TEEKAY OFFSHORE PARTNERS LP

Moderator: Emily Yee
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11:00 am CT

Operator: Welcome to Teekay Offshore Partners Fourth Quarter and Fiscal 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 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 introduction I would like to turn the call over to Mr. Peter Evensen, Teekay Offshore Partners Chief Executive Officer. Please go ahead sir.

(Scott): Before Mr. Evensen begins I would like to direct all participants to our Website at www.teekayoffshore.com where you will find a copy of the fourth 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 fourth quarter of 2012 earnings release and earnings presentation available on our Web site. I will now turn the call over to Mr. Evensen.

Peter Evensen: Thank you (Scott). Good morning everyone and thank you for joining us on our Fourth Quarter of 2012 Investor conference call. I'm joined today by Teekay Corporation's CFO Vince Lok, its chief strategy officer, Kenneth Hvid and its MLP controller David Wong.

During our call today I will be walking through the fourth quarter of 2012 earnings presentation which can be found on our Web site. Starting on Slide Number 3 of the presentation I will briefly review some of the Teekay Offshore's recent highlights.

We generated distributable cash flow of $45.9 million in the fourth quarter, up 11% from the same quarter the prior year. For the fourth quarter we declared a cash distribution of 51 and quarter cents per unit which was paid on February 14th and was consistent with the previous quarter.

We now expect the previously announced acquisition of the Voyager Spirit FPSO to be completed in March 2013 upon final insulation of the FPSO on the Huntington field and commencement of its five year charter to E.ON. In connection with this pending acquisition the partnership expects to increase its cash distribution for the first quarter of 2013 to be paid in May 2013.

I will discuss the partnerships ability to increase distributions in 2013 and into the future during this presentation. I'm pleased to announce that Teekay Offshore has signed a letter of intent to provide a floating storage unit in Asia to London Stock Exchange listed Salamander Energy.

This project represents a broader trend we're seeing in the market of increased demand for FPSO and floating storage unit solutions that I'll discuss later in this presentation. Our sponsor

Teekay Corporation reported a major milestone was reached on the Cidade de Itajai FPSO this past weekend.

On February 16th the FPSO achieved first oil and began its nine year contract plus extension options with Pertobras. As a reminder this FPSO is jointly owned by Teekay corporation and Odebrecht in Brazil. Under the terms of the omnibus agreement, Teekay Corporation is obligated to offer the partnership their 50% ownership interest in this unit within one year of commencement and announced that they intend to offer it to us in the next 30 days.

Finally as I highlighted last quarter Teekay Offshore remains in a strong financial position with $587 million of liquidity in the form of cash and undrawn revolving credit facilities, pro forma for the net proceeds of approximately $167 million received from our recent Norwegian bond offering, net of repurchase of $66 million of our existing Norwegian ((inaudible)) bond.

Of this $587 million in liquidity, only $170 million will be needed for completion of the Voyager Spirit FPSO acquisition. On Slide Number 4, I will discuss our recently signed letter of intent with Salamander Energy to provide an FSO on the Bualuang field in the Gulf of Thailand.

The proposed terms of the contract are for a ten year charter plus extension options for an additional five years and the expected startup date is in mid-2014. We plan to use one of our older remaining shuttle tankers, the 1993 built Navion Clipper as the conversion vessel for this project with a total project estimated approximately $50 million.

This FSO will service the Bualuang field which was originally brought on stream back in 2008. In order for Salamander to lower the cost of oil production the field is undergoing a redevelopment which includes a production platform and an FSO. The FSO solution will be similar to another Teekay Offshore owned FSO, the (Patonic) Spirit which also operates in the region.

If finalized this new FSO project will enable us to successfully extend the life of one of remaining older shuttle tankers under a long-term fixed rate contract which will continue to support the cash flow stability of the partnership.

Moving on to Slide Number 5, I want to discuss how Teekay Offshore is at the leading edge in terms of innovation in two growing offshore markets. With our pending acquisition of the Hiload Dynamic Positioning Unit and Teekay's investment in Remora as well as Sevan's Cylindrical FPSO, we have one of the broadest service offerings in the offshore sector in terms of handling all of our customers transportation, storage and production needs through multiple service offerings.

Importantly, each of these solutions has been tested or utilized in our core markets of the North Sea and Brazil which constitute some of the most exciting areas in the offshore oil space today. We're currently engaged in five front-end engineering or FEED studies analyzing various FPSOs and floating storage solutions. And these projects represent over $3 billion future potential project value in 2016 and 2017.

As the graph on the bottom-left of this slide depicts, we are excited that these markets are expected to continue to grow. We see a lag factor of approximately ten years between drilling and production. And with drilling activity increasing over the past few years and predicted to grow through 2017, we believe there will continue to be a strong demand for our production, storage and transportation services for at least the next decade.

Turning to Slide Number 6, I will expand on our fleet renewal that has been ongoing since January 2011. Over the course of the past two years Teekay Offshore has sold or (laid) up the total of eleven older vessels as part of our fleet renewal process where related charters have either been terminated or expired.

This includes five conventional tankers, one floating storage unit and five shuttle tankers. While the partnership generated approximately $17 million in upfront charter termination fees and $61 million in vessel sales proceeds, the approximate annual loss distributable cash flow or DCF to the partnership as a result of removing these eleven vessels from the operating fleet is approximately $36-1/2 million.

However, as I will show on a later slide, this lost cash flow will be more than made up through acquisitions and organic growth that are already in Teekay Offshore's growth pipeline. On Slide Number 7, we provided an age profile of Teekay Offshore's remaining conventional and shuttle tanker fleets in blue with our recent sales illustrated by the green shaded bars.

With these recent disposals other than the Poul Spirit and Gotland Spirit conventional tankers, our current fleet renewal program is now largely complete with the remaining older vessels earmarked for offshore or floating storage unit conversion projects like the 1993 built Navion Clipper for the Salamander Project. Or other FSO projects which are currently in the FEED study stage.

Our recent acquisition of the (Ominsan) Class shuttle tankers in 2010 and 2011 and the four newbuildings delivering this year which will service the BGs needs in Brazil are helping to renew the fleet and reduce the average age of our trading vessels from 12.3 to approximately 9-1/2 years, well below their expected useful life in the current trading capacity of approximately 25 years.

Moving to Slide Number 8, I will walk through how we expect our new near-term growth will more than rebuild the lost cash flow I already discussed. Distributable cash flow has been reduced by approximately $36-1/2 million due to the vessel sales and associated contract terminations.

However, with the addition of the Voyager Spirit FPSO the delivery of our four newbuilding shuttle tankers and the commencement of the HiLoad DP Unit contract with Petrobras, Teekay Offshore will more than offset the lost DCF from our fleet renewal program allowing for future distribution increases even after adjusting for the additional comment units issued during this period.

Looking at the graph on the right we've highlighted the lost DCF from our fleet renewal program relating to conventional tankers, shuttle tankers and an FSO in green. This lost DCF is then expected to be more than offset with new cash flows of over $77-1/2 million shown in blue, generated through near-term acquisitions and organic growth.

In addition to the known near-term acquisitions our sponsor Teekay Corporation has a number of other FPSO acquisition opportunities which may be offered to the partnership. These will be reviewed in more detail on the next slide.

On Slide 9 I will review the significant visible growth opportunities for Teekay Offshore which will help is further growth the partnership and its LP distributions over the coming years. In addition to the near-term growth already discussed, we may be offered a number of attractive assets serving under long-term contracts with high quality customers over the next several years and we believe this growth pipeline will allow us to drive distribution growth to unit holder going forward.

Notably as indicated at the bottom of the slide, Teekay Offshore has developed a potential pipeline of new projects through a total of three omnibus agreements. One with our sponsor Teekay Corporation, another with Sevan Marine and one more with Remora AS. These omnibus agreements have expanded Teekay Offshore's product offerings, improved our market position and should provide a steady flow of new development projects into the future.

In addition as indicated at the right side of the slide, Teekay Offshore is currently working on five FPSO and FSO FEED studies related to projects valued at over $3 billion. Should some or all of these studies translate into project awards Teekay Offshore's long-term growth pipeline will be full through 2016 and 2017.

On Slide Number 10, I will review on consolidated operating results for the quarter comparing an adjusted fourth quarter 2012 income statement with an adjusted third quarter 2012 income statement which excludes the items listed in Appendix A of our fourth quarter earnings release and reallocates realized gains and losses from derivatives to their respective income statement line items.

Net revenues increased by $8.1 million mainly due to customer reimbursements of $5-1/2 million associated with FEED studies related to two North Sea floating storage projects that are currently - that we're currently pursuing. Higher revenues from the Navion Saga FSO unit since it was in dry dock in the third quarter and $2 million of catch-up revenues from the volatile organic compound or VOC sequent recently acquired.

FPSO revenue also increased from credits earned on unused shutdown days on the Rio das Ostras and Piranema Spirit FPSOs. This was offset by lower project revenues from our shuttle fleet and redelivery of two in charter shuttle tankers.

Vessel operating expenses increased by $8-1/2 million mainly from costs incurred on the two FSO FEED studies I spoke about earlier. Please note that the revenues and costs associated with the FEED studies are both recognized when the FEED studies are completed.

Time-charter hire expenses increased $600,000 mainly due to hire ((inaudible)) in chartering to service our contract of affreightment. Depreciation expense decreased by $500,000 mainly due to the write-down of the Navion Clipper in Q3.

General and administrative expense decreased by $1-1/2 million primarily related to cost reduction initiatives and timing differences. Net interest expense including realized losses on interest rate swaps and cross currency swaps decreased by $1.2 million primarily due to the proceeds of the September 2012 equity offering which were applied toward the reduction of revolving credit facilities.

Net loss income from discontinued operations reflects the results of our conventional tankers that were sold in 2012. The loss in the current quarter mainly relates to the write downs and loss of the sale of three conventional tankers that occurred late in 2012.

Looking at the bottom line, adjusted net income increased to $29.1 million in the fourth quarter from $24.3 million in the previous quarter. I won't walk through all of Slide Number 11 which was included on our recent earnings release; however I'd like to highlight the information in the box at the bottom of the slide. We generated approximately $45.9 million in distributable cash flow which when compared to our total distribution payout resulted in a coverage ratio of 1.0 four times for the fourth quarter.

As discussed earlier, although our cash flows from our older shuttle and conventional tankers will decline as a result of the current fleet renewal program, the pending acquisitions in new building deliveries more than offset this lost cash flow, particularly our upcoming $540 million acquisition of the Voyager Spirit FPSO. Thank you for listening and, Operator I am 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 1 on your telephone keypad. If you are using a speakerphone please make sure your mute function is turned off to allow your signal to reach our equipment.

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 insure our equipment has captured your signal. We will pause for just a moment to allow everyone the opportunity to signal for questions. The first question comes from Michael Webber from Wells Fargo. Please go ahead.

Michael Webber: Hey, Peter. How are you?

Peter Evensen: I'm okay. Thank you.

Michael Webber: Quick question on the Voyager. You mentioned first the distribution of ((inaudible)) in May of '13 assuming the completion of the dropdown. It's only going to be operating for a brief period of Q1. Is that going to be a two stage bump to that distribution or would you do it all in one take?

Peter Evensen: I think we'll do it all in one take. We're used to increasing the distributions in order to reflect the run rate. And so the fact that it comes on late in the quarter shouldn't affect that.

Michael Webber: Okay. That's helpful. Around the FSO contracts, can you give a sense on where the IRR is for that asset? Maybe a range?

Peter Evensen: On the new ones that we're looking at or the Salamander?

Michael Webber: The Salamander and the new ones.

Peter Evensen: Kenneth, do you want to take the Salamander?

Kenneth Hvid: The Salamander is basically like $50 million over ten years. So I think if you (bet) on running around $20,000 a day roughly on an (EBITDA) basis is pretty close.

Michael Webber: Okay. That's helpful. And then the new FSO business you're doing is around the same level?

Peter Evensen: Well we haven't contracted that yet so I don't really want to be drawn on that. But it will be well above 10%.

Michael Webber: Fair enough. Just a couple more. The color on Slide 9 is definitely helpful around the FEED studies on the five FPSOs. Are those relatively uniform in size or do you have any of those that are sticking out larger than 1 billion along the side of the Knarr?

Peter Evensen: Well in - so there's three different kinds I guess you could say. We have out two FPSOs where we're looking at ship shape and cylindrical. So the ship shape, we're interested in those that are more of what I call a sister vessel concept.

So we're looking at Knarr type of FEED studies. So those would be, call it around about 1 billion. And then we're looking at using the Sevan design and those would be $600 or $700 million depending on the top side configuration.

So those are that size. And on the FSOs, those are revolving around conversion of existing units that we have in the North Sea and they range depending on the top-side configuration. So they can go anywhere from $200 million to $400 million.

Michael Webber: That's very helpful. One more for me and I'll turn it over. The Remora HiLoad System, I know it's only been one quarter and it delivers and I think you said Q1 '14. But any early color from Petrobras.

I mean is it something that we'll need to see a trade and perform for a little while before you get a sense of the additional interest? Just any additional color around that asset. I just find it very interesting.

Peter Evensen: Actually I was down in Brazil in December meeting with Petrobras as well as meeting other customers. And since we became involved we've seen more interest in that unit. In particular that we can operate it.

So we're actually more enthusiastic about being able to deliver multiple units there. Of course the system has to be proven. But there is a lot of enthusiasm for the Remora unit because when you look at its cost of lifting and how much it can save the customers like Petrobras, it's significant. And so we're seeing a lot of attraction from other oil companies besides Petrobras.

Michael Webber: Got you, very helpful. All right, thanks again for time guys.

Peter Evensen: Thank you.

Operator: Thank you. The next question comes from Edward Roe of Raymond James. Please go ahead.

Edward Roe: Good morning guys. In regard to the Cidade receiving first oil and then I think you reiterated I guess 30 days before you can get - there may be an offer in place. What - you know, how should we look at the dropdown of the Cidade timing wise?

Peter Evensen: So Teekay Corporation yesterday announced that they would offer it within the next 30 days to Teekay Offshore. So I don't have a formal offer yet. But I've been told it's coming.

And so I think that as per it, that takes somewhere around, you know, 30 to 90 days to go through the system. But the important thing is that we don't drop these down until we've gotten first oil. So we know it's up and operating and in fact on of the wells is already producing 12,000 barrels of oil a day.

Edward Roe: All right. Very good. My next question is, is there any update on the Foinaven?

Peter Evensen: So this is an FPSO that's up at Teekay Corporation which we've indicated in the past is available to be dropped down and is still on Slide 9. That's on charter to BP and we have so far been able to reach agreement with BP on the terms under which they would agree to the transfer of the unit to Teekay Offshore.

So as Teekay Corporation said yesterday there was some operational issues on that unit and that's what's occupying the dialog between Teekay and BP right now. So that continues to be available and it is the intent of Teekay as well as Teekay Offshore that it will be sold down when we reach agreement with BP.

Edward Roe: Okay, and a couple other questions. On Slide 8 the LOSS conventional tanker DCF, that 21.5. Is that taking into account the - you know, once the Poul Spirit and the Gotland are sold, is that the DCF lost? Or is that from previous cash flows lost from other vessels?

Peter Evensen: David, do you want to take that?

David Wong: Sure. If you refer back to Slide 6, it's just the vessels that are sold as of now.

Edward Roe: Okay. So whenever the - there's some clarification around the Gotland Spirit and Poul where you guys say that you expect to sell these in mid, you know, 2013. But are these contract - are the contracts still expiring in 2014 and as per one of the Teekay presentations around, you know, 3Q of last year?

David Wong: That's right. The original contracts are still in place. They expire in 2014. So if we do sell them early and terminate the charters with Teekay they would likely be a termination fee similar to what you saw in the Hamane Spirit last year.

Edward Roe: Okay. All right. Very good. That's all I had. Thank you.

Operator: Thank you. The next question comes from Martin Roher of MSR Capital Management. Please go ahead.

Martin Roher: Thank you operator. My question is regarding your dividend growth target over the long-term. In the past you've talked about mid-single digits I believe. But given the increase number of projects being constructed with charters in place and the two accretive acquisitions you've done it appears at least to me, that Offshore will grow its cash flow on a per share basis at a rate higher than that.

Is that accurate and what are your current thoughts regarding the long-term dividend growth? I know you've been increasingly conservative on the balance sheet. But what can you share with us?

Peter Evensen: Hi Marty. Yes, we're comfortable saying that we'll grow at the mid-single digits. But as you point out and as we show on Slide 9, if those come a little faster you could actually see much greater growth.

And there's some very big units like the Knarr for $1 billion that could materially increase the cash flow. But we haven't been drawn on those. So we're sticking to what we're saying which is "We're comfortable that every year we'll grow by at least mid-single digits."

Martin Roher: Thank you and thanks again for all the forward calls you do. They're very informative.

Peter Evensen: Thank you Marty.

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

Peter Evensen: All right. Thank you very much. As you've heard there's a lot going on in Teekay Offshore's space both on the shuttle tankers where we're delivering ships as well as on the FPSOs. And we're already setting up for multiyear growth. So thank you for your support and I look forward to reporting back to you next quarter

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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