TEEKAY CORPORATION'S FIRST QUARTER EARNINGS RESULTS CONFERENCE CALL

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

Moderator: **Emily Yee**

Date: **Thursday, 17th May 2018**

Conference Time: **14:00 ET**

Operator: Welcome to Teekay Corporation's First Quarter 2018 Earnings Results Conference Call. During the call, all participants will be in 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. And 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, sir.

Ryan Hamilton: Before we begin, I'd like to direct all participants to our website at www.teekay.com where you will find a copy of the first quarter 2018 earnings presentation. Kenneth 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 Kenneth to begin.

Kenneth Hvid: Thank you, Ryan. And thank you all for joining us today for Teekay Corporation's first quarter 2018 earnings conference call. I'm joined this morning by our CFO, Vince Lok.

Starting with slide three of the presentation. In the first quarter, Teekay Corporation generated total consolidated cash flow from vessel operations, or CFVO, of approximately $168 million and a consolidated adjusted net loss of approximately $18 million or $0.19 per share. This is a significant improvement from the same period last year. The result was primarily driven by higher cash flows from Teekay Parent's three directly owned FPSO units that have upside exposure to oil prices and production volume, as well as the delivery and contract start-up of several growth projects across the group.

Our stronger results were partially offset by weaker crude tanker rates. As a reminder, since we deconsolidated Teekay Offshore on 25th September of last year, our consolidated CFVO in the first 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 $310 million in the first quarter of 2018 compared to $275 million in the first quarter of 2017.

Lastly, it is important to note, as a result of adopting the new revenue accounting standard in the first quarter of 2018, we were required to gross-up certain revenues and expenses, resulting in an increase of approximately $61 million in voyage expenses and approximately $14 million in vessel operating expenses in the first quarter of 2018. But this had no impact on the bottom line since revenues increased by the same amounts. In addition, consistent with prior first quarters, we experienced higher G&A during the quarter due to timing of recognition of certain equity-based compensation which is typically expensed in the first quarter of each year.

Also in the quarter, Teekay Parent generated adjusted CFVO of approximately $13 million, which includes CFVO from our directly owned assets and cash dividends and distributions from our publicly traded daughter entities. Teekay Parent CFVO also significantly improved compared to the prior year's first quarter, due primarily to higher cash flows from our three FPSO units, as I just mentioned.

As of 31st March, Teekay Parent had total liquidity of approximately $480 million, which provides us with flexibility and optionality as we are evaluating our options and the best path for addressing our January 2020 bond maturity. I'll just briefly review the next three slides on our daughter entities as I will assume most of you listened in to their respective earnings calls earlier today.

On slide four, we have summarised Teekay LNG's recent results and highlights, and the status of its growth projects. Teekay LNG Partners generated total CFVO of approximately $118 million and distributable cash flow or DCF of approximately $35 million, resulting in DCF per limited partner unit of $0.44 and a coverage ratio of approximately 3.11 times.

Teekay LNG's results include certain non-recurring items relating to a tax indemnification guarantee liability and lower utilisation on some of its mid-sized LPG carriers as they transition into TGP's new Teekay multi-gas pool. Despite these items, the partnership continues to generate stable cash flows that we expect will grow as newbuildings deliver over the next couple of years.

Since the beginning of the year, Teekay LNG has taken delivery of four LNG carriers, all on to long-term contracts, and a mid-sized LPG carrier. Looking ahead, we believe TGP is in the early innings of a multi-year cash flow ramp up with an additional 11 LNG carriers and a regasification facility scheduled to start up through to early 2020.

Teekay LNG is different from other marine MLPs as it has warehoused its entire order book on its own balance sheet and funded it mostly through retained earnings over the past two and a half years. Although this has temporarily elevated Teekay LNG's financial leverage, the benefits are that the vessels are acquired at the actual contracted price with the shipyard. So, the value creation ramps up as Teekay LNG naturally delevers its balance sheet since a significant amount of the incremental $310 million of CFVO expected to be generated from all of LNG projects has not yet been reflected in our financial statements.

Our LNG team was active on the chartering front as well. We secured charters on the Arctic and Polar Spirit LNG carriers and extended the charter on the Torben Spirit LNG carrier. With the financing of our newbuilding programme virtually completed, Teekay LNG is also executing on its refinancings. Recently, Teekay LNG refinanced a 2018 maturity with a new six-year long-term debt facility secured by seven of the ex-Skaugen LPG vessels.

Turning to slide five, Teekay Tankers reported total CFVO of approximately $22 million and an adjusted net loss of approximately $22 million or $0.08 per share. OPEC supply cuts and an oversupply of tanker tonnage continued to weigh on crude tanker rates during the first quarter. While we expect the tanker markets to remain under pressure in the near term, we remain encouraged by the significant increase in tanker scrapping and strong oil demand forecasted through to the end of this year and into 2019, which, in combination with more moderate fleet growth, should lead to an improving market during the latter part of 2018 and into 2019.

Since reporting earnings in February, TNK continues to take proactive steps to further strengthen its balance sheet and liquidity position, most recently signing a term sheet for a sale leaseback financing which is expected to improve liquidity by approximately $36 million. In addition, TNK eliminated its minimum quarterly dividend to preserve liquidity in this weak tanker market. However, it maintained the variable portion of its dividend policy which is linked to earnings.

With significant operating leverage, we believe TNK has considerable upside from a cash flow and valuation perspective when the tanker market strengthens. As the chart at the top right of the slide depicts, if Aframax reverts back even to just mid-cycle levels of $25,000 per day, we believe that TNK can generate approximately $1 per share in free cash flow, roughly equal to TNK's current share price.

Looking at slide six, we have summarised Teekay Offshore's recent results and highlights and the status of its growth projects. Teekay Offshore Partners generated total CFVO of approximately $162 million and DCF of approximately $39 million, resulting in DCF per limited partner unit of $0.10. With the recent start up of the Petrojarl I FPSO and the East Coast of Canada shuttle tanker newbuilding, TOO has now completed all of its near-term offshore growth projects, which will also allow Teekay Offshore to naturally delever its balance sheet. TOO also completed the previously announced contract extension for the Voyager Spirit FPSO.

As can be seen on the right-hand side of this slide, over the course of the last eight months, all of TOO's near-term growth projects have now delivered, which are expected to generate approximately $200 million of annual cash flow from vessel operations, some of which has not yet been fully reflected in its financial results.

Turning to slide seven. Teekay Parent is at a positive inflection point with growing adjusted CFVO driven by recent contracts on the Banff and Hummingbird Spirit FPSO units, linked to oil prices and production, as well as the redelivery of our last in-chartered LNG and conventional tanker assets, partially offset by the reduction in dividends from TNK.

In addition, Teekay Parent continues to strengthen its balance sheet with the completion of our capital market transactions in January of this year and our remaining FPSO units now on more favourable contracts, which opens up strategic options for the future of these units.

In the appendix to this presentation, we have provided some guidance on our second quarter results as well as projected CFVO from the three FPSOs at different oil prices. You will notice that the Banff FPSO has some scheduled maintenance during the second quarter, which we have quantified the impact of.

Wrapping up on slide eight. As captured in the recent headlines on this slide, we believe we're in the early innings of a broader energy market recovery, with crude oil prices reaching a four-year high of $80 per barrel today. At $80 per barrel, oil companies are making even more free cash flow than they were when oil was at $100 in 2014. This is a positive as it clearly stimulates our customer's investment appetite in oil and gas production assets, which is obviously good for all the businesses that Teekay is in.

On the LNG side, global LNG demand is anticipated to grow 25% by 2020 and 70% by 2030, which amongst others is led by China who took over as the second largest LNG importer last year behind Japan. Moreover, and based on recent forecasts, China is expected to become the largest LNG importer by 2030. In addition, we also saw the highest LNG spot tanker rates in three years earlier this year.

On the offshore side, we are already starting to see investments on the exploration side with record interest in both Brazil pre-salt auctions and Norway oil exploration licenses.

On the tanker side, as mentioned earlier, we remain encouraged by high levels of tanker scrapping, which hit the highest level since the early 1980s, as well as strong oil demand growth. Having focused on the execution and financing of our sizeable Teekay Group project portfolio over the past two years, we are now starting to see these projects deliver and generate cash flow, which will further strengthen our balance sheet as we naturally delever, ultimately leading to a lower cost of capital.

With market leading positions, strong operating platforms and stronger financial foundations, we believe Teekay Group is well positioned to benefit from a broader energy market recovery.

With that 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. If you're using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, press star one to ask a question. And we'll pause for just a moment to allow everyone an opportunity to signal for questions. Your first question comes from the line of Fotis Giannakoulis of Morgan Stanley. Please go ahead.

Fotis Giannakoulis: Yes. Hi, gentlemen, and thank you. I want to ask about the FPSOs that you have and how do you view the three FPSOs that you have at the parent level, the renewal or the extension or the potential extension of the charters, starting of course from the Banff, that comes off contract this year. But also the other two that they are − they still have another couple of years of contracts.

Kenneth Hvid: Yeah, hi, Fotis. Thanks for that question and since you've been on every quarter here, you will notice what a difference a year makes here. Of course, all of the three assets are in a much more interesting position today. First of all, our customers are really making very good money on the assets which is always a good starting point.

So, if you take the Hummingbird Spirit, as we've mentioned on previous calls, our customer did a fairly large production, drilling campaign and that's going really well. The production is up and we, as we mentioned on the last call, are benefiting from the upside, both on volume but also because we agreed to an oil price tariff.

On Banff, we hope next quarter to report on what the new contract structure is for that unit. As you correctly pointed out, we have earlier indicated that the contract was ending in 2018. There is actually an evergreen mechanism in the contract. And at the moment the field is producing a lot of gas and a fair bit of oil still. And in this environment, we are, I would say, in very good contractual talks about − that it makes it a lot of sense to keep the Banff on the field producing. So, I can't share the economic details on it on this call but we hope to be able to share that soon.

On Foinaven, I think we're producing around 25,000 barrels per day at the moment. So, needless to say that this is a very profitable asset in the BP portfolio. And as we've said earlier, the production profile is quite long on that field still. So, we have a number of years.

So, all in all, I think what we are seeing happening here is really that of course these assets, it makes a big difference whether you're sitting at $45 or $80 as we hit on Brent today, right? And that is basically doing a couple of things for us. First of all, it's extending where it makes sense at current production volumes, but also it is actually stimulating the customer's interest in potentially doing more production drilling on the existing field so that they can prolong it. And thirdly, of course, it's really − we're still getting the interest from other companies that of course have fields where these units could be used as production units. So, all in all, just a very constructive environment that we're in at the moment.

Fotis Giannakoulis: Thank you for that. That's very helpful. How do you view, long term, the ownership of these three assets? In the previous environment, there were plans of selling these assets to Teekay Offshore. Now, the control of Teekay Offshore has passed to Brookfield. I'm wondering, is there still a plan, now that the oil market is in recovery phase, to potentially sell these assets to Teekay Offshore or even a third party and become a company with no physical assets at the parent level?

Kenneth Hvid: Yeah. And again, thanks also for that question. It's a great question for us because, as you rightfully pointed out, Teekay's focus has been basically to sell off or drop down the assets that we own at the parent level. And as we noted in our prepared remarks here, last year we redelivered our last two conventional tankers. Earlier this year, we redelivered our two only LNG carriers.

So, what we have remaining is the three FPSOs. And what we've always said was that we're not prepared to do a fire sale on these assets, which we would have had to do in the oil environment that we've been in. So, where we're sitting now, the assets are obviously a lot more valuable than they were a year ago and we are therefore considering our strategic options.

TOO has, of course – and we have an omnibus agreement where they always will get a first look. And we are of course looking at these assets long term, which markets do they long term fit into. If they are going to fit into Teekay Offshore core markets, which is in the North Sea and Brazil, then we would expect to have a conversation with them. But it could also be that these assets, post their current contracts, at least a couple of them, that there may be other markets which are not core to Teekay. So, we would, from a Teekay point of view, just naturally look at maximising the value of the assets.

Fotis Giannakoulis: And given the fact that these assets, it's only a very small component of the group and the total capital deployed by the group, what are the future thoughts, because right now apart from these three assets, the parent look as a derivative play of the three daughter companies? Are there any thoughts of potentially becoming a portfolio company that would invest even in companies outside of the Teekay complex? What are the future thoughts and the purpose of Teekay Parent?

Kenneth Hvid: Well, as you know, we came into the current downturn I would say in end of 2014 here with a significant growth portfolio that we were overseeing in the group. We've been executing on that. We've been financing that. Our focus has really been on executing our projects, getting the financings done, which we have executed on over the past 18 months.

And our focus now is to continue to strengthen our balance sheet and we think that there is significant value creation upside in doing that. We have a very interesting structure, I think, in the group where we have the three daughter companies where Teekay will be in a position to dial up or dial down its investment in those three companies.

But most importantly, we have a Teekay brand, a Teekay promise to our customers and all our stakeholders out there. And we think it makes a lot of good sense to be very coordinated across the group. And we have a lot of overlap in our customer base and operational synergies, relationships with our financial institutions.

So, we very must look at running the business on a group basis. But it's correct that of course we have four listed companies. But I can tell you when the senior management team comes together here, we look at what's best for the entire group and we work together as a team.

Fotis Giannakoulis: So, does this mean that the parent will try to focus on supporting still the daughter companies, excluding potential future investment? I'm not talking about the next couple of years. I'm talking a little bit more longer term, excluding potential investments in other companies which are not part of Teekay structure, and potentially even in other sectors that are not related, perhaps dry bulk or some other sectors that you are not involved right now?

Kenneth Hvid: Yeah. No, I think − again, it's a good question, right? I mean, we clearly run the group based on decisions we need today, what we need to make in the medium term and what we need to make in the long term. And those are all conversations we're having with our board.

I'll say the decision we are making today and near term and as well as the midterm, it is very evident to us to stay very focused on our core. We think that there is a lot of value that we can generate from our core businesses. So, by enhancing the balance sheet and continuing to position us in those core markets, we actually think that there are more than enough interesting opportunities within that space.

Longer term, and then we really bring out the crystal ball, clearly, everybody is focused on the changes that our world is going through. But that is I think for future years for us to discuss. Ultimately, the Teekay Group is always focused on building a sustainable company that's going to be around for the next 100 years. And one thing is for sure, the world will look different a 100 years from now or even 30 years from now and we'll be there and figure out what services that we'll be delivering at that time.

But in the near term and to the medium term, we see an enormous need for transportation of oil and gas, which is the business that we're in and that's what we're going to be focused on.

Fotis Giannakoulis: Thank you. I appreciate your answer. Thank you.

Kenneth Hvid: Thanks.

Operator: We have no further questions at this time. I'd like to hand it back over to Mr Hvid for closing remarks.

Kenneth Hvid: Although not reflected in our share price volatility this morning, management is excited about the significant project execution and financings undertaken over the past 18 months and believe that we are well set up to, again, create values to all our shareholders in a recovering energy market. And with that, we look forward to reporting back to you next quarter. Thanks for listening today.

Operator: That concludes today's call. We thank you for your participation. You may now disconnect your lines and have a wonderful day everyone.