you use the 25 cents that - it's a bit early yet, but we assume that will be a good average number. It might fluctuate, as we saw here. So I would say it but with a slight grain of salt until we get a little more into the Navion management.

Magnus Fyhr: So, it's a little too early to see if you've seen the seasonal impact so far reflecting the June results - or the July results?

Bjorn Moller: Well, we're seeing pockets of waiting time, which is normal for this time of year. So I would say we're seeing a normal seasonal slowdown. What I can't give you yet because I guess the whole scheduled maintenance tends to be a little different each year is exactly what impact it will be. So I think we are seeing - I think it'd be reasonable to expect it to be a little bit lower in earnings for that segment in the third quarter.

Magnus Fyhr: OK. And just another question on the recently announced 16 percent stake in TORM. Could you elaborate a little bit on what attracts you to the product tanker market? You have some in your own fleet now. And maybe it'd be interesting to see what your outlook is for that market segment.

Bjorn Moller: First of all, it's a very natural extension of our customer's requirements. Our customers and those of TORM, for example, are quite similar. There's a lot of overlap. And secondly, the product business is an attractive growth business. TORM shares our philosophy, I guess, of consolidation, in their case through the pool concept. But the idea of having a large footprint in a particular market is something we believe in greatly, as you know. And so, we think TORM is an interesting investment opportunity for us at this point.

Magnus Fyhr: OK. Great. And just a final question on the - we've seen some write downs for the older vessels. What's the status on the OBO fleet currently? Do you expect to take some write downs there as well?

Bjorn Moller: We - the OBO fleet is a segment of our tonnage that's under consideration. We would not expect any meaningful write down based on current projections should we sell that fleet.

Magnus Fyhr: All right. Thank you. That's all I had.

Bjorn Moller: Great. Thanks, Magnum.

Operator: Jim Bussone with Delphi Management has our next question.

Jim Bussone: Hi, guys. Great quarter. With the acquisition of Navion now, will there will be further expenses that you can trim out of that, having taken that on?

Vince Lok: When we made the acquisition we said that we were looking to get 20 to 30 cents by early 2004. And with the acquisition going so well, we remain on track for that.

Jim Bussone: OK. Great. What are the prevailing rates right now in the marketplace for the Aframax that you're getting?

Bjorn Moller: The open market at the moment in the Far East is around $17,000 per day, and in the Atlantic basin it's moving around. The Caribbean rates were way down into $12,000 or $13,000 a day. They have jumped back up into the high 20s this past week, whereas other Atlantic region markets have been sliding into the low 20s. So it's somewhat volatile, but I'd say on a blended basis the open market is probably slightly under $20,000 a day.

Jim Bussone: OK. Will you shift going forward here? Is the strategy to go to any more long-term contracts or do you keep the same percentage that you currently have?

Bjorn Moller: The strategy is not necessarily to shift tonnage from one segment to the other because the tonnage we have in our spot segment is not necessarily the tonnage that is suited for long-term special projects. However, we are looking to grow both segments and depending on the momentum at any given time and succeeding in growth in one segment or the other, the percentage will shift. So there's really no kind of target blend. We have a number of ideas or projects we're looking at in the long-term sector, which hopefully will grow that business.

Jim Bussone: OK. How about any more interest on the acquisition front?

Bjorn Moller: Well, I guess we will continue to look at how we can add value to shareholders through accretive acquisitions. And that will - we certainly have the firepower to do it, but we want to be disciplined and we'll continue to monitor the market. I can't give you more guidance than that at the minute.

Jim Bussone: That's fine. What would be a comfort level in taking the - what's the high end of your debt to cap?

Bjorn Moller: The comfort level? I guess we typically kept our net debt to total cap in the mid 50s would be kind of the outer range for us. Right now it's, as Peter mentioned, around 41 percent. However, I guess it's partly influenced by the amount of long-term fixed rate cash flow that we enjoy, a number that has been growing very rapidly. And so, it's not an absolute sign, but certainly we tend to manage a very conservative balance sheet at Teekay. But with the liquidity and the size of our balance sheet, we can certainly manage significant growth without getting beyond that debt to total cap range.

Jim Bussone: OK. Great. Thank you.

Bjorn Moller: Thanks.

Operator: We'll now hear from Jordan Alliger with Lazard.

Jordan Alliger: Yes. Hi. Good morning. Just a couple things. One, is it safe to say roughly - it's hard to get the exact number, maybe 10 million tons under the IMO's sort of decision on the category one tankers will be pulled forward from the original schedule in '06, '07 to mid '05. Is that about the number, would you say?

Bjorn Moller: I haven't looked at it that way. I guess what I've looked at is that by 2005 you will have 12 percent gone.

Jordan Alliger: OK.

Bjorn Moller: And you have another, as I mentioned, 30 million, which is another 10 percent that would be possibly kind of falling over the edge 18 - within the following 18 months based on just being economically in the scrapping zone. So regulatorily you will have 12 percent and possibly a bit more because there's some category three tankers that I think we believe the IMO has agreed to phasing out by 2005, but it's kind of left for the December meeting. And so, I think you probably will have about 40 million tons in total gone by the middle of '05 under regulatory pressure and then, as I said, another 30 million that really is very exposed be for the next 18 months.

Jordan Alliger: OK. And then just the second question. Been reading lately more and more about two things in terms of oil production. One, Russia and sort of their plans to expand production and secondarily how the U.S. may rely more on Africa going forward than in the past. I'm just curious your thoughts on both of those regions and what if any implications it would have sort of on - sort of the tanker proportions or tanker demand proportions as you see it over the next three to five years.

Bjorn Moller: Yes, that's a deep question, Jordan, but I think a couple of comments. Firstly, I think the market and the IEA each year is very quick to suggest that OPEC will be squeezed out more and more. Yet we're finding almost consistently every year that OPEC is in fact keeping its place and growing it also from time to time. So, even if OPEC agrees to be a swing producer I think there is very little slack in the non-OPEC system, and there tends to be downward revisions in the production levels. Maybe Russia is the exception.

Secondly there's the issue of where OPEC is agreeing - will agree on an ongoing basis to be the swing producer or whether they will want to fight for market share. We all know that they've done that at times and are capable of doing it any time in the future. So, particularly with Iraq eventually coming back on, it's going to be very interesting to see whether the Middle East will gain market share or whether the rest of OPEC is going to step down. So I don't know more

about that than anyone else, but it's - it tends to be that OPEC plays a much more central role than people talk about.

Secondly, I guess the issue is also what oil is Russia and Africa replacing. If it replaces Middle East oil that would be - it would still have - if it replaces growth that otherwise would occur in the Middle East you'd still have accretive tanker demand, but you will have less accretive tanker demand. And of course to the extent that it replaces a U.S. production or North Sea production, it actually would be quite kind of stimulating for the tanker demand. So I think that short hull oil production is not good for tanker demand, but some of the West African production is actually not that short hull if you think about it. So we're not concerned about that. We just think that it's part of a very dynamic market in which we operate.

Jordan Alliger: Great. Thank you very much for the time on that.

Bjorn Moller: Thanks, Jordan.

Operator: Our next question comes from Manish Chopra with Tiger Management.

Manish Chopra: Good morning, gentlemen.

Bjorn Moller: Hey, Manish.

Manish Chopra: A couple questions, Bjorn. I noticed in the cash flow statement the purchase price of Navion is listed as $698 million, with earlier - I guess initially announced $800 million and I guess $50 million of cash flow was credited in the first quarter. So I wanted to reconcile the $698 million, I guess, with the 750ish number.

Bjorn Moller: Maybe I'll ask Vince to comment on that.

Peter Evensen: Yes, Manish. That - the acquisition, as previously announced, was $800 million. There was also roughly about $50 million in working capital that we assumed on the closing. And then - so if you net out the cash flows in the first quarter from Navion that'll get you probably close to that number. Remember we also paid $76 million in December as a 10 percent deposit. That's not part of the $698 million.

Manish Chopra: How much - I'm sorry - in December?

Peter Evensen: 76 million.

Manish Chopra: 76. OK. At the - what did we end up financing? What was the cost of financing on this transaction at the end of the day, Bjorn?

Vince Lok: It was around one to one-and-a-quarter percent based on a grid over LIBOR.

Manish Chopra: Over LIBOR. And have we fixed that? Is that float?

Peter Evensen: We fixed that for a three-year period.

Manish Chopra: OK. So - OK. So the returns are - returns on capital are materially higher than this cost of capital at least. Can you give us a little bit of color on the nature of the duration on the COAs now that you've been in there for three months versus - or six months, three months since you've taken over the company? Are the contract rents going up, down, more opportunities, less opportunities?

Bjorn Moller: Well, had a pretty thorough due diligence before we bought the company. And I'm glad to say that we found everything there was to find so that there's no surprises when we came in. The

portfolio of contract is significant. I think it's 45 to 50 contracts of a freight covering different fields, fractional use, full vessel use. So to go through that is quite complex. However, I think we've used the guidance that the average contract length in our fixed rate business is seven years. Now that's a whole blend of long-term fixed rate vessel charters to Conoco Philips, to Seaways and offshore loading.

Manish Chopra: OK.

Bjorn Moller: Some of the contracts are for life of field. That might be anywhere 10, 12, 13 years. We have a frame agreement with that oil, which has a finite period, but we're - some of the ships that we have onto them are really the only suited ships for those types of fields. And so, it's a long-term business.

Manish Chopra: OK. Can you give us an update on the unilateral stances of the U.S., Japan, Australia, some of the other countries relative to what do you propose and what the IMO is working on?

Bjorn Moller: I'll try. It's pretty fluid, but I think what we can first of all say that's very positive is that the IMO affirmed the EU's decision to phase out the oldest ships very, very quickly. And so that's extremely positive news for tanker balance - market balance.

Secondly, as far as the period beyond the oldest tankers beyond 2005 it's still open ended. The EU, as you know, wants to phase out the majority of those ships by 2010, irrespective of the age those ships, the single hulled ships are. And that could mean that ships as young as 15 years of age could be banned. The EU - sorry, the IMO, led by the Japanese and other delegations, feel that they accept an accelerated phase out. However, they think that there should be a minimum of 20 years of life, and some people say 23 years of life. And the current rules are 25 years of life. So that's what's going to be resolved in December. So it's - in my personal view, I would think that there will be a compromise to probably around 20 years of life for single hulled tankers

in category two. So that isn't really significantly dilutive to the phase out because the vast majority of single hull tankers are built prior to 1990. So it's still going to be extremely positive for the other tanker market.

Manish Chopra: But in terms of category one, I read somewhere that India had unilaterally gone ahead and followed the EU's rules, I guess acquiring those ...

Bjorn Moller: That were the rules you're talking about. And I believe most recently that India has sort of stepped back from those regulations in anticipation of a global outcome later this year.

Manish Chopra: OK. Last question, is there an update on the airport in Japan that was supposed to use a lot of tanker building capacity?

Bjorn Moller: We hear about that every year, I guess. There's this major project to build a floating airport, which would take up future months of Japanese shipbuilding space to build the structural units and would take up 50 to 100 BLCC spaces. I can't say that I know of it being any closer to fruition than it has been in each other year I've heard about it.

Manish Chopra: OK. Thank you.

Bjorn Moller: Thanks.

Operator: As a reminder, press star one if you have a question. We'll move on to John Burbank with Passport Capital.

John Burbank: Yes. Hi. I was wondering how you're thinking about your fixed rate businesses, what kind of return on capital you're requiring when you're comparing what to do with your profits. Also

interested to know how much you're considering getting into the L&G business given your size and the probable long-term contracts and safer nature of the business.

Bjorn Moller: OK. Good questions. I would say on the long-term business we certainly look at it on a risk-adjusted basis. I guess the best guidance I can give you is really looking historically. In the long-term business we build up the return on equity exceeds 20 percent on average. And that's very attractive. So it gives you a flavor of what we're capable of doing. And I don't see reason why we should not strive for that kind of returns going forward in the long-term business.

As far as L&G is concerned, it certainly is a growth market. It will be a market growing more rapidly than oil, although oil will also grow. And so, it's a market we will study very closely. One thing if there's a lot of demand the question is how much supply will there be, and that will determine whether it will be profitable or not. There are some players that have decided to enter the market speculatively by ordering ships, whereas the majority of other entrants have done so against long-term contracts. We think the entrant to long-term contracts is the most practical way of doing it. And at some point we'll turn our attention to that and decide based on the prevailing opportunities whether to enter or not.

John Burbank: A follow-up question then. Is - given that you're trading six, seven times earnings, you've made almost $4.58 approximately these last six months. And you can borrow - these bank debt you can borrow very cheaply. How are you thinking about growing this long-term business, getting to 20 percent returns on equity, trading at that valuation? At what point do you think about using your cash to buy back stock or just managing your cash in that respect?

Vince Lok: That's a good question. We right now are trying to digest the acquisition of Navion. It was a relatively large acquisition. So we want to try to bring our balance sheet back into bringing the net debt to cap down under 40 percent, into the 30s. And I think that's our priority right now.

Navion is a rather large acquisition, as you've seen from the income statement effect. And so, that's where we're concentrating most of our efforts right now going forward.

John Burbank: OK. And then one comment. I appreciate very much, and I think it's a very smart thing to separate those two businesses in your quarterly statements. Just I think it will lead to a higher multiple given the security of the earnings on that side of the business. So ...

Vince Lok: Right. Thanks for that.

John Burbank: ... I appreciate that.

Peter Evensen: Thank you very much.

Vince Lok: Thank you.

Operator: Magnus Fyhr with Jeffries & Company has a follow-up question.

Magnus Fyhr: Just one follow-up question on the question on oil demand. Bjorn, I know you look at these IEA numbers very closely. Are you surprised for next year to see non-OPEC production growth at a faster pace than global oil demand growth? And I know there's been a lot of downward revisions in the past, but I guess assuming that most of that is coming from Russia.

Bjorn Moller: Well, I'm really not that surprised given where oil prices are. I think you have to accept that in a high oil price environment you're going to get a lot of non-OPEC production. And I'm sure that's one of the things OPEC will be looking at very carefully. At some point they're going to have to make up their minds. Are they going to fight for price or market share? And it's difficult to know where that political will lies. So I'm not surprised. And I also think one should accept that the forecast for non-OPEC tend to be always higher at the beginning of the year than you have at

the end of the year. That's certainly been the vast majority of outcomes. And so, I'm - it's difficult to say I'm surprised. I just think that we'll find that OPEC will make room for itself, and I think that will be what we have to watch. We have to attract OPEC absolute supply in addition to its relative market share.

Magnus Fyhr: OK. Thank you.

Bjorn Moller: Thanks.

Operator: Our next question comes from Helane Becker with Benchmark Company.

Helane Becker: Thank you very much, operator. Hi, Bjorn.

Bjorn Moller: Hi, Helane.

Helane Becker: I just have two questions. One, I noticed on the write down in the quarter on the older equipment. Have you guys looked at the idea, with the way accounting rules have changed in the U.S., of taking - writing down further goodwill off the balance sheet?

Vince Lok: Yes. That is something we look at every quarter. And so, the way we've accounted for goodwill we've done the test. The auditors have reviewed. So there's no impairment of goodwill at this time.

Helane Becker: OK.

Vince Lok: That is something we follow the U.S. GAAP rules very closely.

Helane Becker: Right. Right. OK. And then the other question is with respect to TORM did you say that starting in the third quarter you would be consolidating some of their results?

Bjorn Moller: No, we didn't say that.

Helane Becker: How will you account for that investment?

Vince Lok: Those will be accounted for as marketable securities, similar to our (nats) investment.

Helane Becker: OK. Great. OK. Well, thank you for your help.

Bjorn Moller: Thanks, Helane.

Operator: We'll now hear from Linc Werden with HG Wellington & Company.

Linc Werden: OK. Some people in light of the recent tax bill have commented that perhaps you are in a position to consider a liberalization of your cash dividend under these circumstances with the current earning power, provided tanker rates and your earnings stay anywhere near current quarterly levels. Would you comment on that?

Vince Lok: Yes. As you know, our dividend policy has been unchanged since we went public in 1995. And we are evaluating our dividend policy in light of the new tax law. So we will revert on that as we make our policy decisions.

Linc Werden: OK. Thank you.

Operator: And there are no more questions in the queue at this time. I'll turn the call over to Mr. Moller for any additional or closing remarks.

Bjorn Moller: Yes. Thank you very much and thanks for joining us. We are very excited about the quarter we had and about Teekay's position. So we look forward to talking to you next quarter. Have a great day.

Operator: That concludes today's conference call. We thank you for your participation, and have a nice day.

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