TEEKAY TANKERS LTD.

Moderator: Kevin Mackay
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12:00 pm CT

Operator: Welcome to Teekay Tankers Third Quarter 2014 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 0 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. Kevin Mackay, Teekay Tankers' Chief Executive Officer. Please go ahead Sir.

Ryan Hamilton: Before Mr. Mackay begins, I would like to direct all participants to our Web site at www.tktankers.com, where you will find a copy of the third quarter 2014 earnings presentation. Mr. Mackay 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 third quarter 2014 earnings release and earnings presentation available on our website.

I'll now turn the call over to Mr. Mackay to begin.

Kevin Mackay: Thank you Ryan. Hello everyone and thank you very much for joining us today. With me here in Vancouver is Vince Lok, Teekay Tankers' Chief Financial Officer, and Brian Fortier, Group Controller of Teekay Corporation. During today's call, I will be taking you through Teekay Tankers' third quarter 2014 earnings results presentation, which can be found on our website.

Beginning with our recent highlights on slide 3 of the presentation, Teekay Tankers reported adjusted net income of 3 cents per share in the third quarter compared to an adjusted net loss of 5 cents per share in the same period in the prior year.

Cash available for distribution or CAD was 19 cents per share in the third quarter, up from 10 cents per share in the same period of the prior year. The improved results were primarily due to stronger Suezmax, Aframax and LR2 spot tanker rates earned in the third quarter.

In the third quarter of 2014 the company declared and paid a quarterly dividend of 3 cents per share. Since inception, Teekay Tankers has declared dividends in 28 consecutive quarters, which now totals $7.39-1/2 per share in dividends. Teekay Tankers' dividend is currently fixed at an annual level of 12 cents per share payable quarterly.

In August, Teekay Tankers completed an acquisition of its 50% joint venture interest in Teekay's conventional tanker commercial and technical management operations, which has resulted in Teekay Tankers becoming a more integrated tanker company.

In October, Teekay Tankers secured two new in-charter Aframax tankers at an average rate of $18,000 per day for duration periods of 6 and 33 months, respectively, with options to extend beyond the firm periods. With the addition of these two vessels, our total in-charter fleet grossed ten ships and meaningfully increases our exposure to what we anticipate will be a firming spot tanker market.

In October, as an opportunistic move, Teekay Tankers invested approximately $10 million to acquire additional shares of Tanker Investment Ltd. or TIL, increasing its ownership to 9.3% as TIL's shares continue to trade a significant discount to its net asset value.

Turning to slide 4, I will provide an update on Teekay Tankers' fixed employment mix and our strategic move to actively increase the company's spot market exposure.

Based on our near-term market view that spot tanker rates will, on average, exceed tank charter out rates we've continued to increase the company's spot market exposure through a combination of new in-charter contracts and transitioning some of our owned vessels from fixed-rate employment to spot rate employment as our existing contracts expire.

By utilizing the capital lever of in-chartering third-party vessels, we can increase Teekay Tankers' spot market exposure without increasing our capital investment.

As a result of the ten in-chartered contracts we have entered into so far this year, we have increased Teekay Tankers' spot exposure by approximately 3600 revenue days for the year ahead. On a fleet basis, our spot market exposure for the next 12 months now totals 31 ships or 82% of revenue days. The decision to scale back our fixed-rate cover is based on our view that the tanker market fundamentals will continue to improve.

Looking ahead, we will look to further increase our spot market exposure through additional in-charter and continuing to allow some of our fixed-rate fleet to naturally roll off existing time charters rather than pursue replacement fixed-rate contracts for these vessels.

Based on our expectations the spot tanker market will continue to strengthen. The increase in our spot exposure should translate into increased earnings and cash available for distribution.

As indicated by the blue line in the chart on the right, for every $5000 increase in average spot tanker rates for the 12-month period ending September 30, 2015, CAD per share is expected to increase by 48 cents per share compared to 32 cents per share for the 12-month period that ended September 30, 2014. This increase in earnings power highlights Teekay Tankers' strong operating leverage heading into what we anticipate will be an improving tanker market.

Turning to slide 5, I will discuss recent developments in the crude tanker spot market. As shown in the chart on the left, year-to-date earnings for midsized crude tankers are averaging over $20,000 per day for the first time since 2010.

This is a reflection of tightening fundamentals in the crude tanker market, supported by very low fleet growth, particularly in the midsized tanker segment, coupled with firm growth in ton-mile demand as more oil moves longer haul from the Atlantic to Pacific Basin. We believe that this upward spot rate trend will continue into 2015 as fleet growth is expected to remain low, while oil and tanker demand continues to grow.

Looking at the third quarter of 2014 in isolation, the chart on the right shows that midsized crude tanker rates averaged $9000 per day higher than in the same period of the prior year. This increase was due to a combination of stronger seasonal oil demand in July and August, as well as an increase in long-haul crude tanker movements from the Atlantic to the Pacific as Asian buyers purchased more volumes from West Africa, Brazil and the Caribbean basin.

Rates subsequently weakened toward the end of the third quarter with the onset of seasonal refinery maintenance, but improved once again in October as refinery throughput increased ahead of peak winter demand in the Northern Hemisphere.

Turning to slide 6 I will take a moment to talk about the positive impact that falling oil prices are expected to have in tanker demand in the near term. As the chart illustrates, the price of Brent crude is currently at the lowest point since November 2010 and is 25% lower than levels experienced in the recent peak in July of 2014.

This drop in oil price is largely due to an oversupply of light sweet crude in the Atlantic region driven by the return of Libyan volumes, the continued increase in U.S. shale production, and recent downward revisions to global GDP and oil demand. We believe that these lower oil prices are likely to persist in the near term as OPEC appears ready to maintain current production levels and compete on price by lowering their official selling prices or OSPs.

This is already having an impact on buying patterns with a reduction in Saudi Arabia's official selling price in September, prompting Chinese buyers to purchase 8 million barrels, with a further 20 million barrels of Middle East crude purchased by Chinese buyers in October. These purchases are likely intended for China's strategic petroleum reserve and are incremental to day-to-day demand.

In addition to encouraging imports for stockpiling, lower oil prices can have several other benefits for the tanker market.

First, lower oil prices positively affect tanker earnings by lowering bunker fuel costs. Each $10 drop in oil price equates to a savings of approximately $2400 per day in bunker costs.

Second, arbitrages created by price competition between different oil-producing regions creates volatility in tanker demand and has the potential to alter traditional trade patterns and lead to increased ton-mile demand.

Third, oil prices typically support improved - sorry, lower oil prices typically support improved refining margins, which could lead to higher refinery throughput.

And finally, a steepening of the contango price structure for oil futures, mainly to floating storage, which would help the tanker market by reducing vessel availability in this spot market.

In aggregate, we believe these factors support our expectation that lower oil prices could have a beneficial impact on tanker earnings in the near term.

Turning to slide 7, seasonal factors are also expected to contribute to oil demand increases, resulting in a stronger fourth quarter and winter tanker market.

As the chart on the left illustrates, during the fourth quarter, global oil demand is expected to increase by around 500,000 barrels per day as colder weather in the Northern Hemisphere drives up heating demand. Chinese demand, which is expected to account for approximately 200,000 of those incremental barrels per day in the fourth quarter, could be much higher as China may continue to take advantage of lower oil prices to replenish its strategic petroleum reserve.

In addition, winter weather and transit delays typically support crude tanker rates in the fourth quarter, particularly in December and January which tend to be the peak months for crude tanker rates. Putting together the combined impact of lower oil prices, seasonal stronger oil demand and lower fleet growth, we expect the rates will continue through the course of the fourth quarter and into the early part of 2015.

Turning to slide 8 I'll provide an update on spot earnings for the fourth quarter to date.

Compared to average realized rates for the third quarter, Suezmax, Aframax and LR2 rates for the fourth quarter of 2014 to date have been slightly lower as October fixtures continued the weakness seen in September. By the end of October however, rates have returned to an upward trajectory and continued to strengthen significantly going into the November fixing window.

Also, as the light blue bars on the graph illustrate, fourth quarter rates to date are already higher in 2014 when compared to fourth quarter 2013 actual results.

Increased seasonal demand, as well as winter weather delays should continue to support a strengthening in spot rates, ultimately improving our final fourth quarter earnings across all three vessel segments. To illustrate this, we highlight the red dotted areas on the graph, which represent projected fourth quarter earnings with our bookings to date are extrapolated out using current forward rates for our unfixed portion of the fourth quarter vessel days.

The Teekay Tankers' strong operating leverage and increased spot exposure, continuing strengthening spot rates will translate into a meaningful increase in our earnings, as well as cash flow.

With that, operator, we are now available to take questions.

Operator: Thank you. Ladies and Gentlemen if you would like to ask a question please press star 1 on your touch-tone phone. If you are using a speakerphone please pick up the handset before pressing any keys.

Once again, if you would like to ask a question please press star 1. And our first question comes from the line of Jon Chappell of Evercore ISI. Please go ahead.

Jon Chappell: Thank you. Good morning guys.

Kevin Mackay: Morning.

Jon Chappell: Kevin, I wanted to ask about strategy in light of the TIL investment and the new charter-ins. Is that a commentary at all on vessel acquisitions? Do you feel you'll go in an asset light-type expansion manner at this part of the cycle?

Kevin Mackay: No, I think the acquisition - or the additional acquisition in our shares of TIL was really an opportunistic move based on the fact that TIL shares are trading under net asset value. And we saw it as a way to increase TNK shareholder value by taking advantage of an opportunity.

I think strategically, as I said at Investor Day, "TNK is looking to grow the fleet and we've got several levers at our disposal to do that." You've seen us use the in-chartering lever recently through the summer months, and we'll continue to look at that. But we're also on the lookout and evaluating fleet acquisitions.

Jon Chappell: Okay. And it seems that asset values have tightened or improved, I guess as the market is tightened and improved. Do you feel like asset prices have run away from you yet? And if TIL continues to trade at a discount to NAV, which I believe it still is, would you consider more purchases of entity?

Kevin Mackay: I think looking at asset prices, yes, they've obviously come up from their floor at the beginning of the year but I think there's still room to grow when you - or improve when you compare it with both the 10 and the 15-year average asset prices for second-hand value.

So I don't think it's too late to look at - to M&A. But we'll evaluate all potential acquisitions and investments on an ongoing basis.

Jon Chappell: And any potential more investment in TIL as you see right now?

Kevin Mackay: We will look at TIL as we look at any other investment. And if they continue to trade under net asset value and we have no other uses for cash at that given point in time, we'll make that decision as when we feel it's necessary.

Jon Chappell: Okay. One last one, on page 6 you laid out all the benefits of the oil price, which you know, we've been talking about for the last five weeks. Sometimes it feels like it's in vain. But I guess the only pushback, you know, we get is at some point will OPEC need to cut production to bring the market in the balance and stop chasing the market share?

What's your kind of outlook for OPEC supply decisions? And would it have as much of an impact on the market as it may have five years ago, before we have this abundance of light sweet crude in the Atlantic?

Kevin Mackay: Well I think I wouldn't want to say I know exactly what's going on within the realms of OPEC. But I think the signals that they've have been sending to market, both the Saudis and the Kuwaitis have indicated that at this point in time they want to maintain market share with their customers, and they're going to use price as the tool to do that. Whether they - that is effective in achieving their goals and stems the decision to cut production, we'll have to wait and see.

Jon Chappell: Okay, thanks a lot Kevin.

Kevin Mackay: Thanks Jon.

Operator: Your next question comes from the line of Amit Mehrotra of Deutsche Bank. Please go ahead.

Amit Mehrotra: Yes, thanks very much. In terms of how you think about your fleet strategy, you know clearly Aframax earnings are impressive today and should go higher over the course of the next few months based on, you know, the seasonality that you talked about. But you know, the long-term fundamentals for ton-mile demand clearly benefit, you know, the outlook for sort of larger vessel categories.

And so can you just talk about how you think the company is sort of, you know, operationally positioned for some of the sort of secular demand drivers, as opposed to maybe just more opportunistic seasonally driven improvement?

Kevin Mackay: I think first off the - I wouldn't necessarily agree with you on the Aframax side of the equation. I think Aframax is our regional players and therefore don't necessarily participate in the longer-haul crude movements but...

Amit Mehrotra: But yes, that's what I'm saying, right? I mean essentially, the larger vessel categories are more benefiting from sort of the demand drivers. And so you know, that kind of is what I was alluding to.

Kevin Mackay: Yes. I think what you will see happen is as Suezmax and VLCCs continue to see demand for longer-haul movements as more oil moves from the Atlantic to Pacific, what that does is take out the competition for these regional Aframax movements in the Mediterranean as well as the U.S. Gulf and other areas, which will lead to Aframax improvements on the basis of a lack of segment competition if you will.

Amit Mehrotra: Okay. And just on the product side, you know, we've seen sort of MR rates tick up pretty nicely over the last, you know several months, and can you just sort of talk about, you know, what your outlook is on that side of the market, whether you think sort of the trend will continue to go higher?

Kevin Mackay: The MRs aren't really Teekay Tankers' core business. We have two spot trading assets that we've put into a commercial pool to trade. But I think generally speaking, the MR story will continue to benefit from oil exports or product exports out of the U.S. Gulf heading into Latin America.

And in the short term I think one of the headwinds that you'll see in the MR sector is the new building program that is due to deliver in '14, '15 and into early '16, which could put a cap on their growth and potential earnings.

Amit Mehrotra: Yes. Okay, thanks very much.

Kevin Mackay: Thank you.

Operator: Your next question comes from Michael Webber of Wells Fargo. Please go ahead.

Michael Webber: Hey good morning guys, how are you?

Kevin Mackay: Morning Michael.

Michael Webber: Hey, just a modeling question and then I wanted to talk on the - touch base on the OSPs that you mentioned on slide 6 again.

But with regards to the two most recent charter-ins, I believe the term is 6 months to I think 33, just curious as to what the rate structure is like on those options that are embedded there, whether there's an actual step-up in the rate? And then how long is that option period? Basically trying to figure out how much flexibility you guys have in that embedded tonnage.

Kevin Mackay: Yes, I think the longer one, the 33-month deal, has a 12-month option and the rates pick up I believe to around $21,000 per day. And on the shorter one we have another 6-month option on those and the rates tick up, if I recall rightly, into the $20,000 a day range.

Michael Webber: Got you, that's helpful.

And just to kind of - to piggyback on the earlier question around the lowered OSPs and trading patterns, you know, you mentioned that we continue to see lower OSPs, you're going to see a change in traditional trading - in trading patterns. And then you had mentioned in your remarks that the bulk of the crude kind of moving from the AG to China, they did lower the OSP in September and October.

If you continue to see that happen, can you give a bit more color about what other changes in those trading patterns we could see besides just more crude moving out of the AG East?

And then kind of related to that, you know - well I guess I'll save my thoughts. So maybe just any additional changes in trading patterns related to those OSPs besides just the AG East?

Kevin Mackay: Well, I think the AG East will really - you'll see benefit across both primarily in VLCC movements, but also the Suezmaxes will continue to enjoy the benefits of those trades.

But as you have more of these sort of staying out East to move those barrels, what I think we'll see is a little bit less competition in the Atlantic for the Suezmaxes to benefit from.

Michael Webber: Okay.

Kevin Mackay: And if they pick up West African barrels, we've seen more movements going into the U.S. as the Brent WTI spread has narrowed. I think as that stays down, West African crude remains attractive to U.S. refineries, which will predominantly benefit the Suezmaxes. And as a result, the Aframaxes will have free run to trade in the regions that they benefit from.

Michael Webber: Got you. And then just to kind of follow-up on that and I guess your comments to Jon earlier, and I know you don't want to speak on behalf of OPEC, but you know, we would assume that there's not enough they can do in terms of cutting production to really matter.

So if they don't chase share, then that, kind of that ongoing flow under the AG East and that kind of dynamic should persist for quite a while, the supply command of the market ends up being non-AG based, over the long term, I guess if you kind of look at that dynamic, and we tend to be in agreement with you guys, what sort of longer-term impact do you think that actually has on utilization mix across the fleet?

And then maybe, which asset class do you specifically want to be most heavily weighted towards?

Kevin Mackay: I think when we started looking at longer term, it's a much bigger macroeconomic question in terms of global economic growth...

Michael Webber: Sure.

Kevin Mackay: ...not just based on oil price. But I think as you continue to see the oil price drop and if it stays low for extended periods, I think you've got to look at your higher cost-producing areas, which you know, North American heavy oil production is some of the more expensive production that may get cut, as well as some of these tight oil plays, which to our mind would actually benefit tanker rates even though you see production cuts because you'll have more demand coming to North America to replace those areas that they cut back on.

Michael Webber: Great. All right, thanks guys. Appreciate the time.

Kevin Mackay: Thanks Michael.

Operator: Your next question comes from Shawn Collins of Bank of America. Please go ahead.

Shawn Collins: Thanks. Good morning Kevin.

Kevin Mackay: Good morning.

Shawn Collins: Thanks. You know, there's a lot of talk out there about U.S. shale oil production. You know theoretically, if the U.S. had the ability to export crude -- I know it's impossible to predict, but theoretically -- what new trade patterns do you think might emerge? Can you give us a few examples? And you know net-net, would you imagine this would be a positive?

Kevin Mackay: Yes, I think anytime you have a large producing area like the U.S., exporting oil is going to be positive for tankers because it's - it'll export to further afield. So generally speaking, across all segments I would say that U.S. export - or the U.S. export question would benefit all sectors, not just Aframax in particular.

Although based on the loading constraints, I think the immediate beneficiary would be Aframaxes because of the shallow draft restrictions you get in the U.S. Gulf. But that could translate into reverse lightering opportunities onto Suezmaxes or VLCCs. So I think as I said, "It could be beneficial across all segments."

I think as you look further afield, if U.S. crude exports do get approved in a large way, I think by the time we get to that decision point we're looking at Panama Canal being an opportunity that could benefit movements towards Asia. You can get a fully laden Aframax and a light loaded Suezmax through the Panama Canal by 2016 so that will make a more attractive option to go East.

I think Europe would also be a beneficiary of light sweet as an alternative to buying West African barrels.

Shawn Collins: Okay great, that's helpful. Thank you. And then you know, a second question. You know, with the recent lower, dramatically lower oil prices and the resulting new arbitrage activity, can you talk about a few of the new trading patterns that you've observed or participated in?

Kevin Mackay: Yes, I think we've seen a fair amount of stockpiling as one of the benefits of that arbitrage. Traders have moved a fair amount of barrels from West Africa into Soldotna Bay for onshore storage in South Africa. We're seeing cross movement of barrels going from West Africa - sorry, into the U.S. Gulf, into the U.S.A. sea, which we hadn't seen for a long period of time.

But there's various developments we're seeing globally that's benefiting from the drop in price.

Shawn Collins: Okay great. Well that's great, that's helpful. Thank you very much Kevin, I appreciate it.

Kevin Mackay: Thanks Shawn.

Operator: Once again Ladies and Gentlemen, if you would like to ask a question please press star 1 on your touch-tone phone. And your next question comes from the line of John Reardon of Merriman Capital. Please go ahead.

John Reardon: Hi, good day, and great quarter. I have a question about the dividend.

I've been a TNK person for a while now. And Vince, you'll probably remember in the old days, the dividend was variable based on the quarterly performance. And then when we kind of went into the Death Valley days, it was decided to cut it to a more regular rate. And now things are picking up again.

Is there any thought - and I noticed you kind of made a mention about 19 cents and distribute of cash flow, up from 10 cents or so a year ago. Is there any thoughts that in a couple of quarters we might go back to a performance-based dividend? That's question Number 1.

Question Number 2 is, correct me if I'm wrong, but it seems that some of the European banks that have a lot of shipping loans have been playing extend and pretend. And a lot of the companies out there that, they loan the money to aren't as say, in the same shape you folks are.

And are you noticing that you're picking up some business by customers who don't want to run the risk of having their cargoes tied up in some kind of maritime legal proceeding because some financial institution is seizing somebody's equipment? That's my second question, and thank you.

Vince Lok: Okay. Well I guess first on the dividend, we made a strategic decision a couple years ago, as you know, to go to a fixed dividend of 12 cents per annum. And we did it mainly because we felt that it was better for us to retain additional operating cash flow to reinvest into the - what we expect to be a stronger tanker market.

And that's turning out to be the case right now. So the additional cash flow that we're generating in the near-term is being used to reduce debt and further strengthen our balance sheet, which in turn allows us to reinvest into the stronger market.

So in short, in the near term we don't have any plans to change our dividend policy. And I don't think - I think TNK isn't really trading on the basis of a dividend yield any more, it's more of - based on our earnings power and a play on the recovery of the tanker market.

But of course longer-term, that is something we obviously will revisit in the longer-term. Should we be in a position where we have excess cash flow, then of course we'll look at ways of - what's the best use of that capital at that time.

Kevin Mackay: Yes, I think taking your second question John, I think with regards to European banks, where the biggest exposure is for a lot of those banks is primarily in the container sector where they, mainly the German banks, have gone extremely long and have been caught out in that business.

On the tankers side, we haven't seen an awful lot of distressed assets being shown. There are one or two out there, but nothing significant in terms of - on a fleet basis.

But to your sort of Part B of your second question around, "How do customers view that sort of operational risk," not to mention the credit risk, having just recently been a customer, I know that the oil companies look very, very seriously at their operational exposure when dealing with companies that have questionable financial solvency and backing.

So it's an opportunity really for companies like TNK, who have got 40 years of strong customer relationships and trust, that we maintain a strong balance sheet, we operate good quality assets that don't cause operational problems. It gives us an advantage, and we can grow our business and our relationships on that basis with those companies.

John Reardon: Thank you.

Kevin Mackay: Thanks for the questions.

Operator: And there are no further questions at this time. I would like to turn the call back over to Mr. Mackay for closing remarks.

Kevin Mackay: Well thank you very much for joining us today and hope you all have a good festive season as Christmas approaches. Thanks 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.

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