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PGS.OL - Q3 2017 Petroleum Geo Services ASA Earnings Call (Morning)

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PRESENTATION

Bård Stenberg *- Petroleum Geo-Services ASA - VP of IR & Corporate Communications*

Good morning, and welcome to this presentation of PGS Q3 2017 results. My name is Bård Stenberg, Vice President of Investor Relations and Corporate Communications. Today's presentation will be followed by a conference call, and people on the conference call will also be invited to ask questions after management's concluding remarks.

Before we start, we would like to give some practical information. As we are broadcasting this presentation, I kindly ask the audience here in Oslo to use the microphones provided when asking questions. For the audience here in Oslo, also, please take notice of the emergency exits located in the back of the room. If the alarm is sounded, please evacuate immediately.

I would also like to draw your attention to the cautionary statement showing on the screen and also available in today's earnings release and presentation. Please study that carefully. Today's presentation will be given by CEO, Rune Olav Pedersen; and the CFO, Gottfred Langseth.

And with that, it's my pleasure to give the floor to you, Rune Olav.

Rune Olav Pedersen *- Petroleum Geo-Services ASA - President & CEO*

Thank you, Bård. Welcome, ladies and gentlemen, to our Q3 results. And our Q3 results were driven primarily by a very good execution of strong or good MultiClient projects in Canada and the North Sea. And you can see it on the screen here. While our Marine contract revenues, we experienced that the good pricing we had achieved for some of the jobs in Q3 were negatively impacted by a particular one challenging project in Asia Pacific.

All in all, our EBITDA was $108.6 million for Q3. Cash flow from operations at, fairly strong, $118.4 million. Another important element is that we are seeing improved visibility for the winter season, which I will get back to. But most importantly, we have, in PGS, embarked on a reorganization, with the aim of reducing costs and improving the flexibility in how we address our customers in this market. The goal here is to become cash flow positive in 2018, after that service, taking into account that '18 may be flat compared to '17. So we are today announcing that we are reducing our gross cash cost by at least $100 million for '18 compared to 2017. I will get back to this.

I'll be fairly brief here on the financial summaries, but simply highlight a fairly strong cash flow from operations of $118 million, and it's been a long time since we've had this kind of strong cash flow. And I'll leave those numbers to Gottfred.

Onto the order book. The order book at the end of Q3 was at a fairly weak $167 million. However, following Q3, the end of Q3, we have seen a significant inflow of new work. So we have secured work in the range of approximately $55 million in October alone. And you see the bars, obviously, the full colored bar represents $167 million and then the shaded bar represents what we have secured after quarter-end.

On the vessel booking side, this is currently based on 8 vessels. But as I will explain to you later, we are reducing the cost base of PGS to a level of 6 vessels. And we will use the remaining 2 vessels more selectively and opportunistically when we have good MultiClient projects or contract projects to execute. And we expect then to use 6 vessels during the winter season, and we expect to use 8 vessels during the summer season.

We still based these booking numbers on the 8 vessels. And as you can see, based on that 8 vessels, we have 70% booked for Q4, 40% booked for Q1 and 10% booked for Q2 '18. This means that, based on 6 vessels, which we intend to operate during the winter season, we are more or less fully booked or, basically, fully booked for Q4, and we expect to be able to book the remaining slots in Q1 for 6 vessels. And then we will, as I said, introduce a seventh or an eighth vessel during this winter season only if we find that we have commercially solid projects to put them into. This is a change.

We reorganized this company for growth in 2010. Since then, the market has changed significantly. The world around us has changed significantly. The market is smaller. It's weaker. It's more uncertain than it was in 2010, where we had a strong oil price and there was a growth in the seismic market, and we expect a strong growth in the years to come.

The customers have reorganized their operations. All the major oil companies of the world have more or less centralized, they've reorganized, and we need to meet that challenge. Governments are easing their local content requirements around the world to stay competitive in today's low-cost oil -- lower oil price environment. And obviously, communication has greatly improved since 2010.

We need to match this. We cannot stay the same when the world is changing. So therefore, today, we are introducing a new operating structure for PGS. It is based on 3 keywords: centralization, simplification and streamlining, which are keywords we have used when we have designed this new operating model.

So we are going to operate in 2 business units going forward. One called Sales & Services and one called Operations & Technology. It's going to be a smaller and more flexible organization, obviously geared towards being more profitable as we are taking out a lot of costs in the process.

A few highlights. We'll have a sales unit, which will sell all the services of PGS, with our imaging, MultiClient, contract in one unit. We have combined the MultiClient part of the business and the imaging part of the business into Sales & Services to bring Imaging closer to MultiClient and to the sales process.

We have centralized -- or we will centralize the bidding organization in PGS. Currently, we are addressing the marine contract bids regionally. Those will be centralized into one unit for project planning and bidding, under Operations & Technology. And we will have an increased focus on project delivery. One organization will be responsible, both commercially and operationally, for delivering any marine contract project in PGS, a stronger focus on project delivery. By doing this, we believe we have a more effective organization and, at the same time, maintaining PGS's competitive advantages. So we will still offer MultiClient services, marine contract services, imaging services. It will still be based on our results and our technology, but we are going to do it in a different way.

Part of what we're doing, as I have alluded to, is increase the fleet flexibility. The pictures here are the 8 vessels we will operate going forward. Two of those will be used only selectively. And as I said, we intend to address the seasonality we are experiencing where we have a stronger demand in the summer months here in the North and a weaker demand in the winter months. So we will address the cost base of the company, both offshore and in the offices to a 6-vessel operation. And then we will use part-time employees, regular part-time employees and contractors to man up the other 2 vessel when we need that. So much more flexible cost structure than what we have today.

We always still own our 6 cold-stacked vessels, and they are an important part of what we -- the recovery story further out. We will, of course, bring them back in as the market come back.

So what will they do? It will bring the 2018 cash costs below $600 million, which is a cash cost reduction of at least $100 million. That will be done by, as I said, centralizing, simplifying and streamlining the organization, closing down offices or reducing the size of it around the world. We still have quite a few offices with quite a few sites. They will become smaller or close down. We will improve vessel flexibility. We will centralize and reduce the imaging capacity, which is currently too big for the market. We will and have renegotiated our contracts with suppliers, and we have several other initiatives all directed at delivering this cash cost target.

It's important to note that operating the 8 vessels you saw, 6 in the winter months and 8 in the summer months, will practically be the same capacity that we have operated in the market in 2017. So we don't see that these initiatives will impact revenue.

We will continue our strong focus on keeping CapEx at a minimum level. These initiatives, obviously, have a cost, and we estimate that we will spend approximately $40 million to $50 million to realize this cash cost savings, and we estimate that most of this costs will be taken in Q4 2017. And there, obviously, the aim is to be cash flow positive after debt service and tax at the very, very bottom line, considering that '18 may be flat compared to '17.

So in conclusion, streamlining and simplification starts at the top. So this is the new [EXT] team in PGS. Sverre Strandenes will head up the Sales & Services organization, Per Arild Reksnes will head up the Operations & Technology, and the person speaking next will still be the CFO. Gottfred?

Gottfred Langseth - *Petroleum Geo-Services ASA - CFO and EVP*

Thank you, Rune Olav, and good morning, everyone.

Revenues for third quarter was $207.6 million, that's a 9% reduction from Q3 last year. The EBITDA for the quarter, $108.6 million, that's a notch lower than what we had Q3 last year.

So the operating loss for the quarter, excluding impairments and charges, $30.4 million negative number. We recorded quite significant impairments and charges in this third quarter, and we will work through that after those charges. Reported operating loss was $113.6 million.

We had the following charges in the third quarter. $28.5 million of impairments relating to the vessels, and this relates to the reduced baseline for vessel operations -- vessels to be operated going forward, and impairments are primarily on the stacked vessels, impact of the B Class Ramform vessels. Due to the expectation, it will take longer time until they return to operation.

We had a $41.7 million impairment relating to the MultiClient library. This relates to a low number of specific surveys, primarily in the Gulf of Mexico, where we've seen lower sales than last. There are no concerns relating to the overall sales performance or the overall book values of the library. This -- under the accounting rules, we, as always, need to assess surveys on a standalone basis and related to project-specific circumstances.

We had $16 million of onerous contract provision in the quarter relating to the charter of the Sanco Sword. This, as well, is driven by the lower baseline for vessels to be operated, which makes it uncertain when -- if and when the vessel will be taken into operation in PGS. This is on a charter commitment until early mid-2020.

In addition to this, we also expensed the remaining deferred tax asset in the balance sheet now in Q3. This is a somewhat technical point that we have concluded that criteria to recognize -- for recognition of deferred tax assets under IAS 12, which are pretty strict and no longer satisfied.

Moving to the Q3 operational highlights. Total MultiClient revenues, $149.6 million. Pre-funding revenues dominating that number. $101.8 million of pre-funding revenues, corresponds to a pre-funding of 124% on the $82 million we had of capitalized cash investment.

So we see from the graph to the right, the purple line, that we're continuing a strong trend on pre-funding levels on our MultiClient investments and developing in a way around the top end of our targeted interval. Late sales, $47.8 million in the quarter.

Marine contract revenues, $43.5 million. We had less capacity allocated to marine contract in this quarter. You'll see from the illustration to the left that -- the yellow curve, that we had the -- this is the lowest relative allocation to contract activity we have had in a long time. And as Rune has pointed to, the price increase we achieved on aggregate on the surveys to perform in Q3, in this -- in our actuals, have been offset by a strongly underperforming project in Asia Pacific, which means has resulted in an unsatisfactory sort of net actuals for the contract activities for the quarter.

Moving to MultiClient revenues by region. Pre-funding revenues, dominated by North America, impacted Canada and Europe, while late sales revenues were primarily from our library in Europe and Africa for this third quarter.

We continue to show strong performance on our MultiClient activities, we compare well with the rest of the industry on most parameters, including the revenue to book value and revenue to cash and investment. As illustrated on this slide, more than 70% of our Q3 revenues were relating -- or were MultiClient revenues.

Book value at the end of Q3, $566 million, down from $647 million at the start of the year. Amortization rate on MultiClient sales for the quarter, 75%, somewhat high, primarily due to, in a way, the mix with pre-funding revenues weighing in more heavily than late sales in this.

So a decrease on the key operational numbers, most of these things we commented on already, but just point to Imaging revenues, lower than earlier quarters. So it's a combination of a weak market for external imaging services and the fact that we are using more of our imaging capacity towards our MultiClient library.

And next, on operating cost and depreciation. If you -- those who are entered in the P&L lines for that, they are quite low. And the primary reason for that is, obviously, that we had high MultiClient investment activity in the quarter, so there are more of those costs capitalized to the library in the quarter than what we've seen in earlier quarters.

Then utilization of vessels, 81% active time in the quarter. We had more streamer capacity in this third quarter than at the same period last year, primarily since Ramform Hyperion was in full operation. We expect now to use 45% of our active capacity full year for MultiClient. So a slightly lower than what we said quarter impact.

Costs. The other sequential cost increase in the third quarter, this is capacity- and project-driven, with more capacity in operation in Marine 3D vessels. And we had higher project costs and some external costs also relating to that, for various reasons, but most importantly, a very expensive Canada -- portfolio of Canada projects in this quarter.

Quarterly costs will be significantly lower going forward from here. And our full year gross cash cost still expected to be below $700 million.

Cash flow. Strong cash flow from operations. A reduction of working capital in the quarter, clearly related to the fact that there is more -- higher and more back-end loaded revenues in the second quarter than what we had in the third quarter.

Net cash flow after investing activities and before financing, you'll see from the table, positive, $18.4 million. Financing activities, which is a large number, $47 million, is primarily relating to a $25 million reduction of the drawing on the revolving credit facility in the quarter and the $13.2 million of scheduled repayments on the export credit loans that we have on the new bids.

Balance sheet. Liquidity reserve quarter-end, $234 million. Net interest-bearing debt, at the bottom of the table, $1,113,000,000. Total leverage ratio, quarter-end, 4.32 to 1, which is down compared to what we had at the end of last quarter.

Last slide for me, summary of debt and drawing facilities. Not a lot of change here compared to what we showed at quarter back, with the exception of the 2 things I already pointed to. The drawing on revolving credit facility is reduced and currently stands at $200 million, with $200 million currently unused. And then a reduction of the balance of the export credit loans by [a little] over $13 million due to scheduled amortization of the loans.

With that, I will stop and give the room back to you, Rune Olav.

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

Thank you, Gottfred. Well, an overview on where we have our vessels currently. I think I will limit myself on this slide to indicate that the vessels in the middle of the picture in Africa are currently on their way to jobs in Brazil. You see Tethys leaving to Brazil, and Sterling, Titan and Atlas will soon be working in Africa.

On the Marine seismic market outlook, we still believe that improved cash flow among the oil companies, combined with the limitation on streamer availability, will benefit the seismic streamer markets, but we do believe that the timing of that is uncertain.

And as you have heard, in PGS, we planned for a flat market in 2018 over '17. That obviously doesn't mean that we necessarily believe it will be flat. I believe that the risk is on the upside rather than the downside, but we planned for a flat market.

The seasonal variations, I have commented on. And as you have heard, we are addressing that with our new operating model, the flexible fleet model.

On a more shorter term, we are seeing encouraging contract leads developing, and you see the leads curve increasing and also the bid curves. And as before, seismic demand is primarily driven by positioning for strategically important licensing rounds and commitments in E&P licenses.

We continue to see a growth and more contract opportunities in the 4D space. And we continue to win a very large share of those contracts, which is an important element of the near-term market for us.

On the marine seismic supply, as you know, this industry has adopted and addressed the reduction in the amount of oil companies, and the average streamer capacity is down approximately 40% from 2013. And we expect that capacity in the winter season coming will be approximately 10% lower than what it is in the summer season, obviously partly because we are operating less vessels in the winter season than in the summer season.

On our guidance, we are still guiding on a gross cash cost below $700 million for 2017, of which, $225 million will be capitalized as MultiClient cash investments. The value is down from approximately $250 million.

Pre-funding level, we predict, will be above 100%, which is up from previously where it said approximately 100%. And we believe that the active 3D vessels time plan for MultiClient will be approximately 45%, which is slightly down. The CapEx numbers are unchanged.

So in conclusion. This quarter was characterized by solid MultiClient performance. We had a very high -- we had high pre-funding revenues, and it was a high pre-funding level of it. We had a fairly strong order intake in October, which has been important because we have then been able to see an improvement of the visibility for utilizing our vessels during the winter season coming up. We still find that the bidding environment in marine contract for the winter season is competitive. And we see, as you have seen, an encouraging bid pipeline for 2018. And again, the most important thing we are doing in PGS these days is embarking on a challenging reorganization and cost-cutting exercise to bring down the cost base of this company with more than $100 million, '18 over '17, and reorganizing, at the same time, so that we can address the market in a better way than we are currently doing. And with that, we aim to be cash flow positive, as I've said a few times, at the very bottom line after debt servicing and after tax payments.

So with that, I think it's time for questions.

Bård Stenberg - *Petroleum Geo-Services ASA - VP of IR & Corporate Communications*

Okay. Thank you, Rune Olav. We can start the questions here in Oslo, from the audience in Oslo, before we go to the people on the conference call.

QUESTIONS AND ANSWERS

Bård Stenberg - *Petroleum Geo-Services ASA - VP of IR & Corporate Communications*

There is no question in Oslo. Operator, can you start us up with the Q&A session and provide the people on the call with the instructions for asking questions?

Operator

(Operator Instructions) We will now take our first question from John Olaisen from ABG.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

A few questions on the cost-cutting initiatives. At the moment, you got 8 vessels, and I see the order book or the vessel booking capacity for the winter is based on 8 vessels. Firstly, do you still plan to have 8 vessels in Q4 and Q1? And if that's the case, when do you expect to use only 6 vessels? Will that be for next winter, so a year from now? That's the first question. If you can answer that first, please.

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

Sure. No, we plan to operate 6 vessels already in Q4 and Q1, Q4 '17 and Q1 '18. We currently have our vessels operating, so they were always there. The reduction from our current 8 to 6 will happen over the next week. And then we will take on additional projects opportunistically, also for this winter.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

All right. And the costs, I presume they will have pretty much full costs for this winter, and you got that less flexibility that you have in that model, with the 2 new vessels will be effective only from next winter, I guess. Or do you have low costs for this already now?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

The costs, we will take it out gradually during this winter. So it will have impact on this winter season as well, obviously more impact the latter part of the winter season rather than the earlier part.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

But how does it work? I presume that it will be fully equipped with streamers, et cetera. And basically, the people and the fuel that you're saving, is that correct?

Gottfred Langseth - *Petroleum Geo-Services ASA - CFO and EVP*

Yes, correct. People, fuel, and support vessels and related costs.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

And what would be the costs of these vessels once -- when they are warm-stacked during the winter?

Gottfred Langseth - *Petroleum Geo-Services ASA - CFO and EVP*

We will not give a specific number on that. But it will be obviously higher than a cold stack, but it would be a significant cost reduction comparing to keeping the vessel sort of truly ready to operate with crew and available sort of source and chase this capacity.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

All right. And then, next winter, they will be stacked as well. And I presume -- since you need to plan for this, you'll plan to take them out? You'll be working -- operating, sorry, 6 vessels for whole of Q4 and the whole of Q1 going forward for the winter seasons is the case?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

The plan is to do that, yes.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

Yes. And you're saying you don't expect that to have any impact on revenues? Is that correctly interpreted? But I guess, you had more than 6 vessels now in October. And also last year -- or sorry, in Q1 2017, you had more than 6 vessels operating, didn't you?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

Yes, we did. But the assumption here is we had idle time during the year. So if remove the idle time and you adjust for the fact that Vanguard wasn't operating in Q1, Hyperion entered the fleet in May when we gave a vessel count -- no, a streamer count which is very similar, '18 over '17.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

Okay. And on the near term, the vessel bookings on for Q4, 70%, the 40% for Q1. The increase since last time you reported this, is this mostly client or contract? And secondly, since you're planning to operate only 6 vessels, I guess, 70% of booking is close to full capacity? Two questions, please.

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

Yes. Yes. No. The -- to answer the last question first. Yes, 70% is full capacity, basically. And to your first question, it's a combination. We are -- we have filled up with both MultiClient and contract. So it's a -- I would say, it's a fairly good mix on MultiClient and contract works, mostly in Q4 and Q1.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

Is it possible to break it down? Is half of it MultiClient or more than that?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

Approximately 50-50, I think, is a good proxy to use.

Operator

We will now take our next question from Christopher Møllerløkken from Carnegie.

Christopher Møllerløkken - *Carnegie Investment Bank AB, Research Division - Research Analyst*

First question. In terms of the costs that you are planning to book here of $40 million to $50 million with relation to this reorganization, is that a cash cost or is it a noncash element as well?

Gottfred Langseth - *Petroleum Geo-Services ASA - CFO and EVP*

So this is primarily cash cost that we call over some time. But as you see from the earnings release, mostly relating to severance payments. So that we will come with the inside the time horizon of sort of 6 -- 6 to 9 months in a way the severance payments are made.

Christopher Møllerløkken - *Carnegie Investment Bank AB, Research Division - Research Analyst*

I understand that, so the 2 chartered vessels that you will be moving from, basically, having your own employees to using more contractors for this summer season capacity. Has there been any discussions regarding also changing the contracts on the vessels in terms of I assume you're paying a flat fare, but now instead trying to opt to a pay per use structure?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

I guess, firstly, it's -- you're right in a way to assume on a general note that we will try to keep the more effective Ramforms as the 6 vessels we use. But we will try to be as flexible as possible. And whether it is a chartered vessel or a Ramform vessel that is in operation depends also on where in the world they've been working, where in the world the vessel is. So we will try to be flexible on where the crews are allocated with respect to vessels. And secondly, I think I will not go into the details, but it's obvious that we have addressed also our suppliers as part of this cost reduction.

Christopher Møllerløkken - *Carnegie Investment Bank AB, Research Division - Research Analyst*

And in the third quarter, you had some issues in Asia Pacific on a contract project. Has that project been completed now?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

Yes.

Christopher Møllerløkken - *Carnegie Investment Bank AB, Research Division - Research Analyst*

And just a bookkeeping question. The guidance on the amortization of $350 million for 2017, does that include impairments, or should we take the impairments into third quarter in addition?

Gottfred Langseth - *Petroleum Geo-Services ASA - CFO and EVP*

It does not include impairments.

Operator

We will now take our next question from Morten Nystrøm from Nordea.

Morten Nystrøm - *Nordea Markets, Research Division - Senior Analyst of Oil Services & Sector Coordinator*

Yes. First, a question to Gottfred. At the Q2 presentation, you were pretty -- you guided on the leverage ratio, et cetera, in -- for the -- for Q3. It seems now that you have decent visibility in Q4, based on your contract revenues, and MultiClient is obviously a big uncertainty. But are you able to give some indications around the leverage ratio for Q4? And secondly, the uptick you see in your tender graphs on sales leads and tenders, are you able to say anything specific on that? Is it new oil companies tendering for work? Is it in specific regions? Is it any work related to the North Sea 2018? If you can comment on that as well, that would be good.

Gottfred Langseth - *Petroleum Geo-Services ASA - CFO and EVP*

I promised to stop doing that -- indicating the leverage ratio going forward, but I would be cautious on that. But if you look at the way this it is calculated and the numbers for Q4 last year and Q1 this year, the leverage ratio should clearly reduce over the next couple of quarters. I think I would limit it to that and may even give the last part of the question to you, Rune. If you thought a bit on that?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

That's fine. Well, the increase in leads and in tenders are -- I would say, it's for -- in both new companies and no majors in there. Probably more so the familiar names than there's, actually, new names in that mix. With respect to whether it's for the North Sea season, we are starting to see, especially on the leads thing coming in the North Sea, but very few bids for the North Sea season, so this is work for this winter. I think it's the most important. And then obviously it's Africa and in Asia Pacific that are dominating.

Operator

Our next question comes from Sahar Islam from UBS.

Sahar Islam - *UBS Investment Bank, Research Division - Analyst*

On the 40% lower streamer capacity you talked about on Slide 27, how much of that capacity do you think has come out of the industry permanently? How much would come back if conditions improve?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

Yes, that's a good question. And I can't give a precise indication, but it is clear that as time progress, more and more of those 40% will be out permanently and less will come back. At the same time, it's clear that there are vessels out there, which are fairly new and will still be new in '19 and '20. So part of that capacity will come back, but it's difficult to indicate any percentages, I would say.

Sahar Islam - *UBS Investment Bank, Research Division - Analyst*

Okay. And on the contract year-on-year improvement, you said was masked by that APAC contract. Can you give us a sense of the quantum of that pricing improvement and how sustainable you think that is, please?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

I'll be cautious on quantifying on pricing. But obviously, we communicated earlier that we had significant better pricing in Q2 than Q3. And I will limit myself to say that the pricing in Q4 and Q1 is lower than what we were able to obtain in Q2 and Q3 as it is a more competitive market environment during the winter season.

Operator

Our next question comes from Mick Pickup from Barclays.

Mick Pickup - *Barclays PLC, Research Division - MD*

Sorry. Apologies, I got late. Can you just talk about 4D demand, if you could? And I think in your previous presentations, you've tended to have a chart of increase in 4D demand or outlook for 4D, and that seems to have disappeared. Can you just tell me where we are on that, please?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

No, that's fine. It's the -- that is still a good indication of what we feel on the 4D demand. The reason the graph is out is not because we don't believe in that one anymore, to put it that way. So you could still relate to that as an indication of where we believe that market is going.

Mick Pickup - *Barclays PLC, Research Division - MD*

Okay. And how has demand change then, given you're giving the charts anymore?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

No.

Gottfred Langseth - *Petroleum Geo-Services ASA - CFO and EVP*

No, the chart says that we have around 15 surveys, number of surveys illustration, and that is expected to increase to around 25 next year, and there's nothing we hear from customers that in a way changed our expectations significantly for next year.

Operator

(Operator Instructions) We take our next question from John Olaisen from ABG.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

Just a follow-up from me. I just wonder have you been in a dialogue with your debt holders. Given partly because what you're doing when taking the big restructuring charges here, basically avoiding a hit on the EBITDA, although it's a hit on the cash flow. Have you been in dialogue with your debt holders on this issue? Because EBITDA is a key figure for the covenants.

Gottfred Langseth - *Petroleum Geo-Services ASA - CFO and EVP*

So that is correct. And the loan agreement regulates how one-off charges and similar are urgently treated. And generally, I don't have any comments to whether or not we have a dialogue with our banks, but this is not a particularly significant issue.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

So there will not be any adjustments to the covenants because of what you're doing there?

Gottfred Langseth - *Petroleum Geo-Services ASA - CFO and EVP*

No, I'm not sure that's what I said. The agreement allows to adjustment for one-off charges in the calculation of total leverage ratio. And I think to be straightforward about it rather than unclear. It can be adjusted, but there is a cap of $30 million in any 12-month period.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

Okay. And now you're taking a lot more, of course, more than $30 million?

Gottfred Langseth - *Petroleum Geo-Services ASA - CFO and EVP*

Than the capital, which is irrelevant.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

Okay. So everything above $30 million will be deducted on the EBITDA?

Gottfred Langseth - *Petroleum Geo-Services ASA - CFO and EVP*

Correct. That's the basic rule. There may be details in here, which is not quite properly covered by this discussion. But that is the general rule, but as all our agreements, there are various types of detail. That's the general rule.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

Sure. And secondly, if the market improves next summer, so if there's presumably a lot of tenders out in over next few months for Q2 2018, will you then bring back the -- be operating 8 instead of 6 vessels for Q2 next year? Or are you having now locked out the capacity at 6 -- locked up for 6 next summer?

Gottfred Langseth - *Petroleum Geo-Services ASA - CFO and EVP*

So no, in a way, our baseline plan absent any other changes and circumstances is to operate 8 vessels for the next summer season and operate 6 vessels for winter season.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

But just wondering, do you have the flexibility to use the 2 warm-stacked vessels next summer -- next -- sorry, next winter, if there is demand?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

Yes. I was going to comment on that. Yes, that's the intention. We have the flexibility to introduce a seventh or an eighth vessel over this winter or next winter at a fairly short notice should demand pick up or should we find -- for example, this winter, should we find any interesting MultiClient project, which thus hence bringing in a seventh vessel, we will do that even this winter. We can do that on a short-term basis.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

Okay. And my final question. Since you had this operational hiccups on the contracts side in December and late sales were a lot weaker than consensus expected, particularly given the very positive comments you have given on the last couple of quarters about contract business this summer and for Q3, are you considering sending out a profit warning for the quarter?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

We always consider that when we are not hitting exactly the target you guys are setting, but it was not a long discussion.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

And if I add on that. You have been -- both you and Gottfred have been in the company now for many years. These changes that you're doing now seem to be what introduced -- similar to what CGG did 1 year ago. Why haven't you done this before? And have you ever -- have you considered doing this before? It seems like you're doing -- just the last guy doing all this.

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

Well, I could just point to the fact that we have, as you know, reduced our cost base continuously quite significantly since 2014, and this is the next step. And I'm not going to consider why we should have done it some months ago or not. So we're doing it now, and that I think is the most important thing.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

Yes. But it seems so obvious that like even CGG managed to do this more than a year ago, and you were actually bringing in more capacity with a new vessel. Because that was just the way you're thinking whether -- were you considering this 1 year ago or were you too optimistic on the market? Or why hasn't this been done before? Because you would have been a lot less trouble if you've done this a year ago.

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

Yes, I guess. But it's -- as I said, now is the time for it. I don't think I'll comment any further on whether -- on what I'm thinking was half a year ago or a year ago with respect to this.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

All right. And since, yes, this is your first quarter as the new CEO, can you tell us a little bit how you're thinking about the balance sheet? The debt that you have, are you comfortable with that level or would you like to start, I guess, discussing with banks on how to improve the balance sheet?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

Well, I'm obviously not comfortable with the debt level we have, and we will clearly, over time, aim to reduce the debt level, which has proven too high for the tough market we have experienced over the last years. But how we would like to address that or not -- how we would like to address that is not something I'm going to comment on here. But just to be clear, we are not planning an equity issue, if that is what you are alluding to. That is not in the cards, and I don't see that is necessary either. So the debt reduction will happen over time.

John A. Schj. Olaisen - *ABG Sundal Collier Holding ASA, Research Division - Co-Head of Global Research*

Yes. But the big maturity of the debt is only in [2020] and when do you think that you need to be -- assuming the market doesn't improve materially and even if it's materially, it seems like you're unlikely to pay that debt at that time. How quickly? Would you wait for one -- before like 12 months before maturity or 2 years before maturity, a year from now, or when would you start addressing the balance sheet issue?

Rune Olav Pedersen - *Petroleum Geo-Services ASA - President & CEO*

Yes. I think we will do that as we normally do. And I think the indication you're giving, somewhere between 24 and 12 months before maturity is a good guesstimate on when we have to address that. And that's why it's so important to get the company in a cash flow positive position after debt service as soon as possible. But then we are in obvious position where it is much easier to do a refinancing of that debt because, as you rightly point to, the market will have to improve quite significantly if we're not going to refinance any part of that debt.

Operator

We now have a follow-up question from Morten Nystrøm from Nordea.

Morten Nystrøm - *Nordea Markets, Research Division - Senior Analyst of Oil Services & Sector Coordinator*

Yes, one of my questions was included in John's 10 questions, so it's okay.

Operator

It appears we have no further questions at this time.

Bård Stenberg - *Petroleum Geo-Services ASA - VP of IR & Corporate Communications*

Okay. Are there any further questions from our audience here in Oslo? If not, that concludes this presentation. I would like to remind you of the conference call we also scheduled for 3:00 p.m. Oslo time here today. So thank you all for coming to the presentation. And also, thank you all for participating on the conference call. Have a nice day.

Operator

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