TEEKAY CORPORATION'S FOURTH QUARTER 2018 EARNINGS RESULTS CONFERENCE CALL

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

Date: **Thursday, 21st February 2019**

Conference Time: **14:00 ET**

Operator: Welcome to Teekay Corporation's Fourth Quarter and Fiscal 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 at any time, please press star one 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.

Lee Edwards: Before we begin, I'd like to direct all participants to our website at www.teekay.com, where you'll find a copy of our fourth 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 fourth quarter 2018 earnings release and earnings presentation, available on our website.

I'll now turn the call over to Vince to begin.

Vincent Lok: Thanks Lee, and thank you all for joining us today for Teekay Corporation's fourth quarter 2018 earnings conference call. I will briefly review our fourth quarter results, before I hand the call over to Kenneth.

Starting with slide 3 of the presentation. In the fourth quarter, Teekay Corporation generated total consolidated cash flow from vessel operations, or CFVO, of $247 million, which is an increase of $50 million, or 25% from the prior quarter, and up 34% from the prior year's fourth quarter. We also reported a consolidated adjusted net loss of $2 million, or $0.02 per share, an improvement from the adjusted net loss of $11 million, or $0.11 per share in the prior quarter.

In the fourth quarter consolidated results, this marks the best quarter of 2018. As shown in the graph on the far right, the improvements quarter-over-quarter can primarily be attributed to higher cash flows in Teekay LNG, due to the delivery of contract delivery and contract start-up of various LNG newbuildings and certain vessels commencing new contracts at higher rates, and an increase in spot tanker rates in Teekay Tankers.

Fourth quarter results also included our minority portion of Teekay Offshore's previously announced positive settlement with Petrobras. However, Teekay Parent's CFVO declined in the fourth quarter, mainly due to the unplanned maintenance shutdown of the Banff FPSO, which we mentioned during last quarter's earnings call and an unplanned shutdown of the Foinaven FPSO from late November, as well as higher oil tariff revenues recognized in the third quarter.

I am pleased to report that both FPSO units were back up and running as of early November for the Banff, and early January for the Foinaven. As a reminder, since we deconsolidated Teekay Offshore on 25th September last year, our total CFVO for fiscal 2018 only includes 14% of Teekay Offshore's CFVO, whereas our fiscal 2017 results include a 100% of Teekay Offshore's CFVO, up until deconsolidation on 25th September and 14% thereafter.

After adjusting our 2017 CFVO numbers, assuming we deconsolidated TOO as of the beginning of 2017, CFVO for fiscal year 2018 of $755 million would have been higher than our 2017 results, which would have been approximately $678 million, instead of the $951 million as reported in the table on page 1 of our earnings release.

Also in the fourth quarter, Teekay parent generated adjusted CFVO of approximately $3 million, which includes CFVO from our directly owned assets and cash distributions from our publicly traded daughter entities. This was down compared to the third quarter, mainly as a result of the unplanned shutdowns, which I just touched on earlier.

On an annual basis, Teekay parent's adjusted CFVO has increased by $51 million in 2018 compared to 2017, driven primarily by higher cash flows generated by our directly owned FPSO units, which have upside exposure to oil prices and production.

Kenneth will touch on our three directly owned FPSOs in more detail later in the presentation. And for further details of our fourth quarter results, as well as our first quarter outlook, please refer to the slides in the appendices to this presentation.

Turning to slide 4, over the last three years, we have focused on delevering Teekay parent's balance sheet and continued to make good progress on this, as well as growing adjusted CFVO. During this time, we have eliminated Teekay parent financial guarantees to TOO as a result of the strategic transaction with Brookfield in 2017, and we have significantly reduced Teekay parent's financial guarantees to Teekay Tankers, as a result of their refinancings.

Although not reflected in the top chart, these financial guarantees have reduced from $750 million at the end of 2016 to approximately $166 million at the end of 2018. We have used cash received from TOO Brookfield transaction in 2017 as – and the portion of the capital raise in early 2018 to repay all of our secured debt and reduced our 2020 unsecured bond balance by $95 million to just below $498 million as of today. This includes the repurchase of $42 million of our unsecured bonds at an all-in average price of about 97% of par since the beginning of December 2018, which is below current levels.

Looking ahead, one of our key priorities will be to refinance our 2020 bond maturity with a smaller bond, which is in line with our strategy of delevering the balance sheet, and strengthening our financial position. And we expect to further delever our balance sheet through growing our adjusted CFVO and the potential sale of our FPSO units at the right time.

Moving to the bottom chart, we have increased our adjusted CFVO in 2018, as a result of redeliveries of in-charter LNG and crude tankers during 2017 and new improved contracts on our directly owned FPSOs, which commenced in the latter part of 2017.

Looking ahead, we are very focused on improving Teekay parent's free cash flow through a combination of increasing distributions from our daughter entities, with TGP's distribution increasing by 36% starting next quarter, managing G&A expenses, maximizing the value of our three FPSOs and reducing net interest expense through delevering the balance sheet. However, this is of course not the only measure of value creation. For instance, free cash flow does not capture the equity value that is being retained in our daughter entities over time.

I will now turn the call over to Kenneth.

Kenneth Hvid: Thank you, Vince. If you turn to slide 5, I'll now provide an update on all our three directly owned that FPSOs. We continue to have discussions with each of the three charters on potential multiyear contract extensions as these units are needed by our customers to continue producing on their fields. So, since the value of these units are highly correlated with the associated charter contracts in place, we continue to prioritize securing contract extensions to maximize the value of the – of these unencumbered assets before engaging in any formal sale discussions with potential buyers.

Despite the recent volatility in oil prices, we believe that the longer term offshore fundamentals remain intact and that all three FPSOs will continue to generate value for our customers and TK. In the meantime, we benefit from improving oil prices from these units, 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 by $45 million in 2018 compared to 2017. Also, as highlighted on the graph on this slide, our results during the fourth quarter were impacted by unplanned shutdown on two of our FPSO units. Excluding the impact of these maintenance shutdowns. the fourth quarter CFVO would have been close to $11 million during the quarter.

Looking at the first quarter, we expect our CFVO to range between $4 million and $8 million and oil prices between $60 and $70 per barrel. This range is lower than the $11 million in the fourth quarter after adjusting for the maintenance shutdowns as a result of $6 million of annual operational tariff revenues that were recorded in the fourth quarter under the Foinaven contract and lower expected average oil prices in the first quarter of 2019.

I will just briefly review the next four slides on our daughter entities, as I will assume most of you listened into their respective earnings calls earlier.

We have – on slide 6, we have summarized Teekay LNG's recent results and highlights. Teekay LNG Partners generated total CFVO of $150 million and adjusted net income of $33 million, or $0.32 per unit, with total CFVO up 13%, adjusted net income per unit up 68% and adjusted earnings per unit up 100% compared to the previous quarter.

Since November, Teekay LNG has taken delivery of three LNG carriers all on long-term charters. This includes the Yamal Spirit MEGI LNG carrier, which delivered on 31st January, soon after they completed its long-term financing.

This is a significant milestone for Teekay LNG since their order book is now fully financed. In November, Teekay LNG announced its balanced capital allocation strategy, which includes a quarterly cash distribution increase of 36% commencing in the first quarter of 2019 and payable in May, which is expected to increase Teekay Parent's annual cash flows from the partnership to over $20 million in 2019.

While Teekay LNG's balance capital allocation strategy results in a more moderate distribution increase in the near-term, we believe that this approach will enable Teekay LNG to delever its balance sheet faster, and thus maximize equity value for all of Teekay LNG's unitholders over the long-term.

In addition, in the fourth quarter Teekay LNG announced a common unit repurchase program, including the repurchase of 1.1 million common units at an average cost of $11.38 per unit to-date. And we believe that opportunistic repurchases by Teekay LNG will create further value. We're committed to creating long-term value for all unitholders, while also maximizing the benefits to Teekay parent through the incentive distribution right structure.

Lastly, Teekay LNG has provided 2019 guidance, which is significantly higher than 2018, including adjusted earnings per unit of between $1.85 and $2.20, up 143% to 190% from 2018. Total cash flow from vessel operations, which includes its proportionate share of its joint ventures of between $635 million and $660 million, up 23% to 28% from 2018 and consolidated cash flow including only those vessels consolidated in our financial statements of between $420 million and $440 million.

Turning to slide 7. Teekay Tankers reported total CFVO of $62 million, an improvement from $28 million in the prior quarter and generated adjusted net income of $14 million, or $0.05 per share, which improved from an adjusted net loss of $18 million, or $0.07 per share, in the prior quarter. Crude tanker spot rates improved significantly during the fourth quarter of 2018 spurred by both winter market seasonality and positive underlying supply and demand fundamentals. Although rates have declined recently from the highs reached at the end of 2018, our crude spot tanker rates booked in the first quarter of 2019 to-date are actually higher than the fourth quarter. Based on approximately 70% and 60% – 68% of spot revenue days booked, Teekay Tankers' first quarter to-date Suezmax and Aframax bookings have averaged approximately $26,000 and $28,500 per day respectively.

For LR2 segment with approximately 51% of spot revenues days booked, first quarter to-date bookings have averaged approximately $24,500 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 Q1 to-date levels, Teekay Tankers' estimated annual free cash flow per share would be approximately $0.85 per share over the next 12 months and at mid cycle rates its annual free cash flow would increase to over $1 per share, which we view as very attractive relative to its last closing share price of $1.06.

Since November, Teekay Tankers has completed various financing initiatives, including the previously announced sale leaseback transaction relating to four vessels and a loan to finance working capital in the company's RSA pool, which provide approximately $40 million of additional liquidity. In addition, Teekay Tankers recently signed a term sheet for an additional sale leaseback transaction for two vessels, which upon completion in the first quarter of 2019, is expected to increase liquidity by a further $25 million and extend their debt maturity profile.

Looking at slide 8. We have summarized Teekay Offshore's recent results and highlights. Teekay Offshore Partners generated adjusted EBITDA of $290 million, up from $172 million in the prior quarter and adjusted net income of $131 million, up from $12 million in the prior quarter. The increase was driven primarily by the previously announced positive settlement with Petrobras. This positive settlement of $96 million, of which $55 million was received in the fourth quarter, resulted in the recognition of $91 million of revenue in the fourth quarter.

Lastly, in January, Teekay Offshore secured a contract extension to extend the employment of the Piranema Spirit FPSO on its Brazilian field by up to three years commencing in February 2019.

I'd like to finish the call today on slide 9, which I won't touch on in detail, because we presented a similar slide in November last year. We're making steady progress toward 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're now available to take questions.

Operator: Thank you. If you would like to ask a question, please signal by pressing star one on your telephone keypad. If you're using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, that is star one to ask a question. We will now take our first question from Nick Covich[?]. Please go ahead.

Nick Covich: Good afternoon. I wanted to follow-up with management. The industry has experienced a lot of changes over the last several years, and one of the things that many companies have done relates to corporate structure, and I know you changed Teekay LNG from a K1 MLP to a C-Corp MLP. Could you address one of the trends in the industry and that's the collapse of the IDR structure, and I wonder what management's intentions are on that topic. And is that something that might be addressed at the, I guess, June investor meeting? Thank you.

Vincent Lok: Yeah, this is Vince here. I mean, we're always looking at ways to optimize our corporate structure. And you're right, I think, the decision to move TGP from a K1 to 1099 is a good move to especially attract larger institutional investors. We have been closely monitoring what's happening in the MLP space with a lot of simplification transactions that have occurred, as well as just the change in dynamics of the MLP market; so, that is something we're closely monitoring.

So, I'm not sure if we have anything specific to report in June, but it's sort of an evolving thing that we're looking at. But even though we do have these four public companies, I think one important thing is that we still really managed the company as one. So, we are an operating company, and there's a lot of synergies that occur when you look at the Teekay Group in terms of way we manage it.

We are looking at number of ways where we can be more efficient and sort of simplify things even without any changes to the structure. But it is something that we're always looking at.

Nick Covich: Okay, thank you very much.

Operator: Once again, if you would like to ask a question, please signal by pressing star followed by the one on your telephone keypad. We will now take our next question from James Lardakis. Please go ahead. Your line is now open.

James Lardakis: Hello. I was wondering about Teekay Tankers. With all the incoming free cash flow and everything turning around, will that be used for buybacks and to payback what is owed for TIL's merger? Also, what do you think about analyst estimates going up so high 1400%? Should it be a bit conservative, or I'm not sure.

Vince Lok: Well, yeah, there was – Teekay Tankers just finished their earnings call about an hour ago. But I'll just maybe echo some of the comments they made. We did see a significant improvement in the earnings in Teekay Tankers and we're very positive on the outlook for that, the tanker market heading into the second half of 2019 and 2020. Teekay Tankers' balance sheet is – I would say their leverage is elevated at this point in time. But that does give a lot of financial leverage and operating leverage into a recovering tanker market.

I think in the near-term, it's prudent for Teekay Tankers to continue to strengthen the balance sheet, pay down some debt and accrue some equity value in the meantime. But in longer term, I think there is obviously some ability to return capital to shareholders in the form of dividends or share buybacks, depending on where Teekay Tankers shares are trading at at the time.

James Lardakis: Thank you. Thank you. I really appreciate it.

Vince Lok: Welcome.

Operator: It appears we have no further questions at this time. I'd now like to turn the call back over to Kenneth Hvid for any additional or closing remarks.

Kenneth Hvid: Well, thank you for listening in today. We had extensive Q&A sessions at our daughter calls earlier this morning, so I believe we've answered most of the questions here. Thank you.

Operator: This concludes today's conference call. You may now disconnect.