TEEKAY TANKERS LTD.'S FOURTH QUARTER 2021 EARNINGS RESULTS CONFERENCE CALL

Company: Teekay Tankers Ltd.

Date: Thursday, February 24, 2022

Conference Time: 12:00 ET

Operator: Welcome to Teekay Tanker Ltd.'s Fourth Quarter and fiscal 2021 Earnings Results Conference Call. During the call, all participants will be in a listen-only mode. Afterwards, you'll 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 introductions, I'd like to turn the call over to the company. Please go ahead.

Ed: Before we begin, I would like to direct all participants to our website at www.teekaytankers.com where you will find a copy of the fourth quarter and annual 2021 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 can concern factors that could cause actual results to materially differ from those in the forward-looking statements is contained in the fourth quarter and annual 2021 earnings release and earnings presentation available on our website.

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

Kevin Mackay: Thank you, Ed. Hello, everyone and thank you very much for joining us today for Teekay Tankers Fourth Quarter and Annual 2021 Earnings Conference Call. Joining me on the call today are Stewart Andrade Teekay Tankers CFO, and Christian Waldegrave our Director of Research.

Moving to our recent highlights on slide three of the presentation. Teekay Tankers had an adjusted net loss of $25 million or 74 cents per share during the fourth quarter, an improvement from an adjusted net loss of $50 million or $1.48 cents per share in the prior quarter. Our improved results quarter-over-quarter were due to higher spot tanker rates. Overall, we reported a 2021 adjusted net loss of $139 million or $4.09 cents per share down from an adjusted net income of $153 million or $4.54 cents per share in 2020.

Despite a challenging year, we continue to maintain a strong liquidity deposition. We have signed two-term sheets to refinance 13 vessels with new, flexible low-cost sale-leaseback financings. These new sale-leasebacks have competitive interest rates only slightly higher than our main corporate revolver and will increase liquidity by $75 million. Including the sale of three 2004-built vessels, Teekay Tankers had a pro-forma liquidity of $246 million and a net debt to capitalization of 41% at the end of 2021. Stewart will elaborate on the new low-cost sale-leasebacks and the company's strong financial foundation later in the presentation.

In the freight market, fourth quarter spot tanker rates improved to the highest point in 2021 but remained weak on a historical basis as the Omicron variant constrained oil supply and high bunker prices emerged as near-term headwinds. Mitigating this weakness, our vessels engaged in full-service lightering were employed at $22,200 per day in the fourth quarter providing support for our Aframax rates. The company also out-chartered one Aframax for $18,000 per day for a 12-month period.

Although the near-term outlook remains uncertain, the current high asset price environment provides opportunities for proactive fleet management. We have taken advantage of the firm asset market to opportunistically sell three, 2004-built vessels since Q4 of last year for total proceeds of approximately $42 million. Looking ahead, we believe the building blocks for a tanker market recovery remain in place, which I will touch on in more detail later in the presentation.

Turning to slide four, we look at recent developments in spot tanker market. Spot tanker rates improved during the fourth quarter with Q4 being the best quarter in what was otherwise a historically weak year. Global oil demand rebounded to 100 million barrels per day in Q4 due to an increase in global mobility on economic activity as the world continues to normalize from COVID-19 disruptions, and was further boosted by a switch from gas-to-oil for power generation in parts of Europe and Asia. Global oil production also increased during the fourth quarter as the OPEC+ group continued with this policy to unwind crude oil supply cuts at a rate of 400,000 barrels per day each month.

However, rates have softened again at the start of 2022 due to a number of near-term headwinds. Firstly, oil demand was impacted in December by the emergence of the Omicron variant, particularly in Asia, and this impact has continued into the early part of 2022.

Secondly, several countries in the OPEC+ group have failed to reach their production targets in recent months, while unplanned outages in Libya, Kazakhstan, and Ecuador also tempered the supply increase. As a result, global oil supply has continued to lag demand leading to a further drawdown in global oil inventories and boosting oil prices to seven-year high of over $96 per barrel as of yesterday's close. This has led to a sharp increase in bunker fuel prices in recent weeks, leading to renewed pressure on tanker earnings so far in the first quarter of this year.

Turning to slide five, we provide a summary of our spot rates in the first quarter to date. As mentioned on the prior slide, spot tanker rates improved in the fourth quarter, which were supported by six of our vessels of employed in full-service lightering, which earned above spot voyage rates averaging $22,200 per day. In the first quarter, based on approximately 70% and 64% of revenue days booked, Teekay Tankers first quarter to date, Suezmax, and Aframax bookings have averaged approximately $10,300 per day and $13,500 per day, respectively. For our LR2 fleet based on approximately 59% of spot revenue days booked, fourth quarter to date, bookings have averaged, approximately $11,200 per day.

Turning to slide six, we look at three potential drivers of higher tanker demand. Firstly, global oil demand is projected to increase by 3.2 million barrels per day in 2022 and to average 101.6 million barrels per day by the second half of the year. This will take oil demand back above pre-COVID levels as shown by the chart on the left of the page. The emergence of the Omicron variant could temporarily slow the demand recovery though it is not expected to derail the 2022 recovery scenario as the fast spread of Omicron and accelerated vaccination rates should lead to increased population immunity through the year. We do, however, acknowledge that further variants could arise during the year, which may impact mobility and therefore oil demand, depending on the severity of the outbreak.

Secondly, global oil production is set to increase significantly this year as the OPEC+ group plans to unwind its remaining supply cuts by September, while non-OPEC production is set to increase due to higher supply from the US, Canada, and Brazil. According to the IEA, global oil supply could increase by up to 6.3 million barrels per day in 2022, if all supply comes online as planned. This would provide a significant boost to crude tanker demand through the course of the year. However, there is a degree of uncertainty in this forecast as OPEC+ output is currently lagging behind its production targets by around 900,000 barrels per day, and OPEC+ would therefore need to find ways to make up for that shortfall through the course of the year.

Thirdly, as shown by the chart on the right, oil inventories declined rapidly during the course of 2021, and currently stand at a seven-year low. Global oil supply is expected to outpace oil demand during the year leading to a replenishment of global oil inventories. This should help flatten the current steep backwardation in the oil price futures curve, which disincentivizes refiners from holding excess stock. A rebuilding of inventories would increase tanker demand and should offer some relief to high oil and bunker prices.

Finally, we must acknowledge some of the wildcards, which have the potential to change oil and tanker market dynamics during the course of the year. The first is the Russia-Ukraine situation, which in recent hours has escalated to full-blown military conflict. As the situation develops and Western power react with threatened sanctions, the full impact on oil and tanker flows remains uncertain.

TEEKAY

The second is Iran and the potential of lifting sanctions. Although this outcome is still far from certain, a lifting of sanctions would in our view, be positive for the tanker market, both in terms of providing more seaborne oil trade volumes, and in helping to shrink the fleet of ships currently employed in sanctioned trades.

Turning to slide seven, we look at fleet potential drivers of low tanker fleet growth. Tanker fleet supply fundamentals continue to look very positive due to a lack of newbuilding ordering, a diminishing tanker orderbook, and an aging tanker fleet. Firstly, as shown by the chart on the left, the tanker orderbook currently stands at 7% of the existing fleet size, which is the lowest since 1996 and well below the long-term average of around 20%.

Secondly, the level of newbuild orders has slowed to a trickle in recent months with just 3.4 million deadweight tons of orders placed in the second half of 2021, the lowest level of new orders placed in a six-month period since the first half of 2009. We expect the level of new tanker orders will remain low in the near term due to high newbuild prices, which are currently at a 12-year high, and a lack of shipyard space due to record levels of containership and LNG carrier orders. According to our estimates, the major shipyards capable of building large tankers are generally full through 2024 and have already filled around 40% of capacity for 2025 deliveries.

Finally, the world tanker fleet is aging with a large number of ships due to reach age 20 in the coming years. As shown by the chart on the right, the number of ships reaching age 20 in the mid-sized sector far outweighs the number of newbuild deliveries in both 2023 and 2024. Although it is not expected that all vessels reaching age 20 will be scrapped immediately, we believe that the combination of weak freight rates in recent quarters, high current scrap prices, and the impact of upcoming environmental regulations should lead to an acceleration in scrapping overall. Our current forecast is for around 2% tanker fleet growth this year followed by less than 1% in 2023 and potentially negative fleet growth in 2024 when ship removals are expected to exceed new tanker deliveries.

To sum up, we anticipate that tanker spot rates will recover from the multi-decade lows seen in 2021, as both oil demand and supply are expected to revert to and then surpass pre-COVID levels during the course of this year. A significant increase in oil supply from both OPEC+ and non-OPEC sources is expected to be the main catalyst behind the recovery. However, the actual timing of this recovery remains uncertain, and we may continue to see periods of weak tanker rates in coming quarters before a more sustained recovery fully takes hold. The outlook for 2023 and 2024 is more positive and very low levels of tanker fleet growth and a continued recovery in all demand are expected to lead to higher tanker fleet utilization and therefore, improve spot rates.

I'll now turn the call over to Stewart to cover the financial slide.

Stewart Andrade: Thanks, Kevin. Turning to slide eight, we highlight the company's strengthened financial foundation. As Kevin mentioned in his opening remarks, we continue to maintain a strong liquidity position. The company has proforma liquidity of $246 million at the end of the fourth quarter, which provides financial resilience in this weak freight market. I'm pleased to announce that we have signed term sheets to refinance 13 vessels with low-cost sale-leaseback financings. These financings increase liquidity by $75 million while also extending our debt repayment profile. Importantly, we retain flexibility through purchase options, which can be exercised throughout the lease terms, starting at inception in some cases, and after two years in others. The first refinancing is expected to close in the coming weeks and the second is expected to close early in the second quarter.

Given the strength of the asset market, in addition to these refinancings, we opportunistically sold three, 2004 built vessels. These sales, one of which was completed in Q4 increase our proforma liquidity by total of $35 million.

A key goal for 2021 was to decrease the company's cost of debt. During the year, we proactively reduced our cost of debt by exercising $186 million of purchase options on 9% sale-leaseback financings. These leases were replaced with low-cost sale-leaseback financing, which are expected to reduce Teekay Tankers

2022 interest expense by approximately $10 million. It is important to highlight that the new sale-leaseback financings entered into since Q3 2021 are only 30 to 45 basis points more expensive than our revolving credit facility.

Teekay tankers has the financial flexibility to face the future with confidence. Our debt repayment profile is very manageable in the coming years and with the longer repayment profile of our low-cost sale-leaseback financings, we have no significant debt maturities through 2026.

With that, I will turn the call over to Kevin to conclude.

Kevin Mackay: Thanks, Stewart. The last two years have been challenging for tanker owners due to COVID-19 and the historic impact the pandemic has had on the demand for oil tanker transportation services. However, through the good work of our staff, both onshore and at sea to meet the ongoing requirements of our customers and the various financial initiatives, we undertook from the latter half of 2019 through the most recent sale-leaseback transactions here in Q1 to strengthen our balance sheet and bolster our financial resilience. We continue to weather the current market headwinds while maintaining a strong financial position and high operating leverage that will allow us to benefit from the tanker market recovery in the quarters and years ahead.

With that Operator, we're now available to take questions.

Operator: Thank you. 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 our equipment. Once again, press star one to ask a question. We'll pause for just a moment to allow everyone an opportunity to signal for questions. And we'll go first to John Chappell with Evercore ISI.

John Chappell: Thank you. Good morning or good afternoon. Kevin, start with you, the big news today is obviously Russia-Ukraine, you named as a wild card and I don't think anybody knows exactly what's going to happen, but maybe if I can just ask you a two-parter on this. First, as it stands today we're seeing you like huge moves in north sea, black sea, even US Gulf to China is I think people try to figure out how Europe's going to maintain access to the commodity. What are you seeing in this short period of time as it relates to any changes in tonne-miles? And the part B to it would be obviously this is pre-sanctions, but maybe a little bit preparatory, in a sanctioned environment, how would you expect the kind of shifting of the map to play out and what impact that have on your side ship specifically?

Kevin Mackay: That's some good questions, John, and difficult to answer given the dynamics of the situation. It's obviously very fluid and it's only a few hours old. We have seen an immediate reaction in the spot market. Rates in the Baltic for Aframaxes are now upwards of $150,000 a day. We're not seeing that same kind of reaction in other parts of the world where the impacts have been less. I think in terms of tonne-mile and how trade patterns change, I think it's too early to tell. We don't know what level of sanctions are going to be placed from the various Western powers and we don't know if that's going to impact the energy infrastructure. I think that the tonne-mile question is a little bit difficult to answer. But I think we have heard rumors and we have heard discussions in the market. Some owners may prefer not to trade in certain areas around the world and that could chase the balance of supply and the demand that exist. So, I think it's an interesting question, but I think it will take a little while here before we really, fully understand the direct impact on the tonne-mile. In terms of the second part of your question, can you just repeat that because I was getting cut off as you were speaking?

John Chappell: Yeah, well, it was kind of a, what if, but if sanctions target the oil markets, seems like it's kind of a last case scenario, but if that were to happen, how would you see kind of a redrawing of the map and how would that specifically impact the Suezmax and the Aframax markets?

Kevin Mackay: If they did go after the energy sector, that's obviously going to impact trade patterns. A large swath of Russian exports do head into Europe and European refiners would be then be forced to seek supply elsewhere, which typically I think would probably come from West Africa, the US Gulf, Brazil. So, there would be an impact on trade patterns. There is also the question that we're seeing today with Iran and

Venezuela in terms of where Russia would seek to move their oil to other parts of the world that aren't sanctioning them. And there could be a draw for some of that shadow fleet to fulfill that. But at this point, I think that's conjecture and it's too difficult to tell how deep the sanctions go and how Russia would react to them.

John Chappell: Okay. That makes sense. Thanks, Kevin. Stewart, just a couple quick ones for you on the modeling front. Can you name the three vessels that have been sold just for modeling purposes?

Stewart Andrade: The Australian Spirit, the Kaveri Spirit, and the Axel Spirit.

John Chappell: Okay. And then as we think about the closing of this 13 vessel refinancing couple weeks in early April, there's not a big identifiable bullet that I'd seen in 2022. So, what's kind of the gross proceeds of these refinancings and what are then, it used to being paid down to net to that 75 million of incremental liquidity.

Stewart Andrade: The gross proceeds are about $290 million and the liquidity increase is about seventy-five. So, the delta between those is the revolver that we will retire.

John Chappell: Okay, so just paying down the revolver.

Stewart Andrade: Yes.

John Chappell: Got it. Thanks, Stewart. Thanks, Kevin

Stewart Andrade: You're welcome. Thanks, John.

Kevin Mackay: Thanks, John.

Operator: We'll go next to Randy Giveans with Jeffries.

Randy Giveans : Howdy, gentlemen. How's it going?

Kevin Mackay: Good, Randy. How are you?

Randy Giveans : Doing well. Couple quick questions, I guess, first looking at those tanker sales, pretty prudent here. You still have several more over 15 years of age. So, what's the thoughts around maybe timing or scale of continued vessel sales, considering your liquidity position as well as kind of positioning the fleet for IMO 2023 and beyond.

Kevin Mackay: I think we do have a couple of ladies that are sort of at the tail end of their life. But I don't think it's a burning platform that needs dealing with necessarily this quarter or next quarter. So, we do have a bit of time to think about that, and really do our sale-keep analysis, which projects out where we think the market's going to go, and what kind of revenue generation those ships will be able to provide us versus what we can get to liquidate them now and take the cash off the table.

The asset price market is firm. We don't see that changing in the new of term. So again, that means that we might have a bit of a time here to consider those ships. We're also confident that as we move towards 2023 and beyond that those ships could be massive cash generation machines for us. So, I think we've been proactive. We've sold the three ships opportunistically because they were in unfavorable positions from a trading standpoint and we were getting good value for money in the positions that we delivered them at. So, we took advantage of that, but I think that doesn't necessarily mean that we're going to follow on and immediately sell the next couple of ships that are in that age bracket. We'll continue to analyze it and we'll make our decision once we've determined what the best value for the company will be.

Randy Giveans : Okay. And then one of your slides here shows your fleet out-charters, your time charter-outs, that's gradually declining over the next few months here. Any appetite for balancing that against your spot exposure, just to securing some more cash flow here in the uncertain times.

Kevin Mackay: Yeah, certainly. I think I've said this in prior calls it's something that's dynamic. We look at where we think rates are going and whether we want to lock in a percentage of the fleet. A lot is determined by the opportunities that we can find from the market. In this case, putting the one ship out we thought was worthwhile given where the ship was trading at that point. So, it all comes down to whether those opportunities present themselves at rates that we think are a good hedge against what our forward view of the market might be. I would expect to see us possibly doing some more if the right numbers come along, but overall, I think you'll probably see us maintain a stronger exposure to the spot market because our view continues to be that the tanker market will recover and we want to be in the spot market to enjoy some of the upsides that might forward in the next few quarters.

Randy Giveans : Yep. That makes sense. That's it for me. Thank you again.

Kevin Mackay: Thanks, Randy.

Operator: We'll go next to Ken Hoexter with Bank of America.

Ken Hoexter: Great. Good morning. Hey, Kevin and Stewart and Christian. If we think about the last comment there, would you move more to the lightering market? I think you've got now six in there and you're getting obviously very healthy rates. Is that something you could consider on some of the Aframax's given the rate differential in the market, and the time difference where you might be able to generate the cash flow until you start seeing that spot market rebound?

Kevin Mackay: That's certainly tactically something that we have been doing, moving more ships across into the Gulf. Lighting volumes generally have increased. We have seen a mark improvement in the volume of export barrels over the last three or four months. So that is driving our customers to have volumes for us and we've been very proactive in trying to secure additional contracts in that space. It's certainly something the team in our Houston office is focused on and if we can add incremental requirements and that would drive more ships into that space at these kind of numbers, the premium we're getting over the spot market, it's certainly something you want to do more of. Absolutely.

Ken Hoexter: Is there a gating factor to do that? Maybe just describe a little bit, I don't know whether it's just, is it just cleaning or is there something more involved, or is it just contracting steady business, maybe just, what is the factor to get that?

Kevin Mackay: It's obviously dependent on the volume of exports that are being handled. And as I said, 2021 was a relatively quiet year for volume but we have seen that uptake in the last three or four months. So, some of it depends on the volume being exported and that can at times be price-driven. There are other competitors out there that we have to compete against, so I don't think it's something where we can grow our volume and take a hundred percent of the market, but it's a competitive environment and if we can dedicate the right tonnage at decent levels, I think, and I'm confident that we'll be able to do more business.

Ken Hoexter: Kevin, maybe just a more general question than John. John was being – great detail you gave on kind of what's going on in terms of the global market now with Russia and the sanctions or sanction potential. But what has your experience been in general around wars and the impact of supply and tonne-miles? Is there anything relatable that you could talk to, whether it's Iraq war II or post US invasion like Afghanistan, is there kind of a general trend short-term, and then a year out you in terms of kind of lasting impacts on the market from global activity like that?

Kevin Mackay: I think first and foremost, war is a horrible thing and as Teekay Tankers and the CEO of our company, our heart goes out to the people of Ukraine. So, it's not something that as an owner you'd want to take advantage of, or wish to happen on anybody. I think to be honest with you looking back over history, there isn't really a definite pattern, every world event, whether it's a conflict or other form of geopolitical unrest, it drives different behaviors from different players in different parts of the world. So, I think with each instance, you have to look at what you're facing in the particular situation. And a lot of other things come into play in terms of fleet supply and general dynamics within the market that have just as much bearing on whether there's a conflict in a certain region, but it will certainly, have an impact. It's just a question of trying to determine overtime what that looks like. So, we'll have to see and report back in future quarters as to what we are seeing and what we've been able to do.

Ken Hoexter: So that, I guess then let's sets a stage for the market currently. So, you've got low inventories, low orderbook, and aging fleet, maybe you're building demand backdrop. What is the, I guess, the timeframe you think that it's going to take for pricing to kind of flow through, you talked about building through 2022 is – maybe just lay out your thoughts on how this year starts to build and into the setup for 2023.

Kevin Mackay: I think nobody in their right mind can predict with any degree of accuracy on a month-to-month or quarter-to-order basis when this market's going to turn. It's an extremely complex market that we participate in. And I don't think it's a single driver that changes the direction of a market. It's a multitude of catalyst that align, that drives things. As I look at our market today, we still fundamentally have less volume than we've had historically. We're still, Christian would probably tell us, somewhere close to 2 million barrels a day short on oil supply, that is starving the tanker market. We're also we're traveling shorter distances because of pricing differentials between Atlantic-based crudes versus the Middle East benchmarks, which sort of incentivizes Asian refiners to buy from the Middle East versus buying from West Africa or the US Gulf or Brazil. Scrapping comes into play, because of the Iran situation, a lot of ships that would've scrapped have perhaps kept trading in that shadow fleet and that's had an impact. There's a myriad of different factors that have impacted the market and that over time will change. We will get more supply as OPEC unwinds their cuts at the chosen rate of 400,000 barrels a day each month. As the Atlantic spread to Dubai narrows, we will start getting refiners taking more long-haul barrels. The longer we have freight rates at the levels we've been seeing, there will be an incentive for a tranche of ship say coming up to 20 years old or above to head to the scrap market because scrap values are high. I think the catalyst will change as we go, but trying to predict which month that they all line-up or which quarter that happens, I think I'm not prepared to do that. I would just say in general, our view is 2022 will be better than 2021 and we think 2023 and 2024 will continue to improve and be fairly strong tanker markets.

Ken Hoexter: Great. Kevin, appreciate your thoughts and insights.

Kevin Mackay: Thanks, Ken.

Operator: We'll go next to Magnus Fyhr with H.C. Wainwright.

Magnus Fyhr: Yeah. Hi, good afternoon. Just a follow-up question on the market developments. I guess it sounds like you're a little bit more, I guess had recent events you think delayed recovery into 2023 and what events do you think, is it US exports or OPEC production that's kind of will be the key driver? Do you think scrapping, I guess that will all have to come into place, but I guess my question is do you think the recovery has been delayed into 2023 given recent events?

Kevin Mackay: Well, I think if you look at it like I said on the previous question, I think 2022 will be stronger than 2021 so you could say the recovery's already started. It's just a question of how much better will 2022 be to 2021? Our view is the improvements are likely to be seen more in the second half than the first half. We think that over the next couple of quarters, we'll definitely see rates where they've been over the last month, which is not great but I think you also get volatility. Prior to today's events, we were seeing Aframax rates in the US Gulf spiking to $20,000 a day, and that was purely driven by weather. So, I think we will see more volatility. We are seeing more volume in the market. We're being hampered right now because of higher bunker prices. But that again, corrects itself over time. So, I'm not writing off 2022, but can I tell you whether it's going to be Q2 or Q4? No, I can't.

Magnus Fyhr: All right. I won't push you more on that. So, you have your polls on the US market, the Gulf lightering market and just kind of want to see your thoughts there with new projects, export projects coming online, shale production is ramping up and a lot of the crude is going to Europe. So, do you see an increasing role there for Teekay to facilitate some of these exports, if they're going to Europe, given your fleet size?

Kevin Mackay: Absolutely. Those barrels move predominantly an Aframaxes, but also on Suezmaxes going TA so we can service the full-service lightering business, we can service the customer's requirements that are going TA. There will continue to be barrels that are moved on VLCCs and not all of it will be done directly from terminals. There is increasing developments in terms of pipeline infrastructure coming down from Canada that will have to come out on an Aframax along the Mississippi River. I think lightering volumes, even with the development of some of these projects that have been discussed, and I know of one that's moving ahead, we're still getting enough volume for lightering and so we'll service that market, but we'll also service the TA. We've got a strong presence in the Atlantic with both our Aframax and Suezmax. So, I'm confident that we can take part in that market as well as it develops.

Magnus Fyhr: All right. Great. Thanks for your answers. That's it for me. Thank you.

Kevin Mackay: Thanks, Magnus.

Operator: And at this time, there are no further questions. I'll turn the call back to the company for closing remarks.

Kevin Mackay: Thank you for joining us today. As I said, our thoughts and prayers are with the people of Ukraine, and we look forward to speaking with you next quarter. Good day.

Operator: This does conclude today's conference. We thank you for your participation.