



TEEKAY OFFSHORE PARTNERS L.P.

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Moderator: Emily Yee
February 21, 2014
11:00 am CT

Operator: Welcome to Teekay Offshore Partners Fourth Quarter and Fiscal 2013 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. Peter Evensen, Teekay Offshore Partners Chief Executive Officer.

Please go ahead, sir.

Ryan Hamilton: Before Mr. Evensen begins, I'd like to direct all participants to our website at www.teekayoffshore.com, where you'll find a copy of the fourth quarter and fiscal 2013 earnings presentation. Mr. Evensen 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 fourth quarter and fiscal 2013 earnings release and earnings presentation available on our website.

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

Peter Evensen: Thank you, Ryan. Good morning, everyone, and thank you for joining us on our Fourth Quarter and Fiscal 2013 Investor Conference Call. I'm joined today by Teekay Corporation's CFO, Vince Lok, Chief Strategy Officer, Kenneth Hvid and MLP Controller, David Wong. During our call today, I'll be walking through the fourth quarter and fiscal 2013 earnings presentation, which can be found on our website.

Starting on Slide Number 3 of the presentation, I will briefly review some of Teekay Offshore's recent highlights. The partnership generated distributable cash flow of \$57.4 million in the fourth quarter, a 25% increase from the same quarter of the prior year, primarily due to the acquisitions of 2 FPSO units, delivery of 4 newbuilding shuttle tankers and stronger performance in our Shuttle Tanker segment.

We declared a cash distribution of \$0.5384 per unit for the fourth quarter, which is an increase of 2.5% over the previous quarter's distribution payout, bringing the partnership's total distribution increase for 2013 to 5%, in line with previous guidance.

An exciting new development today, we agreed to acquire ALP Maritime Services, a provider of long-haul ocean towage and offshore installation services to the global offshore oil and gas industry. And, we ordered four long-haul towing and anchor handling vessel newbuildings, which I will discuss in more detail later.

In November, we took delivery of the Sertanejo Spirit, the fourth and final newbuilding shuttle tanker that will operate under a 10-year contract with BG Group in Brazil. The vessel commenced this contract in early January, following a repositioning voyage from South Korea to Brazil.

During the fourth quarter, the Voyageur Spirit FPSO averaged 93.4% of its full rate from the charterer with the remaining charter hire covered by Teekay Corporation's indemnification. We're still awaiting the certificate of final acceptance from the charterer, which is subject to us completing certain operational production tests.

The commencement of these tests has been delayed due to bad weather in the North Sea this winter and charterer-specific operational issues on the oilfield. However, we hope to complete the operational tests over the next couple of weeks.

As I will discuss later, we have now also signed a new shuttle tanker contract of affreightment, or CoA, to service the oil offtake needs of the Knarr FPSO.

We expect 2014 will be another busy year for Teekay Offshore, as we've laid out on Slide Number 4. The partnership's Remora HiLoad unit arrived in Brazil in November and is currently undergoing technical testing. We expect this innovative DP unit will commence its 10-year charter with Petrobras in the second quarter of 2014.

The Salamander FSO conversion is progressing well, and we anticipate this converted shuttle tanker will commence its FSO charter with Salamander Energy in Thailand in the third quarter of 2014. And while the conversion work on the Gina Krog FSO must wait until the existing shuttle tanker contract expires, planning for this project is well underway, and we expect the conversion work for this FSO to commence in 2015.

And while not directly a Teekay Offshore project, construction of the Knarr FPSO newbuilding, which is owned by our sponsor Teekay Corporation, is progressing well. In addition to these organic growth projects, our sponsor also owns four other FPSOs, pictured at the bottom of this slide that may be offered to us over the next few years as their contracts are amended to suit our acquisition criteria.

Turning to Slide Number 5. I'll provide a brief update on the Petrojarl Knarr FPSO newbuilding, Teekay Corporation's largest FPSO project to date. Construction on the unit is progressing well.

And, and I'm pleased to report that Teekay Corporation recently finalized the new \$815 million long-term debt facility, which includes a combination of Korean and Norwegian export credit agencies and commercial debt financing at attractive terms. This financing facility is transferable and would be included in the dropdown sale of the Knarr FPSO to Teekay Offshore.

The unit is scheduled to sail away from the shipyard in South Korea for the Knarr oil and gas field in the North Sea in early third quarter of 2014. Following installation on the oilfield and offshore testing, the unit is expected to commence its ten-year charter with BG Group in the fourth quarter of 2014, at which point, the unit will be eligible for sale to Teekay Offshore under the existing Omnibus Agreement.

In addition to the Knarr FPSO contract, in December 2013, Teekay Offshore was also awarded a six-year shuttle tanker contract plus extension options with BG Group to provide oil transportation services for the Knarr oil and gas fields. This is a great example of Teekay Offshore's ability to bundle services for its customers.

Turning to Slide Number 6. I'd like to take a moment to discuss our acquisition of ALP Maritime Services. As highlighted in my opening remarks, we announced today that we had agreed to acquire ALP Maritime Services, or ALP, a Rotterdam-based provider of ocean towage and

offshore installation services. ALP currently serves its customers using a fleet of third-party-owned vessels.

As part of the transaction, we ordered 4 state-of-the-art Ulstein X-Box Design long-distance towing and anchor handling vessel newbuildings from Niigata Shipbuilding & Repair Shipyard of Japan, which will be capable of long-haul distance towing, offshore installation and decommissioning of large FPSO, FLNG and floating drill rigs.

These state-of-the-art newbuildings are based on the new ALP design, which incorporates more powerful engines and dynamic positioning capabilities. And they provide ALP with a competitive advantage. The total cost to acquire ALP and order the newbuilding vessels is approximately \$260 million.

The partnership expects to initially finance the acquisition cost and initial shipyard installation payments using our existing liquidity. And, we plan to secure long-term debt financing prior to the vessel deliveries in 2016.

The global build out of the offshore oil and gas industry, combined with a large order book of large floating offshore assets, including FPSOs, FLNGs and floating drilling rigs, is expected to result in strong demand for the services of long haul towing and anchor handling vessels.

In addition, the towing and offshore installation market has attractive cash flow visibility with new projects often booked at least 2 years in advance. We believe ALP's operational capabilities and customer relationships in this growing market segment provides a natural complement to Teekay Offshore's existing offshore project offering and will provide the partnership with another channel for accretive cash flow growth.

Turning to Slide Number 7. Future demand for FPSOs is expected to remain strong. The chart on the top left of the slide shows historic FPSO contract awards, along with a forecast out to 2018 from Energy Maritime Associates. According to the forecast, between 13 and 18 FPSO contracts are expected to be awarded every year for the next five years.

Over half of these orders are expected to be for leased units, like those owned by Teekay Offshore, as opposed to units directly owned by the field operator. This new demand is expected to be met by a combination of newbuildings, conversions and redeployment of existing units, though there is an increasing trend for some operators toward a desire for newbuildings, as opposed to the conversion of older tankers.

We continue to see strong demand for FPSOs worldwide, and we believe we're in a strong position to compete, particularly in our core markets in the North Sea and Brazil. Brazil continues to be mostly Petrobras-sponsored projects. But, we expect an increasing number of international oil companies to develop FPSO projects in Brazil going forward.

The FPSO market in the North Sea is quite different, with a number of field developments being medium-term contracts. We believe this leaves TOO in a strong position to compete with existing FPSOs that have already been built for the stringent North Sea environment.

On Slide Number 8, I'll review our consolidated operating results for the quarter, comparing an adjusted fourth quarter 2013 income statement with an adjusted third quarter 2013 income statement, which excludes the items, which we list in Appendix A of our fourth quarter earnings release and reallocates realized gains and losses from derivatives to their respective income statement line.

Starting at the top of the income statement. Net revenues increased by \$24 million, mainly due to Voyageur Spirit FPSO on hire for the full quarter and higher shuttle fleet revenues from the

commencement of the charter contracts on two of the BG shuttle tankers, as well as higher utilization of the existing shuttle tanker fleet.

While our revenues increased by \$11 million associated with the Voyageur Spirit FPSO. Distributable cash flow remains consistent with the prior quarter for this asset given the indemnity with Teekay Corporation for any shortfalls.

Vessel operating expenses increased by \$1.1 million, primarily from cost increases related to the timing, and repair and maintenance for the shuttle tanker fleet and the delivery of the BG shuttle tanker newbuildings. Partially offset by a decrease in the repair and maintenance cost for our FPSO fleet.

The partnership's distributable cash flow also benefited this quarter by a \$3.6 million reimbursement from Teekay Corporation for repair costs related to the Voyageur Spirit FPSO. Time charter hire expenses decreased by \$500,000, mainly due to the redelivery of one of our in-charter vessels to its owner. Depreciation and amortization expense increased by \$400,000, mainly due to the delivery of the last BG shuttle tanker newbuilding.

G&A expense decreased by \$600,000, mainly due to timing differences. Net interest expense, including realized losses on interest rate swaps, increased by \$2.4 million, mainly due to the delivery of the final 2 BG shuttle tanker newbuildings. And, equity income increased by \$1.5 million, relating to lower vessel operating expenses on our 50% owned investment in the Itajai FPSO.

I won't walk through all of Slide Number 9, which was included in our recent earnings release. However, I would like to highlight the information in the box at the bottom of the slide.

We generated approximately \$57.4 million in distributable cash flow, which when compared to our total distribution payout, resulted in a coverage ratio of 1.13x for the fourth quarter, which is up significantly from the 0.90 generated last quarter and more in line with where we would like to see our coverage ratio in the future.

On Slide Number 10, we summarize our high-level growth plan for 2014. First, we will continue to execute on the existing organic growth projects such as the Salamander and Gina Krog FSO projects, while at the same time working to secure new growth projects and contract extensions.

Second, Teekay Offshore also intends to grow through FPSO acquisition opportunities, which are provided by our sponsor, likely commencing with an offer to acquire a portion of the Knarr FPSO later this year. And, over time potentially acquiring the four remaining FPSOs owned by our sponsor.

Lastly, we will also continue to seek out accretive third-party acquisitions like the acquisition of the Remora HiLoad DP unit, the Sevan FPSO unit a couple of years ago and today's announcement on ALP. These accretive acquisitions are strategically important for Teekay Offshore because they provide us with additional capabilities that we can use to support our customers as part of the continued global build out of offshore energy.

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

Operator: Thank you. If you would like to ask a question, please signal by pressing the star key followed by the digit one 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.

If you have signaled for a question prior to hearing these instructions on today's call, please repeat the process now by pressing star 1 again, to ensure our equipment has captured your signal.

Our first question comes from Michael Webber with Wells Fargo Securities. Please go ahead.

Male: Hi, Peter, this is ((inaudible)) on again for Michael.

Peter Evensen: Fine.

Male: Hello?

Peter Evensen: Yes, hi, can you hear me?

Male: I can hear you. Okay, so my first question is really on the ALP acquisition, which you guys announced for today. Obviously, my understanding of the cash flow visibility of ALP is that projects are booked one or two years in advance. So, assuming an acquisition price of around 260 million, how can we think more about the potential for accretion in earnings, from that acquisition?

Peter Evensen: We're not ready to give guidance on that, but in our opinion, this is going to be accretive because the margins in this business are higher than what we've seen in some of our traditional units.

Male: Got it. And kind of switching gears then to the Knarr. Obviously, the Knarr is owned by Teekay Corporation, but I think you mentioned earlier on the call that the \$815 million of debt, which was received this quarter, would be transferable to Teekay Offshore in the event of a dropdown.

So, in terms of leverage, how should we think about the leverage levels on the Knarr? Is there a potential for additional debt in the event of a dropdown? Or is that kind of like the maximum leverage you see on the Knarr?

Peter Evensen: That's the maximum leverage that we'd put on the Knarr. We generally try to hold down to a 4 to 4-1/2x debt to EBITDA. So while you can put more debt when you have a long-term contract, like we have the Knarr, we tend to want to run with lower debt levels. So, although that isn't as accretive as it could be, that's part of our long-term sustainability that we look at for our partnership.

Male: Got it. Got it. And 4 to 4-1/2x in debt to EBITDA, and in terms of percentage leverage, that would be around, say, 60% to 70%?

Peter Evensen: Yes. And so obviously, we can finance it at a higher debt level since it's a billion dollar FPSO. And so, we can finance it close to 80%. But, that's not how we run the partnership. We try to run it with a lower debt level.

Male: Got it.

Peter Evensen: But we always take the maximum amount of debt available.

Male: Got it. Makes sense. Switching to the post Knarr period at Teekay Offshore. I know from previous calls and you guys have emphasized, the organic projects going on right now, whether it would be FPSOs in Brazil or the North Sea or even beyond that, could you give us an update in terms of any potential project you guys may be kind of pursuing? And anything with kind of -- any kind of potential updates on FPSOs organically?

Peter Evensen: You mean on new projects that aren't new FPSO projects.

Male: New organic FPSO projects.

Peter Evensen: Yes. Well, we're working on projects in the North Sea and Brazil. I can tell you we were unsuccessful in getting the Catcher FPSO. But, we're looking at other opportunities in the North Sea. And there are some new projects that have been announced in the Trade Press as it relates to Brazil. And, we're working on those as well.

Male: Got it. And in terms of the size of those projects, I think previously you mentioned \$3 billion of organic FPSO growth. Is that still kind of a good number to think of? Or has that number changed?

Peter Evensen: No, that's a good number to think about. I mean, the FPSOs cost anywhere from \$600 million to \$700 million up to over -- well, actually, up to \$1.5 billion. So, we generally work on two or three projects at any one time on the FPSO side. But, as you see, we're also working on -- so that's on the FPSO side.

But, I'd like to emphasize that we're also working on shuttle tankers, working on FSOs. Now we have the deep-sea towage. So, we're going to have to expand our slide to talk about more than just the FPSOs going in future earnings releases. So, what I like is that we have a whole bunch of different channels for growth. We have dedicated business development teams. So, it isn't like you're taking people off of other deals.

And, so that's where I think our partnership has matured, that we have multiple channels in order to find good projects for growth. And, the fact that we have -- that people located in Brazil and Norway and now in Rotterdam, I think is only going to add to our ability to find good quality projects. So that, you're bidding on the projects that you really want to do.

Male: Got it. And, the final question on that thought. We noticed that Sevan basically has two floating accommodation units, which are currently being constructed, one of which is on charter to Petrobras for three years. How would you guys kind of think about that in terms of the potential fit with Teekay Offshore?

Peter Evensen: Yes. So, this is for everyone else. Our sponsor, Teekay Corporation, owns a 42%, 43% ownership in Sevan, and we have an agreement with Sevan that they will offer any long-term projects to Teekay Offshore. And so, the accommodation unit that they're building in China, certainly, are part of that discussion.

So, that could be a new area of growth for Teekay Offshore. And, one of those -- so these are floatels or floating accommodation units, which are going to be increasingly used in Brazil. And, the first one of these does have a three-year contract. So, that certainly does fit within TOO's type of cash flows that they want. It's initially three years, and they have an option for, I believe, another three years. So, that might be another area of growth, yes.

Male: Got it. I think that's pretty much it on mine. Thanks for taking my questions. I'll turn it over.

Operator: Thank you. Our next question comes from Gabe Moreen with Bank of America Merrill Lynch.
Please go ahead.

Derek Walker: Hi, this is Derek Walker on behalf of Gabe Moreen. Just going back on the ALP transaction. Can you just discuss a little bit more about the opportunity set here for this new business? Do you see most of it being around FPSOs? Or, you know, how are you looking at the LNG and drilling rig opportunities?

Peter Evensen: Sure. Well, what we're seeing is that the type of units that are being produced are just bigger. And, in particular, if you look at FLNG side, like the Prelude that Shell has ordered, that's

500 meters long. So, you actually need bigger ships in order to do deep-sea towage of those units.

Those aren't units that can be part of a dry tow, which -- where you use heavy lift ships. And so, we had noticed this market. Obviously, the Knarr has to be done on a wet tow basis. And so, these new units are, in our opinion, safer than some of the existing ways that people execute wet tows. But, they also have a lot of, what I would call, good features that are going to make them attractive to that customer set.

But, what we really like about this acquisition is the management team that has come on board. These guys that -- we've gotten to know them over several months. And, we really think, just as we have with our other units that do FPSOs and shuttle tankers, we really do think that they have great customer relationships and they have great operational experience.

And, that's what's going into the design. So, they've been doing business with in-chartering other ships. And, so we feel that if we give them this better equipment, which we can add value to and ultimately be part of the operations on, then I think that we'll have a winning combination. But, we didn't have the skill sets and their customer relationship and their operational know how. So, to bring that within the Teekay Offshore family, that was as important as just the equipment.

Derek Walker: Got it. Appreciate the color there. And, can you just discuss a little bit more about the -- I know you said the total transaction cost was around 260. What's the breakup there between the third-party business of just ALP? And, then how much of that is the newbuildings?

Peter Evensen: Yes. We're not saying exactly how much was the business and how much was the newbuildings. But, the vast amount of it was for the newbuildings.

Derek Walker: Got it. And, then I know you briefly talked about the margins there. Obviously, there's a wide variety of services that ALP provides. Can you just talk about the contract structure? Are they all fee-based? And, how does that vary across different types of services?

Peter Evensen: Yes. So obviously, when you're going to deliver a big offshore unit or a gas unit or even a topside, that's going to go on a flat barge, you need to reserve that space a year and a half, two years in advance. So, they will give a slot requirement or reserve a slot. And, then what's great about these guys is sometimes units don't deliver on time or not, and then they can slot in and move it around.

And, that ability to give that flexibility to customers, let's say a unit comes a little early or comes two or three months late, that's a key part of the customer service offering that they have. And so, by having a critical mass of four units and being able to supplement it by chartering in other units, that's part of the value-added that they give to customers.

And so that -- but for us, that's important because we get to see that visibility, which is part of what is attractive. We're always looking for businesses where you can see the contract visibility a year, year and a half out, as we do our FPSOs that are on contract or our shuttle tankers. And so, this means that we can gate the business.

And so, we're starting with four, but we could easily grow this as the amount of business increases. But, it isn't just the DC towage. There's going to be a bigger market for plug and abandon, as well as installation of these units. So, they cannot only engage in the towage of it, but once they're there, they can help hook up the unit. And so again, you're going to need bigger support vessels in order to make that happen efficiently.

Derek Walker: Got it. And, I appreciate the insight there and thank you for taking my questions.

Operator: Thank you. Ladies and gentlemen, as a reminder, if you would like to ask a question, please press star 1 touch-tone phone.

Our next question comes from Chris Combe with JPMorgan. Please go ahead.

Nishant Mani: Hey, good morning guys. This is Nish Mani on for Chris. Just a quick follow-up question on the ALP acquisition, I know you guys don't want to specifically comment on charter and developments specific to the acquisition. But, can you kind of give us a sense of where unlevered returns might sit in this sub segment relative to perhaps the FPSO and shuttle tanker segments that you guys operate in?

Peter Evensen: I'll just say that it's higher. That's what I'll say. You have -- you don't always have 100% utilization as we have on our shuttle tankers and FPSOs. But the raw margins are higher. So the key is to make sure that your -- that the utilization between contracts is minimized. And that's where I think our management team really excels going forward.

Nishant Mani: Okay. And then, typically, the structure of the contracts is over -- is it, generally speaking, individual transport and project-based? Or is it span or a horizon of time similar to time charter?

Peter Evensen: It's individual project-based. And so, it's the ability to -- just as with our shuttles where you have to book out, it's a question of combining projects in order to have the best utilization.

Nishant Mani: Okay. I want to turn to growth in the medium term. I mean, it looks like with the Knarr kind of 2014, as well as the Salamander and a couple of other smaller projects, 2014 will certainly be a busy year of integration of new assets. And, looking beyond in 2016 and 2017, we have additional scope for both FPSO growth as well as the ALP transaction.

But, kind of looking at 2015, you know, 12 months ahead, there seems to be a bit of lag in terms of growth. So I kind of wanted to ask you guys about the projects, the FPSO projects, you have at Teekay Corp. and if any developments have been made, for example, on the Hummingbird or Foinaven, such that you could execute growth on a faster timeline than through an organic FPSO project.

Peter Evensen: Yes, so when we look at 2014, we don't -- we're comfortable with the existing projects that we have, the Remora and the Salamander. But, Petrojarl Knarr, from a distribution growth, is really a 2015 event, because it's coming in, in the fourth quarter. So, we see most of that providing the distribution growth to 2015.

And, then as you said, we have ALP coming in 2016. And, the FPSO -- the new FPSO projects that we're targeting are beyond 2017. But, in between that, I expect you will see a dropdown of some of the existing four FPSOs that we have upstairs, that we had at the bottom of Slide 4. So, that's an additional way that we can grow. So, I'm confident in our ability to consistently grow the distribution at Teekay Offshore.

Nishant Mani: Are you able to comment specifically on which of the four projects is most likely or most apt for a drop in 2015?

Peter Evensen: Well, each one is a little different. Both the Hummingbird and the Foinaven, we're talking with the charterers on the contracts that are going forward. So, assuming we're successful there, then they would become eligible. The Petrojarl Banff is returning. And, as we've said, that contract as per the existing terms gets better post 2015. So then, the Banff becomes eligible. The Banff is on a breakeven contract now. So there's no sense in acquiring it.

But, post January 1, 2015, then that contract gets better. And then, that one we have permission to drop down. And, the Petrojarl I, we need to find a new contract for before that could be

dropped down. So, I can't give you a runway. But, I can tell you that Teekay Corporation, the management there is committed toward moving toward being fixed asset light, which involves selling the ships down to Teekay Offshore with the appropriate contract.

Nishant Mani: Okay. And then, you know, to the end of distribution growth, you know, this year was -- or this past year was excellent in terms of distribution growth. In kind of 2014 and 2015, do you guys have a kind of minimum threshold that you'd like to hit in terms of PPU growth or are you very kind of opportunistic here and open to...

Peter Evensen: No, we have a track record of consistently growing the distribution every year. And, we are a conservative bunch of guys. We don't give specific guidance. But, I think we have a good track record of growing it. And that's a combination of organic growth, dropdown sales from the sponsor as well as acquisitions like we announced today on ALP.

So, I mean, given that we're in so many different fields, shuttle tankers, floating storage, FPSOs, deep-sea towage, and as I said on one of the previous calls as well, possibly accommodation, I feel really good about our ability to grow.

The question is to find the best projects, not just any projects, but the best projects. And, we have the option to acquire these units. And, we're just pretty methodical. I know that's not sexy, but we're just methodical in how we're going about our business.

Nishant Mani: That's very helpful. Thank you so much for your time guys.

Operator: Thank you. And, there are no further questions at this time. Mr. Evensen, please continue.

Peter Evensen: Okay. I'm going to take the no further questions as being that everyone's watching the U.S./Canada hockey game. So thank you very much. Bye.

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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