TEEKAY CORPORATION'S THIRD QUARTER 2018 EARNINGS RESULTS CONFERENCE CALL

Company: **Teekay Shipping (Canada) Ltd.**

Date: **Thursday, 15th November 2018**

Conference Time: **14:00 ET**

Operator: Please stand by. We're about to begin. Welcome to Teekay Corporation's Third 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 touchtone 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. Kenneth Hvid, Teekay's President and Chief Executive Officer. Please go ahead.

Ryan Hamilton: Before we begin, I'd like to direct all participants to our website at www.teekay.com, where you'll find a copy of the third quarter 2018 earnings presentation. Kenneth and Vince 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 2018 earnings release and earnings presentation available on our website.

I will now turn the call over to Vince to begin.

Vince Lok: Thanks, Ryan. And thank you all for joining us today for Teekay Corporation's third quarter 2018 earnings conference call. I will briefly review our third quarter results before I handover the call to Kenneth.

Starting with slide three of the presentation. Our third quarter results came in better than expected. Teekay Corporation generated total consolidated cash flow from vessel operations or CFVO of $196 million, which is an increase of $32 million, or 20%, from the $164 million in the prior quarter. We also reported a consolidated adjusted net loss of approximately $11 million, or $0.11 per share, an improvement from the adjusted net loss of $22 million, or $0.21 per share, in the prior quarter.

The third quarter results marked the best quarter of 2018 so far with improved results, primarily driven by higher cash flows from Teekay Parent's three directly owned FPSO units, which had upside exposure to the stronger oil prices and production volume during the quarter, as well as the contract start-up of several growth projects across the Teekay Group, and a counter-seasonally strong spot tanker market.

As a reminder, since we deconsolidated Teekay Offshore on 25th September of last year, our consolidated CFVO in the third quarter only includes 14% of Teekay Offshore's CFVO, whereas in the periods prior to the fourth quarter of last year, it included 100% of Teekay Offshore's CFVO. Had we continued to consolidate Teekay Offshore, our reported total CFVO would have been approximately $340 million in the third quarter of 2018 compared to $238 million in the third quarter of 2017, which would have resulted in an increase of 43%.

Also in the quarter, Teekay Parent generated adjusted CFVO of approximately $20 million, which includes CFVO from our directly owned assets and cash distributions from our publicly traded daughter entities, which is up from $17 million in the prior quarter and also marks the best quarterly results for 2018. The improvement was driven primarily by higher cash flows from the oil-price linked production tariffs on the Banff and Hummingbird Spirit FPSO units.

Looking ahead into the fourth quarter. We expect to see a temporary decline in the Banff and Foinaven's CFVO, mainly due to unplanned maintenance shutdowns during Q4. However, this will be partially offset by higher expected revenue from the true-up of annual performance-based revenues under the Foinaven contract. Despite this, we are expecting our consolidated results to be stronger in the fourth quarter compared to the third quarter due to higher forecasted earnings in each of our daughter entities. Also, commencing in 2019, Teekay Parent's adjusted CFVO will benefit from Teekay LNG's intended distribution increase which Kenneth will touch on later in the next slide.

For further details on our third quarter results as well as our fourth quarter outlook, please refer to the slides in the appendices to this presentation. I will now turn the call over to Kenneth.

Kenneth Hvid: Thanks, Vince. I will just briefly review the next four slides on our daughter entities, as I'll assume most of you listened in to their respective earnings calls earlier today.

On slide four, we have summarized Teekay LNG's recent results and highlights, and the status of its growth projects. Teekay LNG Partners generated CFVO of $133 million and adjusted net income of $20 million, or $0.16 per unit, with total CFVO up 15%, adjusted net income up 44%, and adjusted earnings per unit up 78% compared to the previous quarter. Since June, Teekay LNG has taken delivery of three LNG carriers and a floating storage unit which will trade in the spot market until it delivers to the Bahrain regasification project early next year. The deliveries also included our second ARC7 LNG carrier newbuilding for the Yamal LNG project which delivered two months ahead of the original scheduled delivery date.

To date, the Partnership has taken delivery of approximately half of the estimated $310 million of total CFVO growth associated with the newbuilding program. A further 7 LNG carriers are still to deliver along with the start-up of the Bahrain regasification project, which will drive further cash flow growth and the de-levering of its balance sheet.

Looking at the fundamentals, the current spot LNG shipping market continues to strengthen to new multi-year highs. Teekay LNG has taken advantage of this development, recently securing new charters at higher rates for one vessel and is well positioned to further benefit, as three additional vessels have short-term charters maturing through May 2019. In addition, we expect to take delivery of six LNG carrier newbuildings three to five months ahead of schedule, all of which are expected to add significant CFVO in 2019 and beyond.

I'd like to take a moment to recognize our technical teams that have been working closely with the shipyards and the customers to deliver these vessels ahead of schedule.

Teekay LNG has been speaking for the past few quarters about implementing a balanced capital allocation plan, and yesterday Teekay LNG announced its intention to increase distributions to its unit holders by 36%, starting next year. This level of payout will allow the Partnership to de-lever its balance sheet into its target range within the next couple of years, which will create significant strategic flexibility for the Partnership to both return additional capital to unit holders and to continue growing its LNG fleet at a time when we expect significant demand for LNG shipping services.

Also announced yesterday, Teekay LNG plans to amend its tax status to be treated as a corporation instead of a partnership, subject to common unitholder approval, which is expected to provide access to a larger investor base. This change should not result in Teekay LNG recognizing a gain or loss or change its taxes payable going forward.

On slide five, Teekay LNG's new capital allocation strategy allows it to naturally decrease leverage from the current approximately nine times of CFVO down to its targeted range of approximately five and a half times as newbuild projects and their associated cash flow deliver and begin to have a positive impact on its balance sheet.

Teekay LNG expects to generate total CFVO of approximately $650 million to $680 million in 2019 including our joint ventures on a proportionate basis. This will help the Partnership to repay roughly $300 million per year of scheduled debt amortization payments, including its share of joint venture debt. This level of debt repayment represents over 25% of Teekay LNG's current market cap. All of this value builds equity inside Teekay LNG that accretes to its unitholders including Teekay Parent through its LP and GP interest. And as Teekay LNG approaches its targeted leverage range of five and a half times, they will look at increasing returns to unit holders and pursuing attractive growth opportunities in a very disciplined manner. Let me also clarify that changing from a K-1 to a 1099 filer doesn't mean that TGP is not an MLP. As TGP de-levers, it increases its capacity to return capital and therefore there is a high correlation between the de-leveraging and the potential value of the IDRs.

Turning to slide six, Teekay Tankers reported total CFVO of $28 million, an improvement from $17 million in the prior quarter, and generated an adjusted net loss of $18 million, or $0.07 per share, which improved from an adjusted net loss of $29 million, or $0.11 per share, in the prior quarter.

Crude tanker rates strengthened counter-seasonally during the third quarter of 2018, which is typically the weakest quarter of the year. Importantly, rates continue to improve in the fourth quarter to date, driven primarily by very low fleet growth as a result of high scrapping activity and higher oil production from OPEC, Russia and the United States. Based on approximately 59% and 54% of spot revenues booked, Teekay Tankers' fourth quarter to date Suezmax and Aframax bookings have averaged approximately $19,000 and $19,900 per day, respectively. For its LR2 segment with approximately 42% of spot revenues booked, fourth quarter to date earnings have averaged approximately $17,000 per day.

Looking at the graph on the right, we highlight Teekay Tankers' significant operating leverage to a tanker market recovery. If spot tanker rates stay at Q4 to-date levels, Teekay Tankers estimated annual free cash flow per share would be approximately $0.40 per share over the next 12 months. And at current market rates, its annual free cash flow would increase to over $1 per share, which is extremely attractive relative to its last closing share price of $1.06.

Lastly, as the tanker market improves Teekay Tankers continues to work on various financing initiatives, including the recent completion of two sale-leaseback transactions and a working capital loan, all of which help bolster its liquidity position by $100 million, of which $40 million were secured in transactions completed after 30th September, and extended its debt maturity profile.

Looking at slide seven, we have summarized Teekay Offshore's recent results and highlights and the status of its growth projects. Teekay Offshore Partners generated CFVO of $167 million, up from $162 million in the prior quarter. This increase was driven by stronger results in our shuttle fleet, a full quarter contribution from various growth projects, and lower operating costs. In July, Teekay Offshore refinanced its 2019 bond maturities and $200 million promissory note with a new $700 million bond maturing in 2023. The new bond takes out 2019 maturities and significantly improves Teekay Offshore's debt maturity profile.

In late October, Teekay Offshore announced that it reached a constructive settlement agreement with Petrobras for a total of $96 million related to previously terminated contracts on the HiLoad DP unit and the Arendal Spirit unit for maintenance and safety, which Teekay Offshore expects will result in the recognition of approximately $91 million of revenue in the fourth quarter of 2018, based on the present value of future settlements.

Lastly, in October Teekay Offshore entered into a conditional seven-year charter agreement with Alpha Petroleum for the Varg FPSO for their development of the Cheviot oilfield. The customer is now funding the project ramp-up and other work that needs to be completed prior to the Varg FPSO moving to Singapore, where it will undergo upgrades and life extension work which will be funded by the customer in advance. This means that Teekay Offshore is able to redeploy an existing asset on a new field with minimal, if any, of its own capital being required to fund the same. It is important to point out that there are still conditions precedent relating to Alpha's financing.

On slide eight, Teekay Parent's results continue to benefit from stronger oil prices from our three directly owned FPSOs, all of which have contracts that have fixed charter rates with upside exposure from both oil prices and production at oil price levels starting from $45 per barrel. Our FPSO CFVO results improved in the third quarter to approximately $19 million, a significant improvement from the same period over the prior year of negative $2 million, driven by contract extensions secured over the past 14 months.

As highlighted on the graph, at the bottom of this slide, our results in the fourth quarter are expected to temporarily lower as a result of maintenance shutdowns for the Banff and Foinaven as well as some maintenance bonuses recognized in Q3. This is partially offset by additional estimated revenues from the Foinaven annual production bonus. Excluding the impact on maintenance shutdowns, the fourth quarter CFVO would have ranged from $10 million to $20 million at oil prices between $60 and $80 per barrel.

As mentioned in previous quarters, we highlighted that these assets are non-core and debt-free and that we look to sell them over time. However, we are currently in live discussions with each of the three existing charterers on potential multi-year contract extensions, as these units are needed by our customers to continue producing on their fields. Since the value of these units are highly correlated with the associated charter contracts in place, we are currently prioritizing securing contract extensions for engaging in any final and formal sales discussions with potential buyers.

Despite the recent volatility in oil prices, we believe that longer term offshore fundamentals remain intact and that we are well positioned to secure additional contract extensions which would be mutually beneficial to both Teekay and our customers. In the meantime, we will continue to benefit from strong cash flows from these assets.

I'd like to finish the call today on slide nine. We presented a similar slide in February this year that highlighted that Teekay Group was approaching a positive inflection point, financially, operationally, in terms of project deliveries, and from a market fundamentals point of view. We have provided an update for each entity and we are making steady progress towards greater value creation to all our shareholders and unitholders across the group.

Teekay LNG has experienced LNG volume trade growth up 9% year-over-year and the spot LNG carrier market continues to hit multi-year highs and as highlighted earlier, Teekay LNG is taking advantage of the strength by fixing out vessels at higher rates. Teekay LNG has done a great job of completing virtually all of its 2018 and 2019 financings. While its leverage is currently higher than we like, it is well positioned to de-lever as its newbuilds deliver and begin to cash flow. In addition, with a balanced capital allocation strategy, they can continue to strengthen their balance sheet while returning more capital to unitholders. Lastly, Teekay LNG has grown its CFVO by 24% in the third quarter compared to the same period of the prior year with more to come from project deliveries through 2019.

Teekay Tankers continues to benefit from favorable supply-and-demand fundamentals and spot tanker rates have also hit multi-year highs which we believe represents the beginning of a more sustained recovery in the tanker market. Teekay Tankers has done a great job completing numerous financings and continue to focus on building liquidity and extending its debt maturity profile. Lastly, Teekay Tankers CFVO has grown by 35% in the third quarter compared to the same period of the prior year as a result of higher spot tanker rates during the quarter, which have further improved in the fourth quarter of 2018 to date.

Teekay Offshore continues to benefit from increasing offshore activity through securing numerous FPSO contract extensions and a conditional seven-year charter contract for the Varg FPSO. Teekay Offshore has also done a great job with the refinancing of its 2019 bond maturities and will naturally de-lever as its growth projects are fully reflected in its cash flows. Lastly, Teekay Offshore has also grown its CFVO by 35% in the third quarter compared to the same period of the prior year, as a result of project deliveries.

And looking to the far right-hand column of the slide, Teekay benefits alongside fundamental improvements across each of our companies. Teekay has also reduced its financial leverage with the completion of bond buybacks midyear with more to come with agreed sale of our interest in Sevan Marine and the potential sale of our non-core offshore assets at the right time. Lastly, Teekay Parent adjusted CFVO is up $19 million in the third quarter compared to the same period of the prior year, driven mostly by the stronger FPSO results.

So, summing up this slide, we are making steady progress towards greater value creation. The energy markets are providing tailwinds for our businesses. Each of our companies has and will continue to strengthen financially and our cash flows are growing, noting that there is more to come that have not yet been reflected in our financial results. As these factors continue to strengthen in unison, the intrinsic value of our companies including Teekay should increase.

With that, operator, we are now available for questions.

Operator: Thank you. And ladies and gentlemen, as a reminder, if you'd like to ask a question, please signal by pressing star one on your telephone keypad. And if you are using a speaker phone, please make sure your mute function is turned off to allow your signal to reach our equipment. Once again, that is star one to signal for a question. Our first question comes from Michael Webber of Wells Fargo. Please go ahead.

Michael Webber (Wells Fargo): Hey, good morning, guys. How are you?

Kenneth Hvid: Good morning, Mike.

Michael Webber: Feels like a light day with only three Teekay earnings calls today. So I appreciate you spreading them out this year.

Kenneth Hvid: No problem.

Michael Webber: I asked most of the companies the sector specific questions on the respective calls. But, I guess, with regards to Teekay specific – Teekay Parent – I guess, Vince, first around FPSOs – actually both, and Kenneth you mentioned, looking for a long-term charter for those or kind of terming out that employment and really kind of looking under every rock there and trying to exhaust all your resources there before you think about selling, is it right to think about that as kind of one of the levers you guys are looking at near-term, in terms of handling the bonds that come due in 2020? Like, if that – is that the right way to think about that, is that something you would want to get a handle on and figure out what you're doing there before we think about you kind of sourcing other forms of capital to handle those upcoming maturities?

Vince Lok: Yeah. Hi, Mike. Yeah. First of all, we still have a lot of time to address the bond, which is in 2020.

Michael Webber: Yeah.

Vince Lok: And in some ways, when we're – the more time you wait, the make-whole price of the existing bonds decreases over time as well. Right now, as you know, we did buy back some bonds midyear, so we're down to about $540 million outstanding right now. Our cash balance is over $200 million including the Sevan sale. So, first of all, I think when we're going to look at refinancing the bond, it will be a smaller amount, because we can apply some of this cash and potential proceeds from offshore assets – asset sales. And so, it'll be a smaller bond refinancing. And so, you're right that there is, I think, the ability to further de-lever if we are able to monetize some of these assets prior to that. I don't think we're completely dependent on that. I think it would be a nice thing to do, but we want to focus on making sure we maximize the value of these assets first and foremost. And if we do – let's say, do a bond, we want to also look for some prepayment flexibility in case we do sell some of these assets in the future. So, it is – there is a link there to these three FPSOs, but not specifically.

Michael Webber: So, there is no obvious sequencing to how you would tackle those. It's going to be kind of opportunistic, I guess.

Vince Lok: That's right.

Michael Webber: Okay. And I guess, maybe this ties into a broader question – and maybe this is a good one for Kenneth, but just in terms of how you think about Teekay's exposure to offshore longer term, obviously you don't control the GP for TOO anymore. It's – the way it's presented has changed a bit in terms of the aggregated data. Aside from your interest in TOO and the three other FPSOs, is that something where you think over time that you just – do you have a much more kind of a passive exposure to the offshore space, or is it something where you think you could see maybe a year or two from now active investment at either the Teekay Parent level or through some other entity back into the offshore space?

Kenneth Hvid: No, we wouldn't see that. We are very focused on the two segments, the tankers, which we've been in for, as you know, for 45 years, and the –

Michael Webber: Yeah.

Kenneth Hvid: – the gas business, which we've been in for 15 years now. That's what we consider our core businesses. The offshore has definitely become a lot less core last year through the transactions that we did. At the same time, we are intrigued, of course, by the offshore fundamentals at the moment, and it's all about value creation. But, you're not – you're most likely not going to see us invest more in the offshore space.

Michael Webber: And so it's just gradually becoming a bit more passive around offshore, kind of passive exposure?

Kenneth Hvid: Yes, that's right. I mean, offshore obviously still carries Teekay on the funnel, and there is a great customer overlap and there is a brand promise, and we have a lot of synergies by operating together with Teekay Offshore. But from a capital allocation point of view, it is very clear that Brookfield is in the driver's seat on investing in TOO. And they're, of course, a great sponsor for the entity, and we're happy to take a backseat on that and focus on the two areas here that we consider more core for Teekay going forward.

Michael Webber: All right. And just so I'm clear, in terms of bearing the brunt of, maybe, kind of any costs associated with FEED work around other new FPSO projects or continued shuttle tanker investment, is that all being done at TOO now or is it still somewhat split between the Parent and TOO?

Kenneth Hvid: No, that's 100% contained within Teekay Offshore.

Michael Webber: Okay.

Kenneth Hvid: The Varg project actually got funded by the customer, the FEED work done there, but it is contained within Teekay Offshore that any development work or R&D work or FEED work for that.

Michael Webber: Okay, just one more for me and then I'll turn it over. Just, can you remind us, what percentage of the TGP units that are held by Teekay are already collateralized?

Vince Lok: I think most of it is collateralized under the equity margin loan for TGP. We have some units in TNK and Teekay Offshore that are not.

Michael Webber: Okay, I can follow up on those details. Thanks guys, I appreciate it.

Vince Lok: Sure.

Operator: Thank you. Our next question comes from Melvin Shieh of Bank of America.

Melvin Shieh (Bank of America): Good afternoon, guys. I just want to ask a general market question, specifically. Where do you see the risks or what concerns you the most about the story, the story of improving markets for LNG tankers and, I guess, also the offshore sector?

Kenneth Hvid: Well, I think we covered a lot of the market fundamentals in the gas space and that's clearly where we have the greatest balance sheet exposure as a company and as a group. And we've been in the business for, as I said, for 15 years now. And I always remind people about how we looked at it when we got into it and that was at a time when Henry Hub was at $6, and what a difference that we're facing today.

One thing that we've always seen is that once the liquefaction investment has been made, then the production of LNG obviously becomes a marginal cost. And we've seen that essentially all of the LNG produced needs to be transported somewhere and then, it really becomes a more traditional shipping play, which is around the arbitrages that we've seen that moves around. And every time that we have an arbitrage that kicks in, then it's normally good for shipping. And from time to time we have a deficit of ships to cover the cargo that needs to be transported, which is what we're seeing at present, and that gives us some periodic imbalances in the supply and demand, and that is what we are managing. Our core model, as you know from our presentations in TGP, is to have the largest portion of our fleet covered by long-term contracts. And therefore, we don't have a huge exposure to that volatility. But, when we do, then, that's obviously additional profits as we are facing right now.

So, in short, we don't really see any concerns. I think it's mostly a matter of the pace at which FIDs will take place. And as these plants start producing LNG, it needs to be transported.

Melvin Shieh: Got it. Great, thanks, that's helpful. And then, just for – as cash flow is increasing, given the improvement in the daughter entities, can you talk a little bit about your priorities, perhaps the – what are your thoughts around shareholder returns versus de-leveraging?

Vince Lok: Well, I think we've been pretty consistent with our messages in the past several quarters about focusing on de-levering the balance sheets across the group and paying down debt and strengthening the balance sheet. So that would be, I would say, our first priority at this point in time is really strengthening the balance sheet across each of the entities.

Melvin Shieh: Great. Thank you. And then, just lastly, are the three FPSOs – or FPSOs at the Teekay Parent Corp., are they impacted in any way by the IMO sulfur caps?

Kenneth Hvid: No, they're not.

Melvin Shieh: Great. Thank you.

Operator: Thank you. Our next question comes from Fotis Giannakoulis from Morgan Stanley.

Fotis Giannakoulis (Morgan Stanley): Yes, hi, gentlemen. Thank you. I would like to ask you about the FPSO, the oil-linked upside. If you can give us a sensitivity of how does this change overall, how does the cash flow for vessel operations change overall for each dollar of increase in oil prices?

Vince Lok: Hi, Fotis. Yeah. If you look at slide eight, you can see a sensitivity of the CFVO to different oil prices. So, if you look at sort of normalized fourth quarter production, the $20 change in Brent here, the $60 to $80 would give you CFVO range from $10 million to $20 million for the quarter. So, I guess for every dollar, it's roughly $0.5 million for the quarter or $2 million annualized.

Fotis Giannakoulis: Thank you. And regarding the long-term plan, the strategy of Teekay Parent now that Teekay Offshore is driven primarily by Brookfield, and TGP is going to become a 1099 filer, it does not really depend so much on its parent, how do you view the previously declared strategy of becoming an asset-light company? And how feasible it is in the current environment to dispose the three FPSO assets that are still at the parent level?

Kenneth Hvid: Yes. As we said in our prepared remarks, we think the first priority and where we can extract the most value from these assets is obviously by having the right contracts on the FPSOs. So, that's what we are focusing on right now. In parallel, we're having discussions with potential buyers. So, I would say, it's very much alive. And you're absolutely right, those three legacy assets would be the last ones to become really asset-light here and own no assets upstairs at the balance sheet.

So, as Vince said, our focus in terms of the TGP is that I don't think that the 1099 changes a whole lot in terms of how we look at TGP from how we've looked at TGP a year ago. We are still very much focused on building a stronger balance sheet, building a lot of underlying value, which we're doing by paying down debt rapidly. And with that, we will increase our flexibility to create some real meaningful value to the LP holders, but also very importantly for the GP.

Fotis Giannakoulis: Have you given any thought about the plan and the purpose of Teekay Parent, after you achieve these goals, meaning the contracting of the three FPSOs and a potential disposal, either to TOO or some other party, and after you de-lever your balance sheet? Any thoughts of buying back assets or even rolling over the entity to its daughters or investing in other sectors other than the ones that two daughter companies are involved in?

Kenneth Hvid: Yes. The answer is probably yes to all of the above. But, as we've also said all along here, our primary focus has been to build the financial flexibility and the strategic flexibility, which is exactly what you're talking about is how we do capital allocation. But, that flexibility you only have – if you can be truly independent of – at least, partly independent of what the markets are doing and that comes through having a much stronger balance sheet and that's what we are really focused on here. And we believe that we will get there in the next couple of years.

Fotis Giannakoulis: Thank you very much.

Kenneth Hvid: Thank you.

Operator: Thank you. And ladies and gentlemen, that does conclude today's question-and-answer session. I'd like to turn the conference back over to Mr. Kenneth Hvid for any additional or closing remarks.

Kenneth Hvid: Well, thank you, first of all, for participating in our call today. Through the year, we have been focused on executing on our projects and operating our assets well. Our underlying results have continued to improve through the year. And we look forward to reporting back to you on our progress in February. Thank you.

Operator: Thank you. And, ladies and gentlemen, that does conclude today's conference call. We do thank you for your participation. You may now disconnect.