TEEKAY LNG PARTNERS L.P.

Moderator: Peter Evensen
May 18, 2012
9:00 am CT

Operator: Welcome to Teekay LNG Partners' First Quarter 2012 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 one 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 LNG Partners' Chief Executive Officer. Please go ahead, sir.

David Rajanayagam: Before Mr. Evensen begins; I would like to direct all participants to our website at www.teekaylng.com, where you will find a copy of the third – of the first quarter of 2012 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 first quarter of 2012 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, Dave. Good morning everyone and thank you for joining us on our first quarter 2012 investor conference call.

I am joined by Teekay Corporation's CFO, Vince Lok; Chief Strategy Officer, Kenneth Hvid; and MLP Controller, David Wong.

We will try to keep this call short as we reported our fourth quarter 2011 results less than 12 weeks ago, and we will be giving you a comprehensive presentation in mid-June at our biannual investor event, which I will provide further details on at the end of today's presentation.

Turning to slide number 3 of the presentation, I will briefly review some recent highlights. The Partnership generated distributable cash flow of $50.8 million in the first quarter of 2012, up 30 percent from the same quarter last year, when we generated $39.1 million. The year-over-year increase highlights the growth our fleet has experienced over the past year, including recent deliveries of our newbuilding gas carriers, and our accretive acquisition in February 2012 of a 52 percent interest in six LNG carriers. Together with our joint venture partner Marubeni Corporation, we have now completed the acquisition of Maersk LNG fleet of six LNG carriers.

Based on the cash flow from this acquisition and the recently delivered newbuilding, we increased the quarterly distribution by 7 percent, to 0.675 cents per unit. And lastly, we issued a Norwegian bond. We raised NOK700 million, equivalent to $125 million on an unsecured basis for five years, and swapped the proceeds into U.S. dollar fixed rate at 6.875 percent. While we have no immediate use for the proceeds of the bond issue, our current liquidity balance is approximately $440 million, which we believe is a competitive advantage, as we can respond more quickly to third-party acquisition opportunities.

Turning to slide number 4, I will briefly walk through the state of the LNG market. Following the devastating earthquake in Japan in March 2011, Japan's LNG imports are up 24 percent year on year in the first quarter of 2012. Currently, all of Japan's nuclear reactors are off-line, which is one of the factors driving LNG tanker ton mile demand, and explains the backward-dated structure of spot LNG shipping rates, whereby spot rates are approximately $140,000 per day, and are higher than the medium-term charters, which we estimate to be in the neighborhood of $80,000 to $90,000 per day. We expect that the fundamental outlook for spot LNG shipping markets will remain firm in the near term, based on strong growth in LNG demand relative to the current fleet growth.

While the situation in Japan may or may not be a recurring factor, we are seeing increasing signs of development in the long-haul LNG trade. For example, in early April of this year, FERC authorized the construction and operation of a large LNG export facility in Louisiana. The 16 million ton per annum plant, which is scheduled to commence operations in 2015, is the first of its size in the United States, and the majority of its exports are expected to be shipped out long haul to Asian destinations. There are presently 22 potential LNG export projects being discussed in North America. And whilst we know that they will not all be sanctioned, it is one of the many strong indicators that fundamentally supports our bullish view of LNG shipping in the future.

Our LNG business continues to be well positioned to benefit from both the short- and longer-term fundamental strength in the LNG market. In January, we took delivery of our last Angola LNG carrier, completing our latest newbuilding program, and freeing up capacity to undertake new projects as they arise. We have one of the carriers that will be coming off charter later in 2013, and we are already in active dialogue with a number of potential customers today about chartering the ship next year to take advantage of the strong short- to medium-term rate environment. And we continue to actively monitor the market for upcoming tender and acquisition opportunities, looking for growth opportunities that will allow us to develop new accretive growth projects for Teekay LNG Partners. Recently, we've seen a pickup in tendering activity, as a result of the strong fundamentals in this space.

Turning to slide number five, I will review our consolidated operating results for the quarter, comparing an adjusted Q1 income statement against an adjusted Q4 2011 income statement, which excludes the items listed in Appendix A of our earnings release, and reallocates realized gains and losses from derivatives to their respective income state line item. Net voyage revenues increased by $1.7 million, primarily as a result of having no off-hire days this quarter, compared to 37 off-hire days in Q4. Vessel operating expenses decreased by $2 million, primarily due to lower service and maintenance costs incurred in Q1, and lower crew manning due to foreign exchange differences.

Depreciation and amortization remained relatively consistent from Q4. General and administrative expenses increased by $1.7 million, as a result of the growth in our fleet. And effective January 2012 all gas related business development costs are now being allocated to our Partnership on a quarterly basis, whereas before such costs were incurred in the form of success fees paid by – paid to Teekay Corporation, in connection with acquisitions.

Net interest expense was essentially in line with the prior quarter. Equity income increased by $3.4 million, primarily as a result of one month of income from our 52 percent interest in six LNG carriers which were acquired from Maersk on February 28, and equity income from our 33 percent interest in the third and fourth Angolan LNG vessels which delivered in late October 2011 and mid-January 2012. Non-controlling interests remained relatively consistent from Q4.

I won't walk through all of slide number six, which was included as an appendix to our recent earnings release. However, I would like to point out that our coverage ratio of 1.03 for the first quarter comes in slightly lower than our targeted 1.05 coverage, primarily due to the timing of our recent distribution increase, while we had only the cash flow from the Maersk acquisition for one month in the first quarter.

As a result, all other things being equal, we would expect our coverage ratio in Q2 to increase, since we will have a full quarter contribution from the Maersk LNG vessels, and one of the vessels in the JV, the Methane Spirit, commenced a new charter in April, at a much higher rate of over $130,000 per day.

I would also like to point out the figure in the red circle. Due to the large number of ships we own jointly with our partners, the distributable cash flow from these equity investments is increasing. However, under GAAP, this cash flow is not reflected in our consolidated revenues, or cash flow from vessel operations, because they are equity accounted for.

As you can see, the distributable cash flow from these equity accounted JVs has more than doubled since the first quarter of 2011, and will increase further next quarter when we have the full quarter contribution from the Maersk LNG acquisition.

Turning to – Teekay LNG Partners continues to be in a relatively strong financial position, with approximately $440 million in liquidity currently, adjusting for the completion of the Norwegian bond in early May. We have no covenant concerns on any of our debt facilities. Our current debt maturity profile is favorable, and our next significant debt maturity isn't until 2015.

As I mentioned at the beginning of the call, slide number eight, includes details of our upcoming investor event to be held in New York City on Monday, June 18 at the Waldorf Astoria. If you are unable to make it New York to join us in person, the presentation will be web cast on our website, www.teekaylng.com.

Operator, I am now available to take questions.

Operator: Thank you. Ladies and gentlemen, if you'd like to ask a question, press star one on your touch-tone phone. To withdraw your question, press the pound sign. If you use a speakerphone, lift your handset before entering your request. We will pause for a moment to assemble the queue.

The first question comes from Darren Horowitz of Raymond James. Please go ahead.

Darren Horowitz: Good morning, Peter.

Peter Evensen: Good morning.

Darren Horowitz: The first question, regarding that one LNG vessel that you discussed that is going to be available for re-charter in 2013, how do you think about balancing the rate versus the new contract term, given the backwardation in the forward market that you discussed?

Peter Evensen: Well, we're – we have approximately 15 months to make a decision on that. And on the previous one, we chose to go with a shorter charter of over $130,000 for three years. And that was significant, because that was $40,000 to $50,000 a day, and we got half of that cash flow. So I think we will have to look at it. But right now, I would say we'll have to see what the charters come in with, but I actually won't be drawn on that.

Darren Horowitz: Okay. From a bigger picture perspective, and this kind of dovetails with a lot of which you discussed around slide 4, how do you think about, and possibly if you could quantify that would be helpful, the strong growth that you expect in LNG demand, relative to fleet growth? Obviously, recognizing that they are not going to be linear, it's going to be lumpy in nature. But if you could just kind of give us some additional color on both of those two aspects that would be helpful.

Peter Evensen: Sure. Well, I think it's two different markets, to be honest with you. The market up until 2015 relies upon the Fukushima effect, which is extended ton-mile demand. Vessels that would have been in the Atlantic Ocean are, when they can, going out to the Pacific with extra LNG cargoes, and that's generating a lot of extra ton-mile demand. But going up till 2015, there aren't that many new LNG projects coming on line, and therefore, there isn't new gas to take the place of the 34 uncommitted vessels that will deliver between now and 2015. That is to say, in 2013 and 2014.

So we have about 76 new builds, of which 34 are uncommitted. So we could see a softening, which is what I think you see this backward-dated rate structure in the LNG spot market rate. But looking forward beyond 2015, you have Australia coming in, you have the U.S., and whether – and most projects we're assuming come in a year late than what they say, just because that's been our experience over the last few years – most recently in Angola, which is coming in about nine months late.

And so, we think that you'll get lot of extra LNG cargoes coming in 2015, whereas you're getting ton-mile demand effect up until 2015.

Darren Horowitz: Beyond that 2015 time frame, how long do you think it will take, from a supply/demand perspective to where the market ultimately becomes balanced, in terms of all those new vessels coming in, and possibly rates stabilize? I mean is it a situation where it's going take you think two to three years or possibly even longer?

Peter Evensen: No, I actually see that there is enough demand coming in 2015 that it could soak up the existing order book that we have.

Darren Horowitz: Okay. Thanks.

Peter Evensen: That's why we are relatively bullish.

Darren Horowitz: Yes, I appreciate the color. Thank you, Peter.

Peter Evensen: Thank you.

Operator: Thank you. Ladies and gentlemen, if there are any additional questions, please press star one at this time.

The next question comes from Ron Londe of Wells Fargo. Please go ahead.

Ron Londe: Thanks Peter. I get a lot of questions of late concerning the economic outlook in Europe and how that might affect the LNG market. I know that you have ship or pay contracts, but you also have, at least your – the LNG that you deliver into Europe, a lot of it goes into Spain to the utilities and chemical companies there. Can you give us some insight into, if you have any exposure and what you're looking for there?

Peter Evensen: Yes. As you point out, we do have take or pay contracts. We get paid whether we're full or empty. But it is an interesting point. There is few different dynamics. One is that Europe wants to reduce its exposure to Gazprom in Russian LNG. And so they are interested in getting more LNG coming in from other sources, and developing more sources.

So for example, most of the time our RasGas II vessels go from Qatar into Europe, and – but overall, LNG cargoes which are selling at $10.00 to $12.00 in Europe are worth $15.00 to $16.00 in Asia. And therefore any time there's a drop off, we are watching our ships take cargoes out to Asia, and we're actually also seeing re-export. In other words, gas comes into Europe LNG. If it isn't immediately needed, it's resold, and it goes out to Asia. So I think we feel pretty good about that.

And the final point is that Europe is serious about reducing its dependence upon coal, and moving to LNG electricity. So we're seeing a changeover as older coal plants switch over to LNG. And as you know, Germany has said they're going to close all their nuclear reactors.

Ron Londe: Okay. Thank you.

Peter Evensen: Thank you.

Operator: Thank you. There are no further questions at this time.

Peter Evensen: All right. Thank you very much. Hopefully, we can see some of you at Investor Day. Thank you very much.

Operator: Ladies and gentlemen, this does conclude the conference call for today. You may now disconnect your line, and have a great day.

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