TEEKAY OFFSHORE PARTNERS L.P. Q1-2016 EARNINGS RESULTS

Conference Call Transcript

Moderator: Emily Yee
May 19, 2016
11:00 am CT

Operator: Welcome to Teekay Offshore Partners' First Quarter 2016 Earnings Results Conference Call. During the call, 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 participants will be asked to press star 1 to register for a question. For assistance during the call please press star zero on your touch-tone phone. As a reminder, this call is being recorded.

Now for opening remarks and introductions, I would like to turn the call over to Mr. Peter Evensen, Teekay Offshore Partners' Chief Executive Officer. Please go ahead, sir.

(Cam): Before Mr. Evensen begins, I would like to direct all participants to our Website at www.teekay.com, where you will find a copy of the first quarter 2016 earnings presentation. Mr. Evensen will review this presentation during today's conference call.

Please allow me to remind you our discussion today contains forward-looking statements. Actual results may differ materially from results projected by those forward-looking statements.

Additional information concerning factors that could cause actual results to materially differ from those in the forward-looking statements contained in the first quarter 2016 earnings release and earnings presentation available on our Website.

I will now turn the call over to Mr. Evensen to begin.

Peter Evensen: Thank you, (Cam). Good morning, everyone, and thank you for joining us on our first quarter 2016 investor conference call. I'm joined today by Kenneth Hvid and David Wong CEO and CFO of Teekay Offshore Group Limited; as well as Vince Lok, Teekay Corporation's CFO.

During our call today, I'll be walking through the earnings presentation which can be found on our Website. Starting on slide three of the presentation, I'll briefly review some of Teekay Offshore's recent highlights.

The partnership generated distributable cash flow or DCF of $62 million in the first quarter, resulting in distributable cash flow per limited partner unit of 58 cents. Cash flow from vessel operations, or CFVO, generated by the partnership in the first quarter was $166.1 million, up 22% from the same period of the prior year, driven by the acquisition of the Knarr FPSO in July 2015 and continued high up-time and utilization of our offshore units and fleet.

For the first quarter, we declared a cash distribution of 11 cents per unit, consistent with the prior quarter, resulting in strong distribution coverage of 5.16 times in Q1. Over the past few months, we've completed sale leasebacks on two of our remaining conventional tankers to a third-party.

This transaction allowed the partnership to take advantage of strong asset prices and added approximately $30 million to our liquidity which totaled $336 million at the end of the first quarter.

During our last earnings call in February, we announced that Teekay Offshore had funding needs of approximately $250 million in 2016 and $90 million in 2017. As I'll detail later in the presentation, I'm pleased to report on the great progress that the Teekay Offshore team has made since then.

We're now in a position to tell our investors that we've completed or are nearing completion of a series of financing initiatives which fully address Teekay Offshore's near and medium term debt maturities and fully finance our growth projects through 2018.

Similar to other companies in the offshore value chain, Teekay Offshore has continued to be proactive during this period of rapid deflation in field development and production cost across the value chain and has implemented various cost savings initiatives across the organization which are expected to result in sustainable cost savings of over $30 million per year in G&A and operating cost.

Teekay Offshore is also preparing to take delivery of its extensive pipeline of growth projects in 2016 through 2018 which our customers require for their contracted offshore field development.

Turning to slide four, our on-the-water fleet continues to operate with high up-time had and utilization generating stable and growing cash flows which are supported by a diversified portfolio of long-term contracts with high quality counterparties. The partnership had had a successful first quarter with allowed us to grow our CFVO by 22% over the first quarter of 2015 despite a challenging macro energy environment.

The delivery of several new growth projects in 2015 more than offset the lost CFVO from assets that were redeployed or retired, highlighting the continuity of our business and we expect CFVO had to continue to grow as projects deliver over the next several quarters. CFVO from our FPSO fleet grew by over 50% from the first quarter prior year, mainly driven by the acquisition of our largest FPSO to-date, the Knarr FPSO.

The Knarr FPSO is currently operating under a 10-year contract with Shell, formerly the BG Group on the Knarr Oil Field in the North Sea and the start-up of this contract at full rate in June 2016 is more than offset the reduction in revenue from the Varg FPSO as the unit begins to wind down operations in August after almost 18 years on the Varg field.

As a reminder, the first quarter of 2016 results already reflect the fact that the Varg FPSO no longer receives the capital portion of the charter rate hire effective February 1st. Our other FPSO units have continued to generate steady cash flows in the quarter, operating with high up-time.

With the decline in the oil price, we've seen a change in our customers who are now more interested utilizing existing FPSOs to develop new oil fields rather than new build FPSOs because the lower capital cost of existing FPSOs will result in a lower breakeven cost per barrel.

Based on field development discussions being held with several oil companies, this gives us confidence that we will reemploy the Varg FPSO on a multi-year contract in the North Sea beginning in 2019 and additional benefit of using existing equipment is that it shortens the time from project sanction to start-up and reduces project timing risk.

Turning to our shuttle tanker business, despite the sale or redeployment of several older vessels from our fleet in the last year and the expiration of the Hebron contract fragment last year, cash flows decreased only slightly in the first quarter of 2016 compared to the first quarter of 2015.

Two of our retired shuttle tankers, the Randgrid and the Navion Norvegia are undergoing conversion into the offshore units, namely the Gina Krog FSO and the Libra FPSO, which highlights how we've been able to repurpose older tonnage to generate future CFVO growth.

In 2015, we commenced the East Coast of Canada shuttle tanker contracts and have benefited from increased charter rates under several of our contracts. The shuttle tanker market remains tight with strong underlying fundamentals and we're encouraged by the level of inquiry we've had for receiving contracts of a fragment in the North Sea.

Our shuttle tanker fleet is nearly sold out for 2016 and driven by a combination of more lifting points and new fields coming on stream faster than fields are rolling off, we expect global shuttle tanker utilization to continue to be high.

With our strong operating platform and leading market positions in the North Sea, Brazil, and East Coast Canada basins, we can achieve a high level of fleet utilization and have the flexibility to interchange assets between basins to take advantage of additional growth opportunities.

Our other segments, which include our FSO, Towage, UMS, and conventional businesses, grew by 43% in the first quarter of 2016 compared to the first quarter of 2015.

This was mainly due to the delivery of our first UMS, the Arendal Spirit in mid-2015. Our CFVO growth from this new asset was partially offset by the sale of the two conventional tankers in the fourth quarter of 2015 and the sale leaseback of the two remaining conventional tankers in the first quarter of 2016.

One of the leaseback vessels is currently making a small positive spread on a two-year time charter out contract while the other vessel is currently trading in the spot conventional tanker market.

We've also received strong inbound inquiry in our Towage business and we expect further growth in this business as we start building a book of contracts for our four new buildings as they deliver starting in mid-2016 through early 2017.

I do have an unfortunate operating incident to report. On April 21, we experienced an incident involving the gangway connecting the Arendal Spirit UMS to an FPSO in Brazil. The gangway of the Arendal Spirit was damaged beyond repair, resulting in the UMS being declared off-hire by its charterer until the gangway is replaced.

We've received strong support from Costco shipyard in dismantling the gangway from a sister-ship UMS, which is currently under construction at the yard and we've now arranged for the gangway had to be air freighted to Brazil this week.

Turning to slide five, we've provided an update on our proportionately consolidated run rate of 2017 cash flow from vessel operations estimate, incorporating our latest assumptions on the delivery of growth projects over the next two years and the impact of our cost saving initiatives.

CFVO is expected to increase from a combination of various cost saving initiatives which are expected to translate into OpEx and G&A cost savings and the scheduled delivery of various growth projects. Our growth projects include the delivery of the four state-of-the-art long distance towing and offshore installation vessels during 2016 and 2017.

The upgrade of the Petrojarl I FPSO and commencement of its five-year charter with QGEP in the fourth quarter of 2016, the Gina Krog FSO which is scheduled to commence its contract with Statoil in the first quarter of 2017, the newbuilding Libra FPSO which is scheduled to commence its 12-year charter contract with a Petrobras-led consortium of major oil companies in early 2017, and the delivery of two of three newbuilding shuttle tankers in 2017 that will operate under 15-year contracts for a consortium of field partners in East Coast Canada.

These increases will more than offset the cash flow reductions from the Varg FPSO contract termination, the redelivery of the Navion Saga FSO, and the sale of four conventional tankers.

We continue to receive strong interest from current and potential customers to utilize the NORSOK compliant Varg FPSO on various oilfields as a low cost and quick-to-market solution.

Factoring in all of these initiatives, we're now expecting to generate run rate 2017 CFVO of approximately $850 million, assuming the projects are operating for a full year which represents an increase of 25%. This excludes the additional contribution from the third East Coast Canada shuttle tanker which is scheduled to deliver in early 2018.

On slide six, we've provided a summary of the current TOO financing initiatives we're undertake together address our upcoming funding needs in 2016 and 2017. Since early this year, we've been working on a number of important initiatives involving each of our main sources of capital.

This includes new bank facilities, amendments to certain of our existing Norwegian unsecured bonds, and a new preferred equity issuance, all of which are expected to be completed by June 30th, 2016.

Our bank financing initiatives include a new $250 million pre and post-delivery debt facility to finance our three new building shuttle tankers which are currently being constructed to service the East Coast Canada contracts.

A new $40 million debt facility secured by fleet of six of our currently unmortgaged shuttle tankers and FSO units, a $35 million add-on tranche to an existing loan facility financing the Samba Spirit and Lambada Spirit shuttle tankers operating under a long-term contract for Shell in Brazil, and a $75 million refinancing of the Petrojarl Varg FPSO.

In April, we closed the $35 million shuttle tanker add-on tranche and have received commitments for the new $250 million and $40 million facilities. We've received commitments from a majority of the existing Varg syndicate banks and expect to secure the remaining commitments for this financing within the next week.

Our bondholder initiatives relate to amendments to our existing Norwegian Kroner bonds due in January 2017 and 2018 respectively. Through negotiations with the largest holders of these two bond series, we've reached an agreement whereby the final maturity payments will be extended to November and December 2018 respectively.

For the 101 equivalent January 2017 bonds, 30% of the issuance will amortize in each of October 2016 and October 2017 and for the 144 million equivalent January 2018 bonds, 20% of the issuance will amortize in January 2018.

We've now issued a summons package to all of the holders of these two bonds to formerly vote on the agreement in early June, which only requires approval from two-thirds of those voting.

As of today, bondholders representing more than a majority of the outstanding bonds have already given their undertaking to vote in favor of the proposal, which makes us confident in securing the requisite approval level.

We're also in advanced discussions with a select group of equity investors for a new $200 million issuance of preferred units with a warrant structure which we expect to finalize in the next few weeks following the completion of due diligence and documentation. To minimize the effect on near-term liquidity during the first two years, dividends on these new units would be paid in kind in new common units.

Finally, we've also reviewed our existing asset base and upcoming capital commitments to free up additional liquidity. In the fourth quarter of 2015, we completed the sale of the two conventional tankers and in the first quarter of 2016, we completed the sale leaseback of our remaining two conventional tankers with both initiatives bringing in a combined $60 million of liquidity.

In addition, we're in discussions with the shipyard to defer delivery of our final two UMS new buildings, which would result in the deferral of approximately $400 million of CAPEX payments.

Turning to slide seven, we prepared a comparative liquidity sources and uses chart for each of 2016 and 2017 to illustrate the cash flow impacts of the initiatives I just discussed on the previous slide relative to our cash requirements in each of these periods.

In 2016, we started the year with approximately $280 million of available liquidity including all of the financing initiatives expected to be completed by the end of June, we are now forecasting to finish the year with liquidity of approximately $310 million, which would represent an overall funding surplus translating to an increase in liquidity of approximately $30 million in 2016.

For 2017, including our current financing initiatives, we expect to start and finish the year with the liquidity of approximately $310 million with the expectation we will complete refinancings during 2017 for three loans related to vessels under contracts.

We believe the total liquidity of $310 million for Teekay Offshore is adequate relative to our size and cash flow needs and is comfortably above our current liquidity covenant level of approximately $165 million.

On slide eight, we show the expected positive impact of our current financing initiatives on TOO's CAPEX and debt maturity profiles. As you can see by comparing the chart on the left, which represents our maturity profile without the current initiatives, with the chart on the right, which is our maturity profile adjusted for the various financing initiatives.

These initiatives provide TOO with a liquidity run rate to late 2018, with our growth projects being fully financed, and the scheduled UMS delivery dates and bond maturities deferred.

In addition, you can also see that we've deferred existing near-term put options on related interest rate swaps. Although we have added to the various maturities in 2019, we're anticipating more normalized equity and energy market conditions at this time, which will provide further sources of funding or refinancing.

Turning to slide nine, TOO's balance sheet is projected to delever over the next three years as a result of the amortization of its secured and unsecured debt, which is primarily serviced with cash from operations. Driven by various growth projects which deliver between 2016 and 2017, TOO's cash flow from vessel operations is expected to continue to grow over this period.

As a result, we expect our net debt to CFVO to drop by more than a full turn, from approximately four and a half times in Q1 2016 to approximately 3.2 times by Q4 2018. The combination of lower financial leverage and an improved macro environment for energy; TOO will be in a much better position in late 2017 and 2018 to access the capital markets to refinance its bonds.

Wrapping up on slide 10, we provide a summary of our three-year pipeline of growth projects, with committed financing now secured. Starting at the top, the delivery dates of our four state-of-the-art, long-distance towing and offshore installation vessels have been pushed out slightly and are now scheduled to deliver in the second half of 2016 and the first quarter of 2017.

Under our contract with the shipyard, we will be receiving payments to compensate us for the delayed delivery. Once delivered, these vessels will be immediately available for towage charters, and we're already starting to build a book of contracts for these vessels.

The next row down, the timing of the Petrojarl I FPSO has also shifted slightly, due to certain customer variation orders and the comprehensive scope of the project. The unit is now scheduled to commence operations in the fourth quarter of 2016, rather than the third quarter. Upon delivery, the unit will operate under a five-year charter contract with QGEP on the Atlanta field in the Santos Basin offshore Brazil.

Next, the Gina Krog FSO is scheduled to commence its three-year plus extension options contract with Statoil in the first half of 2017. This unit will operate under a contract with Statoil on the Gina Krog oil and gas field. The FSO unit is being converted from one of TOO's former shuttle tankers, the Randgrid and work at the Sembawang Shipyard in Singapore is ramping up, with approximately 700 people currently working to have the unit ready to sail away from the shipyard in the fourth quarter of 2016.

Turning to the Libra FPSO project, the unit is being converted from Teekay Offshore's shuttle tanker the Navion Norvegia at Jurong Shipyard in Singapore, and is a 50-50 joint venture with Odebrecht Oil & Gas, or OOG. The unit will operate on the large Libra pre-salt field in the Santos Basin offshore Brazil, with estimated reserves of 8 billion to 12 billion barrels, currently considered to be the largest offshore oil field in Brazil.

As of April 30th, this $1 billion conversion project is approximately 65% complete and delivery from the yard is scheduled for December 2016, with first oil expected in early 2017.

While the project remains on budget and is fully financed through an $800 million long-term debt facility, we're currently in advanced discussions with the lenders of the Libra FPSO to insure the continued availability to draw down on this loan, despite the challenges facing our joint venture partner, OOG.

As previously announced, in December 2015, the partnership provided OOG a put call option, which would have enabled OOG to sell to Teekay Offshore up to an additional 25% equity ownership in the project.

As well as a call option to OOG to buyback this interest in January of 2018. On April 25th, this put/call option expired without being exercised, which removes this potential use of TOO's liquidity.

Finally, Teekay Offshore's East Coast Canada shuttle tanker new buildings remain on schedule for delivery in late 2017 and early 2018. Following delivery, these vessels will replace existing in-charters and one of our older shuttle tankers, which are currently servicing the 15-year plus extension option contracts with a consortium of nine oil companies producing oil on three separate East Coast Canada offshore oilfields.

TOO is currently the sole supplier of shuttle tanker services for the region. Construction of these vessels are in the initial stages, with steel cutting for the first two vessels scheduled to commence in July 2016.

As mentioned previously, as part of our financing initiatives, we've now secured commitments from our bank group for a new $250 million pre and post-delivery debt facility to finance the construction of these vessels. And with the signing of this loan, we will have secured financing for all of our growth projects through 2018.

Together, we expect these projects to make significant cash flow contribution over $200 million to TOO's annual CFVO, as I talked about earlier.

Finally, I really want to thank all of our financing partners and stakeholders who have participated in the financing initiatives, including refinancing existing maturities, delaying bond maturities, and committing new funds to enable us to complete our growth projects that will increase our CFVO and DCF per share over the next few years.

The confidence they've shown in our business will put Teekay Offshore in a stronger and more healthy financial position, since we had to temporarily reduce the equity distributions in order to conserve cash to complete our capital growth projects.

Thank you all for listening. And operator, I'm now available to take questions.

Operator: Thank you so much. Ladies and gentlemen, if you would like to ask a question please signal by pressing star 1 on your telephone keypad. If you are using a speakerphone please make sure your mute function is turned off to allow your signal to reach our equipment. Again please press star 1 to ask a question. We'll pause for a moment to allow everyone an opportunity to signal for questions.

The first question comes from the line of Spiro Dounis of UBS. Please go ahead sir.

Spiro Dounis: Hey Peter, hey, Vince. How are you?

Peter Evensen: We're good. Thanks.

Spiro Dounis: Good. First-off congratulations on nearing an end here to closing this gap, clearly a lot of work has been done over the last quarter, so pretty impressive from your standpoint. Just want to touch first, Peter, I know you're in the middle of the process with the preferred equity and color you gave was good on the warrants and if I'm thinking about reasons why maybe the stock traded down this morning, I guess there might be some concerns around dilution and so I realize once again you can't say too much, but maybe if you could sort of book end cost of capital ranges or relative to alternatives to issuing preferred and may be why preferred route was the best way to close most of this gap?

Peter Evensen: Sure. Well, I think it has to do with investor interest first of all. There is an investor interest in taking big participations on a preferred level with companies that have steady cash flow and we've seen that and obviously, we're targeting on the Targa deal and so I would say while I can't be drawn on specifics, I would say it's following basically the Targa structure and that included a preferred equity perpetual with a warrant structure.

So, we're in discussions with a number of investors to finalize the terms and conditions and we expect to move into the due diligence and documentation next week and so that's what gives me comfort that we'll close in mid-June.

Spiro Dounis: Yes. That's helpful. Second question just around the distribution when or how that might come back on. It looks like a lot of your cash flows through 2018 are going to go towards the leveraging. Am I right in thinking that we probably shouldn't expect distribution increase before you sort of reach the target leverage level?

Peter Evensen: I'm not going to get drawn on when we're going to restore the distribution and increase it but that remains our plan as we articulated in December. And what we're doing on the financing initiative side I think gives us the opportunity to one, complete our CAPEX; but two, then we don't have any significant CAPEX beyond 2017.

Spiro Dounis: Got it. Okay. And just last really quick one for me. It sounds like obviously the gap is closed for the time being and things have been pushed out. Just wondering in terms of the other things you mentioned you would have been doing in terms of JVing assets or sale leasebacks or selling assets for the time being should we not expect any additional announcements of those actions for the foreseeable future?

Peter Evensen: Obviously, those kinds of things take longer. We have had various discussions with parties that have expressed interest in buying our some of our assets and/or taking minority stakes in those so I'm not excluding that but we would have to have a good use of the cash.

When you look at selling our assets that would take away from our cash flow increase, and therefore, that would actually hurt our ability to deliver. So the combination of our cash flows increasing will allow us to deliver faster, so that remains our go to strategy.

Spiro Dounis: Got it. That makes sense. Appreciate the color and congrats.

Peter Evensen: So I would just say it's all about maximizing the long term value rather than getting short-term. And I think what we've articulated is our financing strategy which has been supported by the banks reflects that.

Spiro Dounis: Appreciate the color. Thanks Peter.

Peter Evensen: Thank you.

Operator: The next question comes from the line of Fotis Giannakoulis of Morgan Stanley. Please go ahead.

Fotis Giannakoulis: Yes, gentlemen and thank you. Peter, I want to ask about the refinancing of the Varg FPSO. Is the $75 million that you're expecting to get refinancing subs to a contract? And can you give share some information about the repayment of this $75 million especially until the contract comes in place?

Peter Evensen: Sure, so the Varg has been on the Varg oil field for 18 years. We had -- it was subject to options and so the actual field isn't producing very much oil but it's still is producing 6,000 barrels of oil a day but the charter has decided to close it down, so that means we need to refinance the $100 million coming due in June of 2016. We've been in discussion with that existing syndicate. We will reduce the loan to $75 million and put in place an 18 month loan.

We reduced the loan because as you point out, it does not have a contract but when we looked at the value of the Varg and went out and took third party valuations, it was worked somewhere between 250 and 300 million which I can tell you from the discussions we're having with new on new contracts would be justified. And therefore, it's become an asset-based loan but it will be for 18 months from June of 2016 to December of 2017.

Fotis Giannakoulis: And regarding the very deployment of the Varg, what kind of CAPEX would you expect that it will require if it goes to a nearby field?

Kenneth Hvid: Yes, so -- hi, Fotis, this is Kenneth. So as Peter said we are in the middle of the peak commissioning and I'll have slowly started that up and we expect the FPSO to permanently leave the field in early August and discussions we are on potential new deployments are really ranging from anything from early well set where you'd need to do minimum outbreaks to something for a longer period where we would be doing both the outbreaks of the hull as well as the top size all depending on which field we're going on.

So what we're really focused on the Varg FPSO is that as Peter said builds to the NORSOK standout which makes it the only unit out there that meets these straight Norwegian standouts which are very difficult to operate for if you aren't either grandfathered in or you're doing a newbuilding.

So, Varg is in a unique position on that having put option capacity of over 50,000 or 56,000 barrels per day and that's really what out there and bargaining in this lower oil price environment that this is really a unit that can go into that asset production mix that can lower the price to where we see our customers are being prepared to sanction projects, so I can't give you an exact number in terms of what the upgrade is. It's anything from very minimal to maybe a hundred to $150 million. Until if we keep looking at.

Fotis Giannakoulis: Thank you that's very helpful. And I want to ask about the UMS new buildings in Europe 20 years you were mentioning there is a possibility of cancellation, you didn't talk about cancellation during the call and I was wondering if this option is out, is not there any longer or if you think that there can be cancellation and even if you have to pay some penalty or even sale of this new buildings?

Kenneth Hvid: What I can say is that we are in very constructive discussions with the shipyard to defer delivery of the two UMS new buildings but also due to continuous reasons we cannot really comment on the specific at this time, but it's clear we have a number of stakeholders here and we expect what we agreed to is something that's going to be satisfactory to all our stakeholders, bondholders and banks etcetera, so I can just say that the discussions are very constructive.

Fotis Giannakoulis: Just to clarify...

(Crosstalk)

Kenneth Hvid: The other point to be mindful of is of course that the contracts continue were entered into by lot and they continue to be non-recourse to Teekay Offshore as we've pointed out before.

Fotis Giannakoulis: Yes, that's very helpful. Just to clarify because I think in your previous call you mentioned that the last vessel was already delayed by one year, are you talking about further delay of last vessel or are you talking about the second vessel that you hadn't discussed about?

Kenneth Hvid: Yes, both.

Fotis Giannakoulis: Okay, great. That's very helpful. And I also want to ask about your discussions with Petrobras, obviously there is a lot of rumors about Petrobras and the changes in the government and the scandal that you mentioned also in your Risk Factors. Do you have any quarter that you can give us regarding the counterparty risk and if there are any thoughts of amending any of the existing contracts?

Kenneth Hvid: Yes, I would say we first of all, all our asset also fully utilized by Petrobras in what I would say is revenue generating activities, so I think that in itself is a fundamental thing that's very important here as we look at the different assets that not only Petrobras but all other companies either have a use for or not have a use for and all assets are all being fully utilized. That's really what we first look at.

The second point is also which is a question received is if we are receiving payment on time and yes we have. So obviously, as we are having with customers around the world we are having discussions about contracts but they have only been constructive up to this point and we have not had any amendments to our contracts up to now.

Fotis Giannakoulis: Thank you very much.

(Crosstalk)

Peter Evensen: I would just add that as we've said to investors that there's been a lot of talk about Petrobras Abrogating charters but all of that is on the exploration side when all of our assets are contributing to generating cash flow for Petrobras.

So that's a different conversation when you're adding to someone's cash flow rather than subtracting from their cash flow.

Fotis Giannakoulis: Thank you very much, Peter. Thank you, both.

Peter Evensen: Thank you.

Operator: The next question comes from the line of Mike Webber of Wells Fargo. Please go ahead, sir.

Michael Webber: Hi. Good morning, guys. How are you?

Peter Evensen: Good, thanks.

Michael Webber I just wanted to go over the subject to follow-up on Petrobras and maybe just be specific about the assets so the FAU, the Arendal Spirit had a gangway issue. One, I mean can you have a value on the gangway? I can't imagine that it's so expensive and the fact that it's getting airlifted over I guess makes sense but I actually haven't thought about how you'd get one over there.

But two, you know, while I'm sure there it's employed in a profitable Enterprise it can always be more profitable so does the fact that there is now off hire and provide a window for the contract to get renegotiated and if you can't give me a specific there is that something that you think that is viable probability that that could happen or possibility that could happen and how do you think about that from a budgeting perspective?

Peter Evensen: Sure. I'll take the first part of the question, and Kenneth will talk about negotiations to extend that contract. So you're right. First of all, it's an insurable event, so we're buying the gangway from the Costco shipyard, and it's going to be air freighted to Brazil this weekend.

The Arendal Spirit has departed the field and has moved closer to shore where we will be installing the new gangway. And so we're in close dialogue with Petrobras for the startup and as well as to insure we don't have a repetition of this incident. So all-in all we hope to be back in operation and of course generating cash in the next couple of weeks and Petrobras really likes the contract.

Kenneth Hvid: That's correct, Peter. We are actually very close to finalizing a potential extension of the contract and without being going on the details which is we won't until we conclude the discussions, it is under a plan and extend model that is clearly in our interest obviously but also works for Petrobras, but we'll be back in due course with more details on it but we have only received positive feedback on the unit and that's of course the reason why we are also discussing an extension.

All of the features that the unit have and where it's at first of all it has very high upside until the unfortunate incident here, but where we've seen it being used and that will add value to the operations is that it has a very large debt capacity and more high train capacity, so in particular in some of the heavy lift operations for on the larger FPSO's where you take large pieces of equipment off its proven itself as being very stable and extremely useful in these operations and that's the feedback that we're getting.

Michael Webber: Okay.

Kenneth Hvid: And then it's also being used as we mentioned before it had some of these features and we've seen that being used for the hydro-blasting which is a big part of the job when you go out and maintain the FPSOs, so we use produce water and because we have a lot of tank storage in these hauls which you don't have, we're using that to produce the water and basically go out, so it's been fully utilized.

Michael Webber: Right, no I guess the question was just does this provide a window for it to lower or bring the rate down or does it impact the amend and extend idea but it seems like that's kind of TBD. I guess one under on this asset.

Out of curiosity the issue at the gangway, I know you aren't giving specifics with what happened with it but is it in any way unique to the cylindrical design of the asset. Is it something that would have happen with the ship shape or something to happen with the design around those?

Kenneth Hvid: No we don't believe so.

Michael Webber: Okay. I did want to follow-up on another question around the FAU. The additional FAU deliveries and this is more nuance and Peter you kind of touched on this but I just want to be clear.

In the deck, the language of negotiations to push those back, I know they are obviously one has been falling off or a follow-up of liquidity side last year but pushed back to 19 and the 17 and it seems like that's relatively tentative and most of that is 90 plus percent of that CAPEX is due upon delivery so you really are just pushing back one bullet.

Is that nuance language for a specific reason or is there any real probability there is going to be some sort of issue in terms of not being able to push those back? I'm trying to figure out as to why that wouldn't be finalized and/or what are the major hurdles remaining to actually locking that down?

Peter Evensen: Well, discussions take time and as Kenneth pointed out, those shipyard contracts are non-recourse to Teekay Offshore. So, I think you can read into slide eight when we looked at our anticipated maturity profile.

Michael Webber: Right, okay. That's what I figured. I just wanted to double check the language. Just to stay on the FPSOs and you touched on this a bit earlier, but they defaulted on their bonds actually I believe it's two of the entities and they didn't exercise the put option but it's a bit more complex and just I guess a simple benefit and a liquidity, your near term liquidity profile.

I guess can you maybe layout for us or walk us through one, how you think about kind of the exiting value at risk associated with that project and how a foreign ownership restriction would impact your ability to proceed with or without and maybe just give us around that prospect because it's certainly something a bit more Esoteric than some of the business you guys have been focused on in the past and it seems to be more complex and simply not exercising the option.

Peter Evensen: Well, that was Odebrecht that did not exercise the option and they didn't meet the terms to exercise the option. As you have pointed out Odebrecht, as well as OOG, which is 80% owned by Odebrecht, they have various financial issues that has drawn concern from us as well as from the banks financing the Libra FPSO but what Odebrecht has agreed to do and has already done is put up all of the equity required for this project up front so we are not at risk that Odebrecht will not fund their portion of the project.

And for me as a joint venture partner that reduces not having to come up with somebody else's cash and negative event is something that I would see as not being that's our biggest risk and we don't have that risk and as far as changing the ownership we don't have any issues as it relates to that, but we have to wait for what's happening at Odebrecht and OOG to play itself out but as far as it relates to the project it is not affecting the project.

The construction is ongoing, it's 65% and we haven't been affected by Odebrecht, going forward and I just will say that the people that Odebrecht had have contributed to the project have been key individuals, so we've been very happy with the contribution that Odebrecht has made to this project.

Michael Webber: Got it. And in any terms any availability of Odebrecht to claw back that equity other then or their bondholders I mean, in the first place my idea if they make it -- made them put the option and they defaulted on the bond and made that payment....

(Crosstalk)

Michael Webber: Got it. And in any terms any availability of Odebrecht to claw back that equity other then or their bondholders I mean, in the first place my idea if they make it -- made them put the option and they defaulted on the bond and made that payment....

(Crosstalk)

Peter Evensen: No, they have prepaid all of their equity, so that's where it is. So we feel good about that from being a joint venture partner.

Michael Webber: Okay. Fair enough. I will slip out and get back in the queue, but I appreciate the time guys, thank you.

Peter Evensen: Thank you.

Operator: The next question comes from the line of Nick Raza of Citigroup. Please go ahead, sir.

Nick Raza: Thanks guys. Most of my questions were answered just had a couple follow-ups. In terms of the prepaid equity for Odebrecht, does that cover any potential cost overruns as well?

Peter Evensen No it doesn't. It just covers the actual amount that is they had to put in that was pre-agreed but we remain on budget right now so we aren't seeing any cost overruns as we sit here right now.

Nick Raza: Okay. And then my second question is understanding that you've sort of are in the works for delaying the UMS vessels, is there a cost associated with delaying them?

Peter Evensen: No.

Nick Raza: What should we look towards in terms of positive news in terms of contracting them besides, you know, an oil price?

Peter Evensen: I think they've been deferred and so we're concentrating on as Kenneth said extending the Arendal Spirit and that's where we're looking at right now.

Nick Raza: All right. Thank you.

Kenneth Hvid: But if you look at the stakes are as such. I think you read across probably on the conversation so you may read that as well but it's as we pointed out before there's some scrapping of older units that looks like it's in the works and that will happen and we still believe fundamentally that there's a lot of maintenance that needs to be done offshore and some of that is maybe being timed a little bit differently but some of those requirements have not gone their way on a permanent basis so it's a timing thing, but as you say, we are all looking at the oil price.

Nick Raza: Fair enough. Actually, I did have one follow-up question regarding the shuttle tanker segment in Canada. What percentage of a producer's cost does the shuttle tanker actually represent

Peter Evensen: I don't know the answer to that question. What I will tell you is that all nine oil companies agreed that Teekay could do it cheaper than they could do it themselves and that's, so I don't have the field specifics on what the lifting cost is on the East Coast Canada you could look at Wood McKenzie or whatever and get that data.

Nick Raza: Thanks, guys. That's all I had.

Peter Evensen: Thank you.

Operator: The next question comes from the line of Wayne Cooperman of Cobalt Capital. Please go ahead, sir.

Wayne Cooperman: Hey, guys I just want to know how I get involved with these discussions for preferred equity given that I'm a relatively large shareholder I'd be interested participating.

Peter Evensen: Okay. Well, give me a call afterwards, Wayne.

Wayne Cooperman: Sure.

Peter Evensen: Okay?

Wayne Cooperman: Yep.

Peter Evensen: Good. Thanks.

Operator: The next question comes from the line of Gilbert Creedberg of EMG Investment Partners. Please go ahead.

Gilbert Creedberg: Thank you. Both of my questions were answered in prior commentary so I appreciate your time. Thank you.

Peter Evensen: Thank you.

Operator: The next question comes from the line of Ben Brownlow of Raymond James. Please go ahead, sir.

Ben Brownlow: Hi, Peter. Congratulations on all of the financing initiatives. Can you discuss some on the cost reduction plan of $30 million, how far along are you to fully realizing that? And just some color on the timeline and is that weighted more towards the OpEx side?

Kenneth Hvid: This is Kenneth here. I'd say out of the $30 million it's probably a little bit more heavy weighted on the G&A side now but we see more we can get on the OpEx side going forward for that needs to be worked on so we make sure that it's actually sustainable but we are very close on the $30 million and we expect to go beyond it and will report back in that in future quarters.

Ben Brownlow: Okay. So that was pretty notable already realized in the first quarter in terms of just kind of modeling purposes and how we should think about that on a quarterly run rate?

Peter Evensen: No, there are some one offs you have to pay as people are made redundant, so I wouldn't model in the full $30 million until Q4.

Kenneth Hvid: Yes, we would have to start it in Q3/Q4 and then full realization wouldn't happen in 2017.

Ben Brownlow: Great, very helpful. Thank you, guys.

Peter Evensen Thank you.

Operator: Next question comes from the line of Michael Webber, Wells Fargo. Please go ahead, sir.

Michael Webber: Hey, guys. Thanks. Just wanted to hop back on to clarify something Peter around delaying the EMS vessel there is a carry cost associated with that correct?

Peter Evensen: No.

Michael Webber: Is that something that was...

(Crosstalk)

Peter Evensen: Not unless we take delivery with it. Not unless we take delivery.

Michael Webber: Okay so there's a cost if you push the delivery back at like 5% to 6% of the remaining CAPEX in terms of carry but if you don't take delivery you're saying there's no walk away fee or anything like that?

Peter Evensen: I answered the question. I'm not answering anymore.

Michael Webber: Okay. Thanks guys.

Peter Evensen: Thank you.

Operator: There are no further questions at this time -- in the queue at this time. Please continue, Mr. Evensen.

Peter Evensen: All right. Thank you all very much. We made a lot of progress this quarter in particular on the financing side and as Kenneth said there's also a lot of work going on the operating side. And so we look forward to reporting back to you next quarter and of course giving you an update in the interim on the completion of the financing initiatives. Thank you all very much.

Operator: Ladies and gentlemen, this concludes the conference call for today. We thank you for your participation. You may now disconnect your line and have a great day.

END