



TEEKAY OFFSHORE PARTNERS' FIRST QUARTER EARNINGS RESULTS

Conference Call Transcript

Date: Thursday, 18th May 2017

Time: 12.00 EST

Operator: Good day and welcome to Teekay Offshore Partners' First Quarter 2017 Earnings 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 one to register for a question. For assistance during the call, please press star zero on your touchtone phone. As a reminder, this call is being recorded.

Now for opening remarks and introductions, I would like to turn the call over to Ingvild Sæther, Teekay Offshore Group's President and Chief Executive Officer. Please go ahead.

Speaker: Before Ms Sæther begins, I'd like to direct all participants to our website at www.teekayoffshore.com where you'll find a copy of the First Quarter 2017 Earnings Presentation. Ms Sæther will review this presentation during today's conference call.

Please allow me to remind you that 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 is contained in the First Quarter 2017 Earnings Release and Earnings Presentation available on our website.

And now, I'll turn the call over to Ms Sæther to begin.

Ingvild Sæther: Thank you, Ryan. Hello, everyone, and thank you for joining us on our First Quarter 2017 Investor Conference Call. I'm joined today by David Wong, the CFO of Teekay Offshore Group as well as Kenneth Hvid, Teekay Corporation's President and CEO, and Vince Lok, Teekay Corporation's CFO.

During our call today, I will be taking you through the Earnings Presentation which can be found on our website.

Turning to slide three of the presentation, I will briefly review some of Teekay Offshore's recent highlights. In the first quarter of 2017, the partnership that generated distributable cash flow, or DCF, of 30.6 million or \$0.20 on a per unit basis. Results for the quarter were better than our expectations



and were generally in line with market projections. This is driven mainly by the stronger than expected performance of our shuttle tankers and FPSO segments.

There were a number of positive events during the quarter. I'm pleased to announce that we took delivery of the 50% on Libra FPSO in late March, which actually arrived in Brazil waters today to commence commissioning on the field for its scheduled start-up at the end of June or early July.

Since reporting earnings last quarter, our shuttle tanker business continues to perform strongly and we have recently secured two new multi-year contract of affreightment in the North Sea. We completed a five-year extension of the charter contract for the Falcon Spirit FSO unit, and finally, in early April, we entered into a customer-funded front end engineering and design, or FEED, receipt study for the Varg FPSO unit on the Cheviot field in the North Sea.

However, despite our strong start to the year, the Partnership's results for the first quarter were negatively impacted by the continue non-payment of charter hire on the Arendal Spirit Units for Maintenance and Safety, or UMS. In addition, we have now received notice from Petrobras, the charter, instructing us to demobilise the unit and thereafter, terminating the charter contract. We are disputing this termination, which I will discuss later in my presentation.

Turning to slide four, we continue to push forward to deliver on our pipeline of committed growth projects. This is a slide we have shown you in previous quarters, updated to reflect the latest remaining capex and financing figures as of 31st March 2017.

We are pleased to announce the delivery of the largest of these projects, the jointly-owned Libra FPSO, which I will touch on in a moment. Updating you on a couple of the other large projects on this slide, Gina Krog FSO's project has experienced some delays and cost increases, with the unit now expected to be hooked up on the field during the third quarter of 2017. We are providing Statoil with an interim solution using shuttle tankers that will enable Statoil to start up the Gina Krog field when they are ready.

Last quarter, I discussed the delays and additional cost we have experienced on the Petrojarl FPSO upgrade project and we continue to work constructively with the charterer, shipyard and our lenders to deliver this unit into operation as soon as possible.

Progress at the shipyard continues with over 90% of pipe welding now completed and 99% of electrical cabling now pulled, both key measures of progress to sail away. We are targeting an early-2018 timeframe for the FPSO to commence the contract on the Atlanta Field offshore Brazil.

As a reminder, once all these projects have delivered, they are projected to contribute an additional 200 million per year of run rate CFVO.



Turning to slide five, I will provide a few more details on the Libra FPSO conversion, which is getting closer to start-up. The Libra FPSO unit, which is a 50-50 joint venture with Odebrecht Oil & Gas, was converted at a Jurong Shipyard in Singapore. The mechanical completion and delivery of this \$1 billion conversion project on time and on budget is a great example of how a project of this scale and scope can be effectively executed. As you can see from the chronological photos down on the right side of the slide, a significant amount of work and materials went into this project, which are reflected in the statistics shown on the slide. And most importantly are the 20 million man hours worked without lost time injury.

The Libra FPSO unit actually arrived in Brazilian waters this morning where it will soon commence commissioning on the Libra field for a 12-year contract with the consortium of oil companies led by Petrobras. The charter contract is expected to commence by late June or early July.

Turning to slide six, through inbound inquiry discussions with our diverse customer base and reports in the media. There has been increasing evidence to suggest that we are beginning to see some greenshoots in our core offshore market, as captured in the recent headlines on this slide. Positive progress is being made in bridging offshore field development – in bringing offshore field development costs down, which may enable further new field developments to proceed towards final investment decision in the coming months. We are still in early days, but already the headlines are translating into tangible results for Teekay Offshore's business in the form of new shuttle tanker contracts, existing charter extensions and potential new offshore production contracts.

Turning to slide seven, since reporting earnings in February in February 2017, our Business Development Teams have continued to successfully secure new charter contracts and extensions. In addition to finalising the five-year shuttle tanker CoA contract I mentioned last quarter. We have also recently secured another new three-year shuttle tanker CoA contract, both done at successively higher rates. The contracts, which will serve as the Kraken and the Catcher Field in the UK sector of the North Sea will commence between the third quarter of 2017 and the first quarter of 2018.

Our shuttle tanker fleet continues to perform strongly, and these new contracts will only add to the approximately 270 million of annualised cash flow from Vessel Operations or CFVO reported in the first quarter. Combined with the new Glen Lyon, shuttle tanker CoA contract, the three recent contract awards will require approximately an additional 3.3 vessel equivalents per annum over the next eight months, which will increase the utilisation of our CoA fleet. And these three contracts will add 230 million to our fixed forward revenues. With the delivery of the three Suezmax class shuttle tanker new buildings, servicing our existing East Coast Canada operations our shuttle tanker CFVO is expected to grow even further as these vessels deliver between Q3, 2017 and Q1, 2018.

Turning to slide eight, the offshore production market is also starting to see early signs of an uptick in direct investment. In March, Teekay Offshore entered into a customer-funded front-end engineering and design FEED study for the Varg FPSO with Alpha Petroleum. During the six month FEED study we will define the required field-specific FPSO modification and negotiate terms of a



potential FPSO lease and operate contract for the development of the Cheviot field, which is one of the largest undeveloped fields in the UK sector of the north sea. In addition, the partnership finalised a five-year contract extension, plus extension options for the Falcon Spirit FSO unit with no material capital investments.

The extension will commence on 1st June, 2017. This extension demonstrates a continued economic viability of the Falcon Spirit FSO unit which has been operating on the Al Rayyan field located offshore Qatar since 2009. Turning to slide nine, in late April, we received a termination notice from Petrobras for the Arendal Spirit UMS charter contract. As a reminder in early November 2016, the Arendal Spirit UMS experienced an operational incident relating to its dynamic positioning or DP system. Following the November incident, the charter Petrobras initiated an operational review and concurrently suspended charter higher payments to the partnership. In response to that incident we worked with GE the supplier of the DP system and upgrades were made to the software control system. The units meets all class requirements has been thoroughly tested and has been fully operational and ready for service since 11th November, 2016.

While I'm not currently able to get into specifics of the termination notification and our response I can confirm that we are disputing the termination and reviewing all of our legal options. This includes our ability to collect all charter hire, owing to the partnership since 11 November, 2016 when the unit was once again available for operations by Petrobras as required under the charter contract. At the same time, we are seeking alternative employment opportunities for the unit in the event that we are unable to resolve our differences with Petrobras. We are working with our lenders under the loan facility secured by the Arendal Spirit to grant an extension of the facility while we obtain new employment for the unit. This is one of our highest near term priorities.

Wrapping up, I believe the recent contract awards represent what is an improving trend in the offshore sector although we have certain challenges to deal with notably the Arendal Spirit termination and completing the Petrojarl I project. We remain committed to the priorities I highlighted last quarter. Remaining focused on continually striving for high standards for safety and operational excellence, maintaining a team focused on project execution and delivering this project to contract startup to drive continued growth in the partnership operating cash flow. Working diligently to extend or secure new contracts for our assets. Optimising our asset portfolio which may include certain asset sales and/or seeking joint venture partners, and finally continuing to strengthen our balance sheet and liquidity position.

Thank you all for listening. Operator, we are now available to take questions.

Operator: Thank you. We'll take our first question from Michael Webber with Wells Fargo.

Michael Webber: Good morning guys. How are you?

Ingvild Sæther: Good morning. How are you?



Michael Webber: Good. Ingvild, I wanted it to start with Petrobras and the Arendal Spirit. The notification period, there are notification periods or any degree of notification acquired to start the 180-day period after which the banks can potentially call the loan on the Arendal Spirit. And does that start from the date that you actually got the notification from Petrobras they were cancelling the charter?

David Wong: Mike, David here.

Michael Webber: Hi David.

David Wong: The loan would -- hi -- 180 days would start with the date that we received the letter from Petrobras. So that would have been late April.

Michael Webber: Got you and I know it is somewhat sensitive, but can you give any colour to how the conversations have gone with your lending banks around the loans on that asset and then also the Petrojarl 1 and then David from a management perspective and from a cash perspective are capital calls associated with those loans something that you think is likely enough that you're budgeting in for the remainder of the year and or kind of looking at I guess liquidity leverage to be able to handle or they're far enough out on the window that, that is not something that's consuming your time right now.

David Wong: Okay so just to give you to address your questions related to talking to our lenders, right now, its early days. I mean we just received the notification, but we are in active dialogue with our lenders on the Arendal loan to seek an extension or amendment associated with that. So with the Petrojarl 1 loan we continued to discuss with the lenders as well. They have been fully briefed on the dialogues we're having with the charterer and the yard, and we had, as you've probably seen, several extensions of that loan and will continue to work with them on that. Related to capital calls certainly looking that the Arendal loan we are looking at that and how it impacts on liquidity and then incorporate all those related to refinance and as well in our sort of medium to long term financing and liquidity requirements. And as we've mentioned and Ingvild mentioned in the presentation we're looking at various alternatives to address liquidity in addition to looking at partial asset sales or joint ventures which we feel will fulfill our needs over the long term.

Michael Webber: Right and I guess just one more and I'll turn it over. But along those lines David can you maybe, can you weigh out maybe specifically the tools you guys have from a liquidity perspective and then how you prioritise those be it asset sales, but then the FPSO or the shuttle side or other segments new equity be preferred or common just maybe kind of layout the toolkit you guys have to kind of handle some of these smaller rush[?]fires?

David Wong: Well as I mentioned looking at partial asset sales or joint ventures, building on the things that we've been doing throughout the Teekay organisation which you see successful in TGP. At this point we can't get into details related to the specific assets or areas that we're looking at, but certainly when we get closer to completion we'd be excited to talk about that.



Michael Webber: Okay thanks, I will turn it over and hop back in the queue. Thanks guys.

Operator: We'll go next to Spiro Dounis with UBS Securities.

Spiro Dounis: Hey good afternoon, thanks for taking the question. Just sticking with the Arendal Spirit, trying to get a sense for your ability to re-charter that asset, I know you had two other UMS at one point that were in the order book and cancelled so give us a sense for the demand for these types of assets and how quickly you could theoretically get that back on charter?

Ingvild Sæther: Yeah, well the accommodation market is a quite a niche market with only 31 units worldwide. And there has actually been quite healthy activity in the last five, six months with several contracts concluded. We have seen Petrobras sites doing a couple of contracts and we do see some requirements in the market both in West Africa and in the UK sector. Mexico is also a typical market for the accommodation units and with the oil companies cutting back on maintenance over the last couple of years as a result of for serving cash we are quite hopeful that we will be able to find employment for this unit in the event that we are not able to come to a agreement with Petrobras.

Spiro Dounis: Okay and just as I'm thinking about I guess obviously this is now your main focus. Is there a concern that this may be spread into the other initiatives you've got in front of you and specifically what I'm getting at is you guys have debt that you need refinance. You mentioned potential sales or partial sales or joint ventures. But then also you've got you know FPSOs coming off charter next year with Petrobras. Does this impact any of those negotiations? Is there any sort of contagion that occurs as a result of this?

Ingvild Sæther: We have a very good and constructive dialogue with Petrobras on several assets. They are a big customer of ours as you mentioned on the FPSO side as well and we don't have any indication that this is impacting other parts of the Petrobras relationship.

Spiro Dounis: Okay and just last one for me. Just on the Alpha FEED study certainly a lot of positive news there. Just ballpark figures do you think you can provide any I think the Varg before was earning about 49 million in EBITDA. Give us a sense for maybe how much Capex you might have to spend on this project and then maybe how to think about EBITDA in that context?

Ingvild Sæther: It's early days on that project and we are going through the FEED study now so that will determine the level of investment that need to be made and then the subsequent charter hire. So it's too early to say.

Spiro Dounis: Okay I appreciate. Okay fair enough, appreciate the colour.

Ingvild Sæther: Thank you.

Operator: We'll go next to Fotis Giannakoulis with Morgan Stanley.



Fotis Giannakoulis: Yes, hi and thank you. Just to follow-up on the Arendal Spirit if I calculate well expenses in G&A this is the last 12 months for the UMS segment was around 38 million. Now that the vessel is without a contract or if we assume that the vessel will stay idle for a period of time. How shall we think of the expenses of this vessel?

Ingvild Sæther: So our main focus will of course be to marketing the units and get this on a new contract, and it's difficult to say what level that will be at. So if we are -- if would have an idle period between now and the possible new contract we will of course the focus on limiting the cost as much as possible in that period.

Fotis Giannakoulis: And regarding the debt repayments can you first remind also what is the debt outstanding on this unit, and what happens with the debt repayments during the period that the unit is between contracts?

David Wong: The debt total now it is 120 million as of March 31st, and it will continue to amortise down during the period whether the unit is on-hire off-hire.

Fotis Giannakoulis: Okay thank you. I saw some you mentioned about some cost overruns for the Gina Krog. I saw that your estimated Capex between previous quarter and this quarter went down \$12 million. It seems that you repaid in this quarter \$55 million for the owned vessels. Are these cost overruns all related to the Gina Krog or they were some other vessels involved this number? And also can you explain to us what were the components of this overruns at which part of the construction the budget was exceeded?

David Wong: Maybe just to address the cost overruns, the cost overruns are both within the Gina Krog project and the Petrojarl 1 project, but not significant in magnitude, but just related to some of the extensions associated with being at the yard a little longer for Gina Krog and then just taking over some more additional work with the Petrojarl 1.

Fotis Giannakoulis: Were there are any upgrades on the vessel or the changes in the specifications and I was wondering if this increase in the cost will be even partially reimbursed by a modification on the contract?

Ingvild Sæther: So there are a number of reasons for the cost increases throughout the projects and it's related to scope increases and also related to the time so that the expenses being driven by time like project management and commissioning. And these are not costs that will be compensated by the customer, but we are very, very close to finalising and sailing. So we feel we have a relatively good overview of what's left and are keen to get the vessel on contract with the charterers.

Fotis Giannakoulis: Thank you. That's very helpful. One last question for me. You mentioned that you're looking for JV partners and potential candidates for sales within your fleet. I was wondering if these discussions may include the possibility of a spin-off of any of your segments or the shuttle tanker segment or any other segment into a new entity that would facilitate this kind of transactions?



Ingvild Sæther: Yeah, we're not in a position to provide any details at this time and we will update the markets at appropriate time. But that as you have seen we are working with the partnerships and joint ventures across many parts of Teekay and that is a model that we see works well. So it is one of our priorities to look at that.

Fotis Giannakoulis: Thank you very much. That's very helpful.

Operator: We'll go next to Ben Brownlow with Raymond James.

Ben Brownlow: Hi. Good morning. Thanks for taking the question. On the Gina Krog, what -- that bridging solution with shuttle tankers can you just give a little colour around what that revenue and fee structure would look like?

Ingvild Sæther: Yeah, that would be shuttle tanker rates for the shuttle tanker so that this is a solution that we have put in place in order to be sure that we are not delaying the start up of the field which is of course very important for the customer. So this will be a short term couple of months solution where we will just be earning a regular shuttle tanker rate for the shuttle tanker.

Ben Brownlow: Okay that's helpful. And more from me on the towage segment, I think you had a reimbursement from some of the delivery delays. Can you talk about the accounting there when that will flow through?

David Wong: Yeah, so we did get -- we get liquidity damages from the yards due to the delays. We received the money in April and from an accounting perspective is really just nets against the capital cost of the unit.

Ben Brownlow: Okay that's helpful. And any update around the trends within that segment that you're seeing?

Ingvild Sæther: Well the towage market is quite challenging with relatively low utilisation and low rate. And we expect that to last for still some time. The activity in this segment is as you know driven by the number of rig moves so it can be new unit, movement of existing units and movement of units sold for scrap. We have a fleet of new vessel that provide good customer value so we are quite confident that when the market does pick up we will be one of the first to benefit from that.

Ben Brownlow: Great thank you.

Operator: We'll go next to Andy [inaudible] with [inaudible].

Speaker: Oh hi, couple of quick questions here. On the FSO Falcon Spirit, any colour on the rates for that?



Ingvild Sæther: What we can say is that this has been a discussion that has gone on for quite some time with this extension. So the -- and we have done a rate adjustment to get a longer contract, but that has already taken effect. So the income will be in line with the previous quarter.

Speaker: Okay so --

David Wong: So it's just about 7 million EBITDA annual and as Ingvild said it's already incorporated into our cash flow as we have always had that amount over the past year.

Speaker: Understood, and then it's positive to see the CFVO from the shuttle this number 270 million that you put out, that is just confirming this is before the East Canada, East Coast Canada shuttles right? This is your existing fleet.

Ingvild Sæther: That is correct. That's the Q1 annualised cash flow. So there will be a number of new contracts coming in over the next couple of quarters to increase that.

David Wong: The 270 million doesn't include the new builds been added to the fleet so that would add additional cash flow once those delivered.

Speaker: Understood and can you disclose approximately what the margin is revenue minus Opex. I know you've got some time charters, some COAs and bareboat so it will vary. But what's sort of a good number to use for revenue and Opex for the variety of contracts?

Ingvild Sæther: Well for the new contracts, there will be a number of the factors influencing. So when they start up, how quickly the ramp-up so it's a bit difficult to give a guidance exactly how that will play out in the next couple of quarters. But as I said it is 230 million of fixed forward revenues so it's significant future cash flow to the partnership.

Speaker: Yeah final question for me. On the \$210 million loan to Arendal Spirit, is that effectively non-recourse to TOO and Teekay?

David Wong: The loan which is just to clarify \$120 million loan would be --

Speaker: 120 sorry.

David Wong: -- would be guaranteed by Teekay Offshore, stay within -- its within the Teekay Offshore facility.

Speaker: So it is guaranteed by that -- you can't just hand over the Arendal Spirit of the banks worst case scenario.

David Wong: No.

Speaker: Okay understood, great, thank you.

Operator: We'll go next to Michael Webber with Wells Fargo.

Michael Webber: Hey guys, just had one follow-up along those lines. Can you remind us who in the lending syndicates for the Arendal Spirit and the Petrojarl 1 and maybe what kind of overlaps there may be there with say the rest of your book trying to get a sense on how intertwined your lending base is?

Vince Lok: Yeah the loan of the Arendal is with couple of our key banks including an ECA so it's a small group of banks in that facility.

Michael Webber: And is it relatively isolated? Is it exposure there across kind of the entire TOO structure?

Vince Lok: Well they are lenders to other Teekay entities and other loans. So it is they are part of other facilities within the Teekay Group, but as you know we have very supportive bank group amongst the Teekay Group and that we are in discussions with them and keeping them informed as we have over the past several months.

Michael Webber: Got you, great, thanks for that.

Operator: And now we will conclude our question and answer session. I'd like to turn the conference back over to Ms. Sæther for any additional or closing remarks.

Ingvild Sæther: Thank you. Well as you heard there's a lot going on across the partnership and over the next couple of quarters we will have delivered all our major projects and they will contribute to our cash flow. So our focus will then be to focus on the redeploying our assets that's coming off contract and really positioning us for the strengthening shuttle market in what we believe will be a recovering offshore market so thank you.

Operator: That does conclude today's conference. We thank you for your participation. You may now disconnect.