TEEKAY LNG PARTNERS' FIRST QUARTER 2018 EARNINGS RESULTS COFERENCE CALL

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

Moderator: **Emily Yee**

Date: **Thursday, 18 May 2018**

Conference Time: **11:00 ET**

Operator: Welcome to Teekay LNG Partners First 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 introduction, I would like to turn the call over to Mr Mark Kremin, Teekay Gas Group's President and Chief Executive Officer. Please go ahead, sir.

Scott Gayton: Before Mark begins, I would like to direct all participants to our website at www.teekaylng.com where you'll find a copy of the first quarter 2018 earnings presentation. Mark Kremin and Brody Speers will review this presentation during today's conference call.

Please allow me to remind you that our discussion today contains forward-looking statements. Actual results may differ materially from results projected by those forward-looking statements. Additional information concerning factors that could cause actual results to materially differ from those in the forward-looking statements is contained in the first quarter 2018 earnings release and earnings presentation available on our website.

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

Mark Kremin: Thank you, Scott. Good morning, everyone, and thank you for joining us on the first quarter 2018 investor conference call for Teekay LNG Partners. I'm joined today by Brody Speers, Teekay Gas Group's CFO.

Turning to Slide 3 of the presentation, I will review some of Teekay LNG's recent highlights. For the first quarter of 2018, the Partnership generated total cash flow from vessel operations, or CFVO, of approximately $118 million and distributable cash flow, or DCF, of approximately $35 million, resulting in DCF for limited partner unit of $0.44.

Our GAAP earnings were impacted by certain non-recurring items, the most material of which is a tax indemnification provision we have now made due to a determination for additional lease rentals from the lessor of our three 70%-owned RasGas II joint venture vessels.

As its customary for these types of lease arrangements, our RasGas II joint venture had guaranteed that the economics to the lessor would be maintained, should the underlying tax rules change. This resulted in an additional tax indemnification guarantee liability of $53 million during the quarter, in addition to the $12.6 million that had previously been accrued. Although Teekay LNG owns a 70% interest in these vessels, we consolidate this joint venture for accounting purposes and thus show 100% of this liability on our financial statements.

Additionally, I think it's important to note that the total liability of $65.6 million on a 100% basis is approximately equal to the upfront benefit our joint venture received upon entering into the lease in 2006.

We were also active during the quarter, securing three important charters for contract rollovers the Partnership was facing in 2018. Two of these, the Arctic Spirit and Polar Spirit, which were recently redelivered from Teekay Corporation to Teekay LNG, as scheduled, were rechartered to Petronas for four years and for nine months, respectively, to service niche trades in China. Importantly, these charters will ensure these two specialised vessels are fully utilised at charter rates that are above the current spot market assessment for larger modern LNG vessels.

In addition, the charter on the Torben Spirit MEGI LNG carrier was extended out to December 2018 at an increased rate and positions this vessel to take advantage of a potentially strong market in early 2019 on the back of strong Chinese imports similar to the second half of 2017 and into 2018.

And, as you will hear from me later, we continue to execute on our newbuilding programme and are in the early innings of significant cash flow growth. Our seventh newbuilding delivery in as many months, the Marina, delivered last week onto its long-term contract with Shell. And we expect another 11 LNG carriers, plus the Bahrain regasification terminal, to deliver between now and early 2020. In total, and including the LNG carrier deliveries starting in October 2017, our LNG newbuilding order book is expected to provide Teekay LNG with $310 million of incremental cash flows annually.

Slide 4 is a visual representation of our existing LNG fleet, updated for our recent charters and excluding the recently delivered and soon-to-be delivered new builds, which are depicted on the next slide. We think there are three key takeaways from this slide that help to differentiate us from our peers. First is the length of our contracts with roughly half of them with more than ten years remaining. Second is the contract laddering we have been able to achieve with very few contracts expiring concurrently, especially over the next six to seven years. And third is the diverse portfolio of customers, with most of them being household names in the gas space.

We have shown Slide 5 before and similar to the previous slide, the majority of contracts on our newbuilding portfolio extend well into the future. And our contracts are with blue chip charters, including

Shell, BP and the Yamal consortium led by Novatek, Total and CNPC. Also, once our entire new build book has delivered in 2020, we will have a young LNG fleet with an average age of just over eight years.

Turning to Slide 6, we look at the fundamentals in the LNG market. We see strong supply in demand fundamentals in the LNG market through the remainder of this decade and longer term, which we expect will translate into a significant increase in global LNG shipping and demand for new LNG vessels. In 2017, global LNG imports increased by approximately 10% compared to the previous year, which was the strongest growth since 2010 according to the International Group of Liquefied Natural Gas Importers. Partly as a result, utilisation of the LNG carrier fleet increased and short-term charter rates for LNG vessels reached a four-year high in December 2017. Although rates have since declined seasonally, average rates in the first quarter of 2018 remained 60% higher compared to a year earlier, which indicates a much tighter fleet balance, which we expect will continue to support charter rates in the coming years.

On the liquefaction side, it is encouraging to see several export projects progressing towards final investment decisions. For example, Cheniere recently announced that they intend to make a final investment decision on a third train at their Corpus Christi LNG export project in the next few weeks. This project and many others will be needed in the years ahead to fill the gap between the supplied LNG from current – excuse me – from export projects currently in operation and construction and the growing long-term global demand for LNG. In the longer term, this growing demand for LNG is expected to result in a doubling of global LNG imports by 2040, according to BP.

To accommodate this growth in LNG trade, the industry will require a significant investment in new LNG vessels. For example, the International Energy Agency estimates that approximately 220 additional LNG vessels will be needed on top of the current order book by 2030. With a leading position as one of the world's largest LNG carrier owners and operators, Teekay LNG is well positioned to benefit from this strong long-term growth in the LNG industry.

Turning to Slide 7, we take a look at the growing role of China in the LNG market. Over the past decade, China's influence in the global LNG market has increased rapidly. In 2010, China was the seventh largest LNG importer in the world, consuming less than 5% of global LNG imports. However, China's LNG imports has since increased at a cumulative average growth rate of approximately 22% per year. And in 2017, China surpassed South Korea to become the world's second largest LNG importer. In fact, over the past two years, China has been responsible for roughly 40% of the total net growth in global LNG imports. We expect that China will continue to increase its share of the global LNG market. By 2030, BP expects that China will be responsible for almost 20% of global LNG imports and will be importing more LNG than Japan does today.

In 2017, 14 vessels in Teekay LNG's fleet delivered a total of 2 million tons of LNG to China, which is approximately 5% of China's total LNG imports. Our recent charter contracts for the Arctic Spirit and Polar Spirit, combined with our existing share of LNG deliveries to China, positioned Teekay LNG to capitalise on China's long-term growth in the LNG market.

And I'd like to end today on Slide 8. We believe Teekay LNG is at an inflection point, as we continue to execute on our new building projects and financings, and are in the early innings of significant cash flow growth, which will create long-term value for our unit holders.

I'm going to finish up today's presentation by digging into each of the key steps that we see contributing additional value for our unit holders. For the last few years, we had been focused on execution, both on securing financing for our new builds, delivering the vessels on schedule, and managing our ongoing re-financings. We have now substantially financed our new building order book, which at this time last year, stood at 18 LNG carriers. Our final unfinanced LNG vessel, the Yamal Spirit, which delivers in 2019, is expected to be financed within the second half of 2018.

Finally, we have made excellent progress this year on our 2018 re-financings, with two re-financings already completed, and two more expected to be completed by the time we report Q2 results in early August.

We have taken delivery of seven LNG carrier newbuilding vessels in the past seven months on top of two mid-sized LPG carrier newbuilding deliveries during the same period, including one mid-sized LPG carrier to be delivered next week. This has taken in an inordinate amount of effort across the organisation, and I'm proud of how everyone has stepped up during this critical time. We have many more ships to deliver onto contract, and I have no doubt they will deliver on time and on budget like those that have come before them.

Importantly, and as I have mentioned previously during this call, for just the LNG fleet and regas[?] terminal, we expect TGP to generate approximately $310 million of additional annual fixed-rate cash flow from our new building order book. However, this cash flow will not be fully realised until all the newbuildings have delivered right out to the final arc seven in early 2020.

This cash flow growth, which is all backed by long-term contracts, is coming and it will create value for our unit holders. It is worth noting that this order book will have been financed through new debt and leasing facilities, two preferred equity offerings and retained earnings, and without issuing any common units since July 2014.

Next, we intend to maintain a balanced financial strategy that allows us to de-lever our balance sheet, return capital to unit holders, and continue to service our customers' growing needs in the LNG space. Unlike many other marine MLPs, TGP has warehoused its entire order book and its own balance sheet in the form of pre-delivery yard payments.

The benefits that the vessels are required at the actual contracted price with the shipyards has provided TGP with an attractive portfolio of multi-year, built-in growth. However, since the vessels do not generate cash flow until they deliver, this has resulted in temporarily elevating our credit metrics. As of 31st March 2018, our balance sheet leverage stood at approximately eight times net debt to CFVO, taking into account a proportionate share of our equity accounted joint ventures. Normalising for the over $800 million dollars in newbuilding instalments that are not currently generating cash flow, our leverage sits at approximately 6.5 times as of 31st March, which is still above our long-term target leverage of approximately 5.5 times CFVO. Given the fixed-rate nature of our forward cash flows, our balance sheet will naturally de-lever over the next few years as our projects deliver and generate cash flow.

Given the size and predictability of our projected cash flow growth, we believe that we will have the capacity to naturally de-lever our balance sheet, return capital to unit holders, and grow accretively, which will all contribute to building long-term value for Teekay LNG and its unit holders.

And finally, as I discussed on Slide six and seven, we believe the short- and longer-term fundamentals for the LNG shipping industry are strong and likely to strengthen further. China will be a big driver of this growth, and we are well positioned to service this and other growing markets to our operational expertise, scale, and our strengthening financial position. This strong underlying market backdrop and need for more LNG vessel orders will create new opportunities for Teekay LNG.

Operator, we are 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. Again, press star one to ask a question. If you're using a speakerphone, please make sure your mute function turned off to allow your signal to reach our equipment. We'll pause for just a moment to allow everyone an opportunity to signal for questions.

And we'll take our first question from Randy Giveans with Jefferies.

Randy Giveans: Hey, thanks, operator, and good call, guys. So just two quick questions. In the past, you provided a slide showing the remaining CAPEX and the completed kind of undrawn debt financing against that. So for example, at the end of 4Q 2017, you had $1.9 billion remaining CAPEX, $1.7 billion in completed, undrawn debt re-financing I think another almost $200 million in process debt financing. So can you provide an update for those amounts at the end of 1Q on the remaining CAPEX, and then the kind of completed financings against this?

Brody Speers: Hey, Randy. Yeah, at the end of Q1 we had approximately $1.5 billion of remaining CAPEX for our committed order book, and we had financing placed for just over $1.3 billion of that, and we have in process debt financing for just under $200 million. So between the in-process financings and the committed financings, roughly the entire remaining CAPEX was financed.

Randy Giveans: Okay. Then you made some comments there saying about eight times net debt to CFVO, but on an adjusted, kind of go-forward basis, that's closer to 6.5 times net debt, currently. Long-term target of 5.5 times. So is that kind of what you expect distribution increases to commence once you kind of get to that long-term run rate of 5.5 times maybe sooner, maybe later? Just trying to get a little timeframe or benchmark per se for when that distribution increases could possibly come.

Brody Speers: Yeah. I think in terms of any distribution guidance, as we've guided in previous quarters, we expect to provide more details on that in the second half of this year. I think more specifically we can say now that's likely to be in Q4 of this year.

In terms of our target leverage and achieving that target leverage, you know, as Mark mentioned in his prepared remarks, we are aware, having seen a lot of advances on newbuildings for the order book, which is, you know, temporarily increasing our leveraging. As these vessels begin to deliver in cash flow, we expect our leverage to naturally decreased. So we think a natural de-levering process is going to occur over the next two years and we think ultimately we can achieve our target of around 5.5 times kind of by the end of the period when these newbuildings deliver. But we don't necessarily need to wait for that to address the distribution policy. We expect to be able to do both at the same time.

Randy Giveans: Sure. Okay, and last question, have you seen any kind of moves – obviously, the short term rates have gone all over the place from $80,000 plus in December, January, in February, down to $30,000, kind of [inaudible] range[?] talking. Now recently, kind of upticking to the low 40s or so. Have you seen any movement in the three, five, seven-year time charters kind of coinciding with those?

Mark Kremin: Not so much yet. We've seen an extraordinary amount of moves in multi-month, multiyear not so much. But multi-month from the likes of GDF and BP as Exxon Mobil, Cheniere, a lot of folks have done multi-month. It hasn't necessarily moved voyage rates yet, I think it will, in a nice way, in second half. But hopefully that answer your question, not the multiyear but a lot of multi-month.

Randy Giveans: Yeah, sure, a lot of people are trying to cover, you know, 2018, 2019 winter and maybe another 2019, 2020 winter. So it makes sense. That's it from me. Thanks again. Good quarter.

Operator: And we'll take our next question from Fotis Giannakoulis with Morgan Stanley.

Fotis Giannakoulis: Yes, hi, everyone. Can you give us some details about the refinancing of the five LPG carriers and the financing of these two additional vessels that were added in the collateral package? What is the balloon of this $90 million facility?

Brody Speers: Hi, Fotis. Yeah, that financing, we just closed it last week. It's a six-year financing for the seven LPG vessels you mentioned and it got a balloon at the end of the six years of approximately $25 million.

Fotis Giannakoulis: For all the vessels?

Brody Speers: Yes, that's right.

Fotis Giannakoulis: Okay. That's it. I don't have any other questions. Thank you.

Operator: It appears there are no further questions at this time. Mr Mark Kremin, I'd like to turn the conference back to you for any additional or closing remarks.

Mark Kremin: Well, thank you. I'd like to thank everyone for the support. I look forward seeing many of you in New York City next month, and in the meantime, have a great day. So thank you very much and good-bye.

Operator: This concludes today's call. Thank you for your participation. You may now disconnect.