TEEKAY TANKERS LTD.'S THIRD QUARTER 2020 EARNINGS RESULTS CONFERENCE CALL

Company: Teekay Tankers Ltd.

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Conference Time: 12:00 ET

Operator: Welcome to Teekay Tankers Ltd's Third Quarter 2020 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-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 now like to turn the call over to the company. Please go ahead.

Ryan Hamilton: Before Kevin begins, I'd like to direct all participants to our website at www.teekaytankers.com, where you'll find a copy of the third quarter 2020 earnings presentation. Kevin and Stewart 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 2020 earnings release and earnings presentation available on our website.

I'll now turn the call over to Kevin Mackay, Teekay Tankers' President and CEO to begin.

Kevin Mackay: Thank you, Ryan. Hello, everyone. Thank you very much for joining us today for Teekay Tankers' Third Quarter 2020 Earnings Conference Call. And I hope you and your families are all safe and healthy. Joining me on the call today are Stewart Andrade, Teekay Tankers' CFO and Christian Waldegrave, Director of Research.

Moving to our recent highlights on slide 3 of the presentation, Teekay Tankers generated total adjusted EBITDA of approximately $46 million during the third quarter, an increase of $18 million from the same period of the prior year. We reported adjusted net income of approximately $3 million or $0.09 per share in the third quarter, up from an adjusted net loss of $21 million or a loss of $0.63 per share in the third quarter of 2019.

Our improved results are largely due to higher revenues from several lucrative fixed rate charters secured during periods of market strength at rates substantially higher than the third quarter spot rates.

We have continued to build financial strength this quarter generating free cash flow from operations of $31 million. Net debt has been reduced by nearly $50 million to $502 million and we continue to have a strong liquidity position which was $470 million at the end of the quarter. Our net debt to total capitalization declined to approximately 30% at the end of September, compared to 32% last quarter and 52% a year ago.

As mentioned in the earnings call in August, the company finalized a three-year $67 million term loan at an attractive rate to refinance a debt facility secured by four Suezmaxes that had been scheduled to mature in 2021. With the completion of this refinancing, the company does not have any debt maturities until 2023.

Lastly, as highlighted at our investor day in November 2019 and in recent quarters, one of our 2020 strategic priorities is to reduce our cost of capital. I'm pleased to report that in October, we repurchased two Aframax vessels previously under sale leasebacks for $29.6 million, reducing our exposure to this

relatively higher cost debt capital. The vessels were acquired using existing liquidity and are now unencumbered.

In the freight market, third quarter crude tanker spot rates decreased compared to the first half of this year, primarily due to knock-on effects of COVID-19 which I will touch on in more detail in the next slide. We were able to significantly mitigate the impact of these weaker rates by securing fixed rate charters for a number of our vessels during the periods of market strength, which enabled us to have 22% of our fleet on fixed rates charters in the third quarter at an average rate of $37,600 per day, well above the prevailing spot market rates.

Turning to slide 4, we look at recent developments in the spot tanker market. As mentioned, spot tanker rates declined during the third quarter of 2020 due to the continued impact on oil demand from the COVID-19 pandemic. Global oil inventories built rapidly during the first half of the year due to the large mismatch between supply and demand, leading to a sharp correction in both crude oil prices and refining margins. In response, OPEC and its partners slash production by a record 9.7 million barrels per day in May. Although they have returned two million barrels per day of production in August, global oil supply remains well below pre-pandemic levels. And this has been negative for tanker trade.

Refinery runs have also been significantly cut as refiners respond to weak margins. And this has further dampened demand for crude and hence crude transportation. At the same time, some of the ships that were placed into floating storage earlier than the year have returned to the fleet, adding to the supply demand imbalance.

Although Teekay Tankers saw a drop in earnings compared to the first half of the year, our third quarter results were higher year-on-year as shown by the chart on the left of the slide. This was particularly true for our Suezmaxes, where rates were further bolstered by the fixed rate time charters that we entered into during late 2019 and the first half of 2020 at rates much higher than current spot market.

The chart on the right of the slide shows the extent to which spot rates have fallen in recent months. Looking ahead to the winter, we are currently facing a challenging rate environment due to the fundamental headwinds that I described earlier. However, you could see some support for mid-sized tankers due to the return of Libyan crude oil exports which have a risen to around one million barrels per day, having average only around 100,000 barrels per day last quarter.

Libyan crude is predominantly moved on Aframaxes and Suezmaxes, so the return of exports could provide some support rates in the Mediterranean. Furthermore, we expect the normal winter seasonality may provide additional support later in Q4 in the form of winter heating demand and an increase in vessel delays due to bad weather.

On the flip side, the resurgence of coronavirus cases and fresh lockdowns, particularly in Europe, may weigh on demand. On the whole, we anticipate that the typical winter market strengths will be moderated compared to prior years.

Turning to slide 5. We give a summary of our fixtures in the fourth quarter of 2020 to-date. Based on approximately 49% and 45% of spot revenue days booked, Teekay Tankers fourth quarter to-date, Suezmax and Aframax bookings have averaged approximately $10,100 and $7,700 per day respectively. For our LR2 fleet, which are predominantly trading dirty based on approximately 44% and spot revenue days booked, fourth quarter to-date bookings have average approximately $8,500 per day.

Teekay Tankers has been proactive in managing its fleet by locking in attractive fixed rate charters during periods of significant strength in the tanker market over the last few quarters. As a result, the company's combined rates for fixed and spot fleet so far in Q4 have been significantly higher than current spot market rates. Our Suezmax fleet has 62% of its Q4 revenue days booked at $24,200 per day, our Aframax fleet is 54% booked, $12,400 per day and our LR2 fleet is 52% booked, $13,500 per day for the fourth quarter of 2020. For further details on our fixed rate charters, please refer to the appendix of the presentation.

Turning to slide 6. We turn to the outlook for the tanker demand over the next 12 months. Global oil demand has recovered sharply from the low point in Q2 though demand remains several million barrels per day below pre-pandemic levels. We expect demand will grow through the course of 2021, particularly during the second half of the year and this will help bring oil inventories back to more normal levels.

As shown by the chart in this slide, the oil market moved into a deficit during the third quarter and tock draws are expected to continue for the remainder of 2020 and in 2021. However, depending on the speed of the demand recovery, it may take the majority of next year to fully reverse the large build of inventories which took place in the first half of 2020.

As demand recovers and oil inventories are drawn down, we expect an improvement in refining margins, which will lead to a recovery in refinery throughput. This will create additional crude demand and give support to crude oil prices. It should then lead to higher oil production for both OPEC and non-OPEC sources. As this happens, tanker demand is expected to recover and give support to freight rates. The exact timing of this recovery, however, is uncertain and will depend to a large extent on how the coronavirus pandemic evolves next year.

We remain hopeful that a coronavirus vaccine will become widely available during 2021 and that this will accelerate a return to more normal demand patterns in the transportation and travel sectors leading to higher oil and tanker demand.

Turning to slide 7, we look at the positive fleet supply fundamentals. The outlook for fleet supply continues to be very positive due to a significantly reduced level new build ordering, diminished tanker order book and the potential for higher scrapping due to an aging tanker fleet. As of October 2020, the tanker order book totaled 47 million deadweight tons or just over 7% of the existing global fleet. When measured as a proportion of the total fleet, this is the lowest tanker order book seen in over 24 years.

Tanker scrapping has been very low over the past two years, and this has resulted in a buildup of older vessels, which face removal in the near future. As shown by the chart, the tanker fleet currently has an average age of almost 11 years, which is a 17-year high. A potential period of weaker rates in the coming months combined with balance water treatment system installations and dry dock costs could encourage higher scrapping in 2021 to help limit overall fleet growth.

Finally, new tanker ordering remains very low due to a more restrictive financial landscape and uncertainty as to what type of propulsion system to order given upcoming environmental regulations. Around 12.5 million deadweight tons has been ordered so far this year versus an average annual order rate of around 34 million deadweight tons over the past 20 years. We believe new build ordering will remain relatively low in the near future and this will help keep the order book at or near historic lows. When taken together, a combination of low ordering, a small and shrinking order book, and the potential for higher scrapping should help keep fleet growth low over the next two to three years. This will help facilitate tanker market recovery once the demand side normalizes. I'll now turn the call over to Stewart to cover the financial slide.

Stewart Andrade: Thanks, Kevin. Turning to slide 8, over the past year, Teekay Tankers has transformed its balance sheet, which provides us with financial strength to be resilient in any tanker market. Over the last 12 months, Teekay tankers has generated over $400 million of free cash flows from operations and completed over $100 million of asset sales, creating a resilient financial platform for the company. This strong free cash flow has had an enormous impact on our overall financial position, decreasing our net debt by nearly $500 million or 50% to $502 million while improving the company's liquidity position by $375 million to a total of 470 million at the end of September.

We currently have 13% of ship days on fixed rate charges for the next 12 months at an average rate of $33,500 per day, which is well above the current spot market. Our fixed rate charters combined with our almost $500 million of debt reduction and the unwinding of our sale-leasebacks has resulted in a low free cash flow breakeven for our spot fleet of approximately $13,500 per day through the end of Q3, 2021.

As Kevin mentioned in his opening remarks, we closed the refinancing of our 2021 debt maturity in August, and now have no debt maturities until 2023. We have taken steps to reduce our cost of capital by starting to unwind our sale-leasebacks with the acquisition of two vessels previously under sale-leasebacks in October. In addition, we intend to declare two more sale-leaseback purchase options later this month, which will further reduce our cost of capital when the vessels are required in May, 2021. Over the past year, we have reduced our quarterly net interest expense by $4 million or 26%.

Lastly, as shown at the bottom of the slide, having prepaid a significant amount of debt in 2020, our debt repayment profile is very manageable in the coming years. With our efforts to delever and reduce our cost of capital, along with a manageable debt repayment profile, we have positioned ourselves financially to weather potential market headwinds. With that, I will turn the call over to Kevin to conclude.

Kevin Mackay: Thanks. In closing, I would like to say thank you again this quarter to all of our seafarers and shore-based staff for their continued extraordinary efforts in bringing energy to the world with Teekay spirit during the COVID-19 pandemic. I'm extremely proud of our team for continuing to execute despite the unprecedented global challenges. Operationally, we continue to focus on the safety and wellbeing of our seafarers all the while continuing to deliver Teekay's high quality of service to our customers. Commercially, the impact of the weakness in the spot market has been mitigated by our well-time fixed rate charters. Financially, we have transformed our balance sheet over the last 12 months and have built resilient financial position.

With a strong financial foundation, a low free cash flow breakeven and our mid-sized fleet profile, we believe that Teekay Tankers is well positioned to continue to create shareholder value, even in these unprecedented and uncertain times. With that, operator, we are now available to take questions.

Operator: Thank you, sir. At this time, we'll open the floor for questions. If you'd like to ask a question, please signal by pressing star one on your telephone keypad. If you are 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, we'll pause for just a moment to allow everyone an opportunity to signal for questions. We'll take our first question. This comes from John Chappell with Evercore, your line is open, please go ahead.

John Chappell: Thank you. Good morning. Stewart, if I can start with you, you mentioned two more leases that you hope to have done by the fourth quarter. Can you give us the magnitude of those leases and then also, just to continue on that theme, what's the timeline look like into 2021 when you have the opportunity to maybe to pursue the further removal of those higher cost of capital pieces of paper?

Stewart Andrade: Hi John. Yes, so the two that we intend to exercise later this month have a total lease balance of about $58 million. And those – we would declare those in November, but we would actually acquire them in May just in terms of timing. So it's about $57, $58 million. And the rate on those is about 9%, so quite significant savings from buying those back. And then moving into 2021, by the end of 2021 actually, all the remaining 14 leases are available to us through purchase options. The various leases have different terms. Some of them have specific dates during the year when we can exercise and others are a little more flexible in terms of exercising when we'd like. But by the end of the year, the remaining – all of the remaining $367 million in leases are available. The average – the average financing cost across all of those is about 7.5% roughly, so there's quite substantial opportunity for savings.

John Chappell: Great. And then that kind of leads to my second question for both you Stewart and Kevin. You know, you guys were in New York almost a year ago to the day, laying out your plan for 2020 and certainly this year hasn't turned out like anyone would have expected, but as far as you executing your plan, it's gone probably better than you would have even hoped. What's kind of the next steps now for the next 12 months? Is it to continue to pay down those leases? Continue to bring the leverage down, you know, even further? Raise more liquidity? Do you think that now we're in this period, although uncertain, where things are about as dire as they can be and now you shift a little bit more to offense? How do you think about the path to November, 2021?

Kevin Mackay: That's a good question. And John, I think, you know, to close out this year really we're sticking to plan. It has, as you said, been a very different year than what we anticipated coming into it when we spoke to everyone in November last year. But I think we've been very successful in executing along the lines that we wanted to and as a result, I think we can – we can look forward you know, from a – from a position of strength.

However, I think, as we've mentioned in our remarks, 2021 is an uncertain year. We're not clear on the timing of the recovery. The fundamentals are there on the fleet supply side, but demand and the potential resurgence for COVID does leave question marks. So as we look to go into next year, I think we'll sit down with our board at the end of the year. We'll assess what we've managed to achieve this year and I think I'm looking forward to a robust discussion with them about what sort of plans we lay out for 2021. But at this point in time, we haven't – we haven't had that conversation yet, so come back to the market when we have further clarity and direction, given the uncertainty –

John Chappell: We should assume until that point that it just continue to delever, number one priority.

Kevin Mackay: Yeah, I think as Stewart mentioned, you know, we've got some upcoming sale-leasebacks that we'd like to eliminate and get rid of that higher cost of debt. So until that plan is finalized, should it differ from what we're doing now, we'll come back to the market.

John Chappell: Okay. Thank you, Kevin. Thanks Stewart.

Kevin Mackay: Thanks, John.

Operator: Our next question comes from Randy Giveans with Jefferies. Your line is open, please go ahead.

Randy Giveans: Hello to you, gentlemen. How's it going?

Stewart Andrade: Doing well.

Kevin Mackay: Good, thanks.

Randy Giveans: All right. Looking at your kind of operating leverage, right? Are you content with your current fleet or looking at possibly expanding it further following your debt repayments that you were kind of just alluding to and when it comes to that expansion, would it be by acquiring secondhand vessels or maybe additional time charter ins?

Kevin Mackay: Yeah. Good question, Randy. I think first and foremost, we're very comfortable with our fleet profile, both with its scale and its makeup. I think in terms of where we go from here, given where the market is given the uncertainty, I don't think you'll see us do anything in terms of further fleet building or anything of that nature, I think we've got the scale we like. We have sold some of the older assets earlier in the year, so I think where we stand now is more of a wait and see, let's figure out where this market is going, where the – when the demand recovery comes into play and take care of the sale-leaseback opportunities that we have to lower our cost of capital.

In terms of new buildings, newbuild prices have come off. It's something that we monitor as we do with the secondhand sale and purchase market and over time, those are decisions that we weigh up and compare and contrast what is the expected long-term return for either newbuilds or secondhand and to be honest with you, we're agnostic as to which one we would go after at the appropriate time. It's based on which path of growth provides the best value to shareholders and that varies during various points in a cycle. So I think for now, we're not active, we're not looking to add a lot of ships, it's more wait and see how things play out.

Randy Giveans: Okay. I guess following that, your balance sheet liquidity's clearly rapidly improving, evidenced on I guess slide 8 there. Now one thing that has been removed from slide 8 and also the appendix is your NAV calculation which was I think $28 a share at the end of 2Q. So with that, what is your current NAV today and how have secondhand Aframax and Suezmax asset values fared here in recent months?

Stewart Andrade: So we haven't actually run the NAV recently like since probably the – since last quarter, so I don't have an accurate NAV to provide but I do know that asset values certainly have been under pressure and if you look at – based on Clarkson's probably over the last quarter depending on the age of assets, they're probably down between 5% and 10%, so they're – they have been under pressure. Of course there's a lack of liquidity in the market, so there's not a lot of transactions which always makes it difficult to really know what the values are but I guess as a rough guide, probably down 5% to 10% in the last quarter and that would translate as expected into our NAV but I don't have an exact number for you.

Randy Giveans: Got it. All right, so maybe mid to low twenties at worst it sounds like.

Stewart Andrade: I think that's the right ballpark, certainly.

Randy Giveans: Well, well above $10.43, so – all right well, that's it for me. Thank you.

Operator: Our next question comes from Ken Hoexter with Bank of America. Your line is open, please go ahead.

Ken Hoexter: Hey, good afternoon. Kevin, maybe just talk a bit about where your thoughts on where storage is now the, the impact you're seeing from COVID to those spot rates. I guess ultimately just to wrap that up, when do you typically see the seasonal pickup? Is it not until Thanksgiving and you mentioned kind of a delay in that, maybe just expand on your thoughts on rates.

Kevin Mackay: Sure, Ken. With regards to the first part of your question on floating storage, it's interesting in – on the crude side of the ledger. It's really a tale of two different sort of stories, one the VLCCs and interestingly, they have maintained a fairly steady level of vessels in that play. The peak of the market, you had about 84 VLCCs and I think as of last week, there was about 87, so it's – it dropped a little bit in midsummer, then picked up again. So on the V side of the ledger is – I would say is fairly steady. Where we have seen the

declines is on the Suezmax and Aframaxes and as a relative comparison, you had over 80 Aframaxes that were in storage at the peak in May and I think now the latest figure is down sort of in the low 20's, 23, 24 at last count.

Similarly, Suezmaxes were down about 60% from where we were at the peak. So the mid-size spaces, given that cost per barrel storage on those is obviously higher than on VLCCs, those are the first classes of ships that you'd see –see unwind, and that's why I think we've seen mid-size rates on Suezmaxes come off earlier than what you saw the VLCCs come off.

In terms of the typical pickup and seasonality, a lot of it will depend on weather and we've had Q4 that have picked up earlier than now but typically you run into – when you start getting delays in places like the Bosphorus canal, you start getting the fog rolling in and out of the US Gulf, that tends to gum up the works, the logistics, especially on the Aframax but also on the Suezmaxes and that sort of eats into supply and at least puts a floor, if not bolsters the supply dynamic which we're hoping to get some off during this winter months but so far, it's been relatively benign. I think the hurricane season has extended longer than we've seen in recent years, so perhaps the fog season in the US Gulf will be a little bit delayed this year. We'll have to wait and see.

Ken Hoexter: Thanks for that. Any thoughts on moving any of the LR2s to clean vs dirty, do you view the product market as having better fundamental outlook or not?

Kevin Mackay: We are actually in the process of moving one of our LR2s, that is coming out of dry dock. We're going to move that. She has been trailing dirty and we're going to move her into the clean Asian market and we're doing that really because the cost is absolutely minimal given the fact she's coming out of dry dock. So seeing where the markets are, it's unclear which one, crude versus clean, is going to increase first. So given the fact that it wasn't going to cost us anything to do the changeover, we decided to shift some of our egss from the crude basket starting with this one ship.

So it's something that we monitor daily. Obviously, the pandemic resurgence in Europe may dry some short term storage and we felt that that might come into play over the very near term but at the moment, it's just the one ship that we're moving over and if we do do future ones, it would be on the most efficient and cost efficient way that we could possibly do it rather than just to spend a lot of money to change over with no certain prospects of demand pickup.

Ken Hoexter: And I know it's really early for my last one but obviously new I guess discussion of rules on IMO 2030 and beyond, any early read on kind of ability to adapt to those proposed targets and thoughts on costs or is it just too early days?

Kevin Mackay: It's – yeah, you're absolutely right, it is very early days but we have had a history of upgrading our fleet and putting in endcaps into our fleet to make them more efficient. We've got a very successful program around our hull coatings which has saved 2% to 3% of our fuel bill over the last several years and whether it's fitting, mewis ducts docks or propeller boss cap fins or various technical upgrades that we do to our ships when they go into dry docks, we've made some serious inroads into reducing our carbon footprint already and that's something that we'll continue to do.

Ken Hoexter: Great. Thanks for the time.

Kevin Mackay: Thanks, Ken.

Operator: This marks the end of the question-and-answer session. I would now like to turn the call back over to the company for any closing remarks.

Kevin Mackay: Thank you for joining us today and please keep yourselves and your family safe during these difficult and dangerous times. Speak to you next quarter, thank you.

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