TEEKAY LNG PARTNERS' SECOND QUARTER 2018 EARNINGS RESULTS CONFERENCE CALL

Company: **Teekay LNG Partners L.P.**

Date: **Thursday, 2nd August 2018**

Conference Time: **11:00 ET**

Operator: Welcome to Teekay LNG Partners' Second Quarter 2018 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 Mark Kremin, Teekay Gas Group's, President and Executive Officer. Please go ahead, sir.

Scott Gayton: Before Mark Kremin begins, I would like to direct all participants to our website at www.teekaylng.com, where you will find a copy of the second quarter 2018 earnings presentation. We 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 second quarter 2018 earnings release and earnings presentation available on our website. available on our website.

I will turn the call over to Mark to begin.

Thank you, Scott.

Mark Kremin: Good morning everyone and thank you for joining us on the <u>second</u> quarter 2018 investor conference call for **<u>Teekay LNG Partners</u>**. I'm joined today by Scott Gayton, Teekay Gas Group's CFO.

Turning to **Slide 3** of the presentation, we will review some of Teekay LNG's recent highlights:

- For the <u>second</u> quarter of 2018, the Partnership generated total cash flow from vessel operations, or CFVO, of approximately $115 million, resulting in adjusted earnings per unit, or EPU, per limited partner unit of 9 cents. [DO WE REALLY WANT TO HIGHLIGHT EPU THIS QUARTER?]
- The Partnership also reported distributable cash flow, or DCF, of approximately $31 million, resulting in DCF per limited partner unit of 39 cents.
- Our LNG operations continue to improve and will strengthen further as we take delivery of additional newbuildings, all of them going onto fixed-rate charters. In May, we took delivery of the Myrina. In July, we took delivery of the Megara and our Pan Union joint venture took delivery of the Pan Europe. Based on total deliveries to-date, we have delivered over $120 million of annualized cash flow from vessel operations and expect this to continue growing as more vessels deliver. Looking ahead, in August and September we expect to take delivery of two more LNG carriers, including one wholly-owned Floating Storage Unit, or FSU, for the Bahrain project and one 50%-owned ARC7 ice-class vessel, which will service the Yamal LNG project.

- Yamal LNG has requested early delivery of our second ARC7 ice-class LNG carrier, the *Rudolf Samoylovich*, because their second LNG train is ready for an earlier start-up this August. We have worked with the shipyard, our joint venture partner and our JV's lenders, and we're happy to report that our JV intends to deliver the vessel in mid-September, approximately two and a half months before the previously scheduled delivery date in late-November.

- Unfortunately, our consolidated results this quarter were negatively impacted by the 7 multi-gas carriers we took back from Skaugen late last year. They continue to perform poorly, as evidenced by the non-cash write-down taken this quarter. When compared to the same quarter of last year, this multi-gas fleet decreased our quarterly CFVO by almost $5.5 million due to repair expenditures and our inability to trade two of the vessels while they were under creditor protection. All seven vessels are now under our control and available for trading, but the negative contribution from them this quarter shielded the cash flow strength exhibited by our LNG fleet. Looking ahead, we expect the strong contribution from our LNG fleet to more than outweigh any future weakness from our multi-gas fleet.

- We have been proactively addressing our upcoming debt maturities with the completion of 4 financings since our last earnings update. Importantly, in some cases, we have been able to reduce the financing cost while also extending maturities. All of our financings and re-financings for 2018 are nearing completion, and we have begun addressing our 2019 maturities and expect to complete them later this year.

Turning to **Slide 4,** we look at the fundamentals in the LNG shipping market, where we continue to see improving rates for LNG carriers. Spot charter rates for 160,000 cubic meter LNG carriers were on average 63% higher year-over-year in the first half of 2018, reaching an average high of nearly $90,000/day in June, according to Clarksons. Demand was driven by strong Chinese imports, which were almost 50% higher in the first half of 2018 compared to the same period of the prior year. Spot rates were also supported by supply outages at export facilities in the US, Australia, and Malaysia, and ongoing start up delays at some LNG export projects. This combination of higher LNG demand, and gas supply disruptions, led to higher LNG prices in Asia, which created a Europe-to-Asia arbitrage opportunity similar to previous peak winter levels. Teekay LNG was able to take advantage of these elevated spot rates when our Teekay-Marubeni joint venture fixed the Magellan Spirit in June to an Asian charterer in the region of $90,000 per day.

Turning to **Slide 5**, we expect the remainder of this year to continue with this positive outlook.

We anticipate that new liquefaction capacity, combined with higher seasonal demand in Asia, will likely lead to a firmer market for the remainder of the year and beyond.

On the liquefaction side, we are expecting new export capacity to come on-line in the United States, Australia and Russia, which will increase the demand for LNG vessels. In addition, we expect that seasonal demand for LNG imports into China will again strengthen into the winter, as we have seen in recent years and as can be seen on the chart on the bottom left of this slide. This seasonal demand has historically been supportive of increases in spot LNG charter rates during the winter months, as seen on the chart on the bottom right.

Turning to **Slide 6** we are excited to provide you with an update on Bahrain LNG.

Bahrain LNG, of which Teekay LNG holds a 30% interest, has a 20-year contract with the Kingdom of Bahrain to build, own and operate the country's LNG import terminal. In addition, Bahrain LNG has chartered in our 100%-owned FSU, the Bahrain Spirit, for 20-years. The picture at the bottom right of this slide is our FSU on gas trials. We look forward to its delivery from the shipyard around the end of August and, as expected, the commencement of its charter contract in September of this year.

The Bahrain Terminal is now over 90% complete. Significant recent milestones include the completion of the breakwater, the installation of the offshore jacket which will support the regasification module, and the completion of the subsea pipeline.

The photo on the left of slide 6 shows the construction status of the offshore facility with the installed offshore jacket structure in the foreground. The regasification module, currently under construction in Thailand and scheduled to deliver to the site this quarter, will be installed on top of the jacket structure. The jetty platform can be seen behind the jacket structure. This is where our FSU and the carriers discharging LNG will moor.

Construction of the onshore facility is ongoing, as you can see in the top right photograph.

This is a strategic project for Bahrain and we look forward to updating you on its status as it approaches its commercial start-up date at the end of the first quarter of 2019.

We presented **Slide 7** last quarter and we have updated it for this quarter's activities. We like this slide because it acts as a Scorecard of how we see strong operational and financial execution, prudent financial policies and a strong fundamental LNG market backdrop all combining to add value for our unitholders.

- As mentioned earlier, our financings are progressing and we have already made headway on our 2019 maturities.
- We have delivered 9 LNG and 3 mid-size LPG carriers over the past 10 months. With that, our Exmar LPG joint venture took delivery of the final newbuild in its current fleet renewal program. We have another 9 LNGs including our Bahrain Spirit FSU, plus our interest in the Bahrain LNG terminal, set to deliver on-time or, as is the case with our next Yamal ice-class LNG, to deliver early.
- Our LNG newbuilding projects will collectively increase the Partnership's cash flow by over $300 million which, when combined with our balanced financial strategy, will allow us to delever our balance sheet and return capital to unitholders while continuing to service our customers' growing needs in the LNG space.

- And we still see the LNG fundamentals being strong, as indicated by the counter-seasonal strength experienced earlier this summer.

Operator, we are now available to take questions.

Operator: Thank you. If you'd like to ask a question, please signal by pressing star one on your telephone keypad, again that is star one on your telephone keypad and we'll take our first question from Ben Nolan from Stifel.

Benjamin Nolan: Yeah. Great. Thanks. So I have a couple of questions. Number one is, could you – is there anything new that you can say about how you're thinking about distributions, and then similarly the corporate structure more broadly?

Mark Kremin: Sure, Ben. I'm happy to have Scott jump in. On the distribution side, we said it in previous quarters, we will be intending to come out in Q4 with our guidance. Things haven't changed. We're still looking at the deleveraging and getting that down and that will naturally delever as we bring out our order book. We definitely want to have a more sustainable policy, but we're going to become be coming out in Q4. So we don't have much to say, but you're not far away from getting some news on that. On the corporate structuring in itself, we have been looking at various things, including the K-1 status, we certainly don't have any determination on it, but the MLP space has, obviously, undergone some change in recent years, and we're looking at several alternatives. Scott, do you have anything further on that?

Scott Gayton: I think the only thing I would add, we really want to make sure that Teekay LNG is as attractive as possible to our existing and new investors. And so, as we are evaluating our overall tax structure, that will be something that we are very focused on.

Benjamin Nolan: Okay. And is that something that is a 2018 targeted resolution?

Scott Gayton: Yeah. I think that we would like to try and make some decision as we head into the end of the year, it's not critical that it happened on 31st December, 1st January, but it could be easier from a tax reporting point of view. So I think if we are going to make a decision, it would probably be within the next six months, call it.

Benjamin Nolan: Okay. No, that's great. Thanks for that. And then secondly from me, you had mentioned and I know it's been a little bit of a challenge of this multi-gas carriers, that in the press release you're considering the possibility moving them or operating them in adjacent transport markets. So just curious what that would entail?

Mark Kremin: There’s two ways we can look at it. One is adjacent markets and the other is we actually operate them. A few of the ships that – and these are involved in the impairment analysis. They do multiple markets. They could do – there is a petrochemical, and there is more of a chemical market. We might take a look at the cargos that these particular ships are carrying. The other thing we'll do is take a look at how we do commercial marketing regardless of what market we are in. So these things, we're going to be certainly looking at over the next quarter, and we see how it goes.

Benjamin Nolan: Okay. And then lastly from me. As it relates to the ARC7, and we've heard that about Yamal that it's actually ahead of schedule. How difficult is that to actually bring forward the delivery of those and is it something at this point you might expect on some of the subsequent Yamal-related vessels?

Mark Kremin: Sure, Ben. First of all, I'm going to apologise if anyone is experiencing technical difficulties, pardon for us. We've seen there is a bit of a breakup on the line. The Yamal question, the delivery is – we're pretty confident of being able to join to do it at least on this and hopefully subsequent ones. It's not an overwhelming task for DSME and the partners to bring the ship forward. I wish we could actually bring it forward it earlier, but we are trying to be, and I think we will stay the same. They are actually going to be I think August ready to go with the train to very well. But the mid-September, that we've put forward should be a relatively easy thing to do, and we will be going through the northern sea route for that. You've recently seen a number of voyages going very well in the northern sea route, so not expecting any great challenges for earlier delivery on that ship.

Benjamin Nolan: And would you expect any of the subsequent vessels to also be early or request it to be early?

Mark Kremin: Possibly, when we see train three, that's also ahead of schedule. The entire Yamal project is doing very well. So to the extent they ask us, being Yamal to deliver early and to the extent the yard can accommodate, we are happy to accommodate. And I'll say that on behalf of our JV. We are not sure yet on the subsequent vessels, but let's keep our fingers crossed.

Benjamin Nolan: All right. Sounds good, I appreciate it. Thanks guys.

Operator: We'll take our next question from Randy Giveans from Jefferies.

Randall Giveans: Thanks. Good morning, guys. So a few quick questions from me. So with so much focus on delivering the balance sheet, what are your plans for crude tankers or the 10,000 and 12,000 cubic meter LPG carriers or asset sales kind of on the table or even being pursued maybe?

Mark Kremin: On the crude tanker side, it's not a core business for us. So we have our core tankers left, including one is in-chartered. And I think their intention is probably to sell that ship in Q4. We've, as you previously seen, put our two crude oil Suezmaxes – we have marketed them for sale. And so, the intention is certainly to exit the tanker space in due course. It's not going to be a core business for us. In terms of the multi-gas business, we are as you said, looking at various alternatives. We haven't yet started to look at sale, but it is certainly – it's one thing we are going to consider, as well as the commercial management, I mentioned previously. So I think we can get back to you hopefully, later in this year with more or more advice on dealing with multi-gas.

Randall Giveans: Okay. And, Mark, can you give some more colour around the LNG shipping market, but specifically the 35,000 or 38,000 cubic meter sector segments?

Mark Kremin: That's a sector we like, it's cyclical market. Right now, it's down. And we expect that recovery to lag LNG. Good news is that our JV with Exmar is largely fixed. We are fixed to the extent of about 70%, over 70% this year and around 40% next year. And the rates that we fixed, I think, are in excess of – well in excess of both rates, both this year and next year. But in a nutshell, I think it's a good franchise that we have on the mid-sized space. But it's going to be – take a while to recover. And I don't think that's necessarily this year, but we look forward to next year and the years beyond with that.

Randall Giveans: Okay. And then, I guess, last question. Just following up on kind of recent quarters. You've historically shown a – basically a slide showing remaining CAPEX, and then a completed undrawn debt financings for, I guess, at the end of 1Q 2018, you had $1.5 billion of remaining CAPEX, and $1.3 billion in completed undrawn debt financings, can you give us an update on those two numbers?

Scott Gayton: Sure. I can, Randy. At the end June, we had remaining CAPEX of both $1.26 billion, and we had completed...

Randall Giveans: Sorry. Sorry. The line went out there, say that again.

Scott Gayton: Yes. $1.26 billion, $1.26 billion?

Randall Giveans: $1.26 billion, got it.

Scott Gayton: Yes. And we had completed debt financings of $1.1 million, $1.1 million. And we've got the Yamal spirit financing is in progress, and that is roughly $160 million; 1-6-0 million.

Randall Giveans: $160 million. Excellent. All right, well that’s it from me. Thank again.

Scott Gayton: Thank Randy.

Operator: We'll take the next question from Fortis Giannakoulis from Morgan Stanley.

Fotis Giannakoulis: Yes, hi guys and thank you. Regarding the refinancing of the LPG carriers that you announced this quarter, has this refinancing been completed? Or can you give us some colour on that?

Scott Gayton: Yes. That one was done a quarter actually. So it's – that one has been in place since the time of our last call.

Fotis Giannakoulis: Okay. And also trying to understand your dividend capacity; is there a way that you can give us an outlook of what will be your debt repayments going forward? And how these debt repayments will differ versus the maintenance CAPEX that you have?

Scott Gayton: Sure. Yes. As you know, the maintenance CAPEX calculation is one that extends out over the entire life of the assets or it does go over the full 35 years, in the case of an LNG carrier. And then on that debt side, we are typically only able to get debt facilities that are going to amortize over at a maximum of about 16 or 17 years. And so we do end up in a situation where the amount of debt that we pay down is far outweighing the ultimate cash flow that comes from that unit upfront because of the mismatch that we have between the debt and the life of the asset. But as we have seen, we are able to refinance those facilities, so that, that essentially extends and matches the debt facilities with the actual average, with the age of the vessel. So there is a mismatch between the DCF and the amount of debt pay down. And I think from a go-forward point of view, I would look at – we do disclose what our balloon payments are, which we have shown we are able to refinance. And then we've got a regular amortization, that is disclosed and that's probably what I'd look out on a go-forward basis.

Fotis Giannakoulis: Okay. And regarding the overall market, there is a lot of discussion on the positive side about the significant growth in Chinese LNG demand. And on the other side, there are lot of concerns about the trade frictions between US and China? Have you seen any impact on the behaviour of Chinese buyers of LNG, and the appetite to secure long-term contract and how does this – what are the implications for the shipping market, and also the potential of a new wave of FIDs that will create additional demand?

Mark Kremin: I'm so sorry, Fotis, I missed a bit of your first part of the questions, but I heard the rest, I think which is about China, and what the demand is going to do. Hopefully, I captured all but do feel free to clarify.

Fotis Giannakoulis: Yes. I also wanted – yes, I also asked about the implications of the trade friction between US and China, and if this will have any impact on contracting activity and long-term purchasing of LNG?

Mark Kremin: Okay. Well, I don't think that I'm assuming anyone to speak to global trade and the impact to that. I've heard and seen various statements on it. On the one hand, there could be a reduction in trade. On the other hand, if China's exporting goods to us, maybe a balance for that is to sell them a lot of LNG. So where it goes. I'm not an expert on, but I certainly heard both sides of the story. The demand itself regardless of the trade impact is something that we're big believers in, as I said in my prepared remarks. They're up 50% year-on-year and the gas usage itself is really increasing not just LNG, but they are a massive user of gas. And we're seeing a lot of that, fortunately, we ship about 5% of their LNG right now. And we hope to do more in the future. I think that, I guess, I'll leave it at that.

Fotis Giannakoulis: Thank you very much, Mark.

Operator: And we will take our final question from Hillary Cacanando from Wells Fargo.

Hillary Cacanando: Yeah, hi. Thanks for taking my questions. So obviously, China is a big player in terms of the demand, but Japan is still a top importer. I just wanted to get your view on their nuclear restart program, I think it's been a little delayed, but do you think it will be accelerated going forward? Perhaps just wanted to get your view.

Mark Kremin: I don't have a strong view on what the Japanese restarts are going to do on the nuclear power. What I will see I think our opportunity lies more so with China. At this point, the amount of work we can do probably to import LNG into China is more than we can perhaps do for to import LNG to Japan. There is a bit of less of a Japanning type of situation in China. And I think we're able to hopefully grab more of that space [inaudible] get the tenders that we're seeing right now [inaudible] very much many of them are focused for instance on the US [inaudible] to China. And I think we are going to be able to see some of this space. So we are not watching as closely what's going on with the nuclear reactor situation in Japan.

Hillary Cacanando: Good. And also with some of your competitors I've seen them install re-liquefaction units to reduce oil loss during those dry-docking period, is that something you would consider, or is that something that you think is beneficial or not?

Mark Kremin: [Inaudible] and it can't make sense in some situations. It really depends on your future outlook for fuel cost, how old your ship is, whether you have an imminent dry-docking coming up or not. There are number of factors. I think it can make sense in some cases, but where our schedule is right now in terms of docking and our fleet, we don't intend to put any plants on in the near future.

Hillary Cacanando: Okay. It makes sense. That’s it from me. Thank you.

Operator: And there are no further questions. I'd now like to turn it back over to Mark Kremin.

Mark Kremin: Well, as always, I'd like to thank everyone for their support. And also wish you a pleasant end to the summer. So thank you very much and goodbye.