

## Q3 2019 Earnings Call

### Company Participants

- Bard Stenberg, Senior Vice President, Investor Relations and Communications
- Gottfred Langseth, Executive Vice President and Chief Financial Officer
- Rune Olav Pedersen, President and Chief Executive Officer

### Other Participants

- Terje Fatnes, Analyst
- Unidentified Participant

### Presentation

#### **Bard Stenberg** {BIO 19147078 <GO>}

Good morning, and welcome to this presentation of PGS Q3 2019 results. My name is Bard Stenberg, Senior Vice President of Investor Relations and Communications.

Before we start, I would like to give some practical information. As this presentation is being webcasted, I kindly ask the audience in Oslo to use the microphones provided when asking questions. Also take notice of the emergency exits located in the back of the room. And 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 available in today's material. Today's presentation will be given by CEO, Rune Olav Pedersen; and CFO, Gottfred Langseth.

So with that, it's my pleasure to give the word to you, Rune Olav.

#### **Rune Olav Pedersen** {BIO 16158611 <GO>}

Thank you, Bard. And good morning everyone. Our Q3 '19 financials are characterized by strong earnings on an improving seismic market. We delivered the highest EBITDA since Q4 2014, that's almost five years ago. That's driven by strong contract revenues of \$76.3 million, which is more than double than what we had in Q3 of 2018, which again obviously is driven by a price increase of 40% on average for '19 versus the average of 2018, or close to, I should say, and solid vessel production.

MultiClient revenues came in at \$148.8 million. And it's worth noting that we had particularly high sales from surveys, which are still in the processing phase, or quite late in the processing phase I should say, which is reported as pre-funding by PGS, and it drives

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the pre-funding presence quite a bit up to 125% and obviously has an equal impact on late sales, negative impact on late sales.

Order book more than doubled from Q3 2018, and you know that we will be running eight 3D vessels through the winter season, and which obviously gives visibility for the earnings in the fourth quarter and the first quarter of 2020 in particular.

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So our financial numbers, we are showing key financial numbers in line or stronger than what we have done four to five years. Revenues, basically at par with the three highest we've had in the last four years. EBITDA, highest since the fourth quarter of 2014. EBIT second highest since the third quarter, 2014. And cash flow from operations, highest since the first quarter of 2015. So our key numbers are in line with what we saw before the downturn, four to five years ago.

Order book, more than doubled from Q3 2018, and the highest we've seen, or at par with Q1 '17 as you can see. Before that, it's Q1 '15 again. This obviously is driven by very strong vessel booking. We are now fully booked for eight vessels in the fourth quarter, and we have booked 28 [ph] of the 24 vessel months in the first quarter 2020. And as you can see, we already started booking up the second quarter of 2020, which as I said gives strong visibility for earnings over the winter season. And I remind you of the very weak booking we had over the last year's winter season, where we struggled to fill work for six vessels. So a very different picture today from what we saw a year ago.

And with that, I give the word to Gottfred.

**Gottfred Langseth** {BIO 5277539 <GO>}

Thank you. Good morning, everyone. I will start with the key financial numbers. Revenues at \$234 million in Q3, EBITDA \$160 million. Both of these are more than 20% up from Q3 last year. The EBIT came in positive \$38 million in the quarter, and it's also positive year-to-date as you can see with \$26 million.

Other than that just a quick comment on the as-reported numbers, which are IFRS 15 based, the revenues under IFRS -- according to the IFRS 15, \$42 million higher than the segment numbers in this quarter. This is a tactical [ph] timing difference and will even out over time and you will see for the year-to-date numbers, we're at pretty similar revenue numbers, both for segment and as-reported.

A couple of more comments on this slide, net financial items in Q3 is lower than what we had in Q3 last year. Two primary reasons, interest costs are somewhat down as a result of lower interest rate on floating rate debt, and also reduced debt level compared to last year.

In addition, there's a foreign currency translation gain relating primarily to lease obligations, which are denominated in Norwegian kroner. Lastly, income tax expense in the third quarter and year-to-date somewhat lower than what we had last year.

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The next one, key operational highlights. Total segment MultiClient revenues, \$148.8 million. Pre-funding of 125% on \$75.7 million of investments in the quarter. Late sales ended at \$53.9 million. Our total MultiClient revenues in this third quarter is at par with Q3 2018, despite the fact that we used quite a bit less of our acquisition capacity for MultiClient this quarter compared to same quarter last year.

Contract revenues, \$76.3 million. That's more than a doubling from Q3 last year, as a result of significantly higher pricing, but also using somewhat more capacity in the contract acquisition.

MultiClient revenues per region, our pre-funding revenues were dominated by North America and South America in this third quarter. Biggest contribution to late sales came from our European library.

Vessel allocation and utilization, we had 88% active vessel time in this quarter. Second consecutive quarter with very high utilization, no stacked or standby time. We also expect high utilization for eight vessels in the current quarter, the fourth quarter, and we will have an overweight of the capacity working on contract versus MultiClient.

The bottom graph on this slide illustrates the utilization over a bit more time, and it shows that we are approaching pre-downturn utilization levels. I would say despite the fact that we started the year by operating -- with only operating six vessels with two vessels warm stacked. This is obviously an important driver behind, in a way, the price momentum in our segment and for us.

When it comes to cash costs, cash costs are slightly up sequentially, driven by higher project specific costs. We now expect full year gross cash costs to be approximately \$575 million. That's an increase of 25% compared to what we have said earlier. And the two primary reasons for that is operating more vessels. We're operating eight vessels through the fourth quarter and we also have an increase of project specific or geographical area related costs.

Cash flow, strong cash flow from operating activities, \$151.9 million, driven by higher earnings. Year-to-date, cash flow before financing activities is \$183 million. We have reduced our RCF drawings by \$95 million year-to-date.

Balance sheet, gross interest bearing debt at \$1.93 billion. That's down \$133 million so far this year. Net interest bearing debt, \$1.15 billion, that's down \$93 million so far this year, and liquidity reserve of \$216 million, which is up \$56 million. Total leverage ratio 2.55:1.

This slide illustrates our cash flow generation for the last 12 months, and this is same format as we used a quarter back. So after paying interest, CapEx and payment on financial leases, we have \$133 million available on cash flow before debt repayment. Then our debt structure, which is unchanged, except for a reduction of the revolver drawings and the scheduled amortization on the ECF loans.

Then moving to the refinancing, currently, it is challenging for oil service companies to refinance in the high yield market. The High Yield index is dominated by rigging and other offshore services, and we borrowed a graph from DNB Markets to illustrate a little bit, and you will see that there is a quite dramatic negative period so far this year for some of the sub-segments in the sector.

The seismic sector is outperforming most other offshore service sectors. The market for seismic is demonstrably improving, positive cash flows, earnings, and significant supply side consolidation, and moving into a supply demand balance that is starting to get quite favorable.

We plan to refinance during Q4 or as we say now early 2020 without equity. We are positioned and prepared to execute on very short notice. Exact timing and structure will depend on the market. We are generating solid positive cash flows as demonstrated by our numbers. And our net debt is reducing quarter-by-quarter. If we end up doing the refinancing early 2020, we will be at a place where we'll have a lower leverage. There will be less capital to refinance than we need now in Q4. With the debt market being as it is, we are evaluating our options to optimally address the 2020 and '21 maturities.

On that note, Rune Olav, I'll invite you back to the podium to talk about the market.

### **Rune Olav Pedersen** {BIO 16158611 <GO>}

Thank you, Gottfred. A little bit about where we have current streamer operations. We have two large Titan-class vessels currently in Guyana. Ramform Tethys has been there for quite a while, and will stay there for quite a while. And Ramform Titan is in there for a few weeks on the way to -- from Canada, doing a little bit of work here before transiting for work in West Africa.

The Sanco Swift which is our eighth vessel, is now transiting to work in West Africa over the winter. We have the Ramform Atlas, shooting seismic now in Ghana. And Sovereign continuing to shoot seismic in Angola. Ramform Vanguard is finishing off the GeoStreamer X project, which we have launched in the North Sea before traveling south.

PGS Apollo currently in the Comoros, and the Hyperion currently in Malaysia. So that's where we have streamer operations currently, and as I said, this vessel will obviously come down to the Southern Hemisphere fairly soon.

Seismic contract market outlook, you know this graph, most of you. But just to repeat, the blue line is the dollar value of all the bids we have in house, while the light blue line is the dollar value of or the -- it is the blue line plus the dollar value of the sales leads we have. And as you can see, there is a positive trend in the contract market in terms of bidding. And you have to correlate this with the fact that we are more or less fully booked for the winter. So there are plenty of work to choose from to fill the remaining slots, we have to fill over the winter. And therefore, we believe that we are seeing an emerging supply constraint in our market even over the winter season. And we just repeat that our average pricing in '19 is now almost 40% higher than the average pricing in 2018.

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On the supply side, the supply in '19 is on average down by 50% compared to the high in 2013. And we do expect to see a supply increase into 2020, mainly because of less warm stacked vessel in the industry. We will of course run our eight vessels through the first quarter of 2020 while we only had six in the first quarter of '19, which will impact this. And we are starting to see that the market fundamentals, and what we have done with the company, the cost savings we have taken out over the last three to four years are starting to show strongly into our financials.

On the top left here, you will see last 12 months Q3 '18 and last 12 months Q3 '19 EBIT. You see the difference is more than \$100 million and we are close to \$80 million of EBIT last 12 months, Q3 '19.

The order book below, as we have talked about is 133% up year-on-year. Cash Flow before debt repayments, 259% up when you take last 12 months Q3 '18 versus last 12 months Q3 '19. And our net interest bearing debt is down by 12% over the last 12 month period. So obviously, we are showing quite a bit stronger results than what we did a year ago.

Our guidance, as Gottfred has already mentioned that now our Group cash cost guidance is now \$575 million, excluding deferred steaming. Our MultiClient cash investments are up from \$225 million to \$250 million. Reason for that, main reason for that is obviously that we are operating one more vessel in the fourth quarter, but also there is a shift in the MultiClient activity in the quarter compared to what we expected earlier.

We still expect to use approximately 50% of our 3D, active 3D vessel time in MultiClient for the year. And CapEx are down from approximately \$70 million to approximately \$60 million for the year.

So in summary, we are showing the highest EBITDA since the fourth quarter of 2014. And as I have shown you, our key financials are at par or better than what we've seen for the last four years to five years.

Total MultiClient revenues in line with internal expectations during the quarter. But as I explained, we have higher than normal sales from service in the processing phase, which drives the pre-funding level in this quarter higher than what we had expected. And therefore, we now see that the pre-funding level for the year will be in the high end of the targeted 80% to 120% interval that we guided.

Contract revenues benefited from increased demand, strong price increase and high utilization in the quarter, and more than double of the ordering -- of the order book obviously.

So the seismic streamer market continues to improve. Focus for this management team over the next months is clearly refinancing. So let there be no doubt about that, it is a challenging market, and we will focus on handling that in the fourth quarter or early 2020.

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And with that, I think we open up for questions. Bard?

## Questions And Answers

**A - Bard Stenberg** {BIO 19147078 <GO>}

Yeah, thank you. We can start with the audience in Oslo first.

**Q - Unidentified Participant**

Two questions really. One is you mentioned increased capacity. What is your view on the current streamer capacity amongst yourself and competitors? Is there enough streamers to increase the capacity for next year? Or do you believe that you have to do massive investments to have that capacity available?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

What we predict when I told you that the capacity will be increased somewhat over next year, that can be done without new streamers. It's basically warm stacked vessels with streamers that will no longer be warm stacked in 2020 versus 2019. I believe that if you are going to take capacity, let's say significantly above that will require reactivation of vessels and more streamers. We hear rumors that one of our competitors have streamers, otherwise we don't know what kind of investments will have to be done in the vessels, which have been cold-stacked for four to five years or other MC equipment for that to be brought back to build --

**Q - Unidentified Participant**

Second question was on the high pre-funding number. Are you then saying that the potential late sales will be lower than expected in Q4 or?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

No, there's no correlation.

**Q - Unidentified Participant**

You said that the way to define pre-funding, since we're still in the processing phase has some negative impact on late sales.

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

Yeah, I think what I tried to explain was that in this quarter, we sold quite a bit from a survey very late in the processing phase. We had assumed that would have been processed and completed and therefore reported that late sales, which would have increased the late sales number in the fourth -- in the third quarter, and taken down the pre-funding level in the fourth quarter. It's just a shift over that timeline. It was not a reflection on what we believe will happen in the fourth quarter.

**Q - Unidentified Participant**

Okay. Thank you.

**Q - Terje Fatnes** {BIO 4311623 <GO>}

I'm Terje Fatnes from SEB. Very high vessel booking for winter season. Can you say something about pricing for the winter, and also if possible into 2020 season?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

I mean, obviously we are reporting more than 40% up, which is slightly up from what we have indicated earlier, and the pricing, the relative pricing winter season over winter season is similar -- in the similar range to what we report for the full year. So, it's quite a bit higher than what we experienced over the last winter season.

**Q - Terje Fatnes** {BIO 4311623 <GO>}

So those are reflected for first quarter or?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

There's no difference in pricing in fourth and first quarter in that respect.

**Q - Terje Fatnes** {BIO 4311623 <GO>}

I think you said in connection with the second quarter report that the pricing you had for 2020 secured so far was significantly up compared to the average of 2019. Is that still a statement that will be valid?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

I can't remember how we said that. No, I don't think that's correct. We expect I mean, we obviously expect pricing to be higher in 2020 versus '19, given the market outlook we currently see. But it's too early to say you know what that delta is, whether it's a lot or -- but first quarter '19 pricing versus first quarter '20 pricing is obviously up significantly, if that was what you were referring to, yeah.

**Q - Terje Fatnes** {BIO 4311623 <GO>}

My final question is on the CapEx for 2020. Is it possible to give an indication of how that might look like?

**A - Gottfred Langseth** {BIO 5277539 <GO>}

Yeah, it won't be too precise, but I think the general approach to this, at some stage, we will start renewing CapEx on our streamer portfolio. Until that happens, we aim to stay at the level you've seen for the last few years around \$50 million, give and take a little bit. Whether we will end up seeing some increase next year, that's too early to say but our aim is to keep our ongoing maintenance CapEx at the same level you've seen, until we decide that we need to start in a way that replacing streamers.

**Q - Terje Fatnes** {BIO 4311623 <GO>}

Okay, thank you.

**A - Bard Stenberg** {BIO 19147078 <GO>}

Okay, any more questions from the audience in Oslo?

**Q - Unidentified Participant**

Quickly, in terms of vessels being fully booked for the winter. I can assume that it will be fully booked for the summer in 2020 as well. Are you beginning to consider reactivating some vessels for the summer season next year?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

I would say no. I think it's -- the most likely time we will reactivate vessel will be for the 2021 season. And the reason for that is we would then need to invest in a new streamer set, and that has a lead time, which is longer than what we probably can manage now. So, I think you should assume that we will run the eight vessels through next year.

**Q - Unidentified Participant**

And also in terms of the order book, you mentioned pricing was up 40%. Obviously, the order book is up. I don't have the numbers on top of my head, but how much of the increase in the order book is attributable to more activity rather than price?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

Yeah, quite a lot. Clearly, if you compare -- if the comparison was Q3 '18 versus Q3 '19, I can't remember what we had in booking at that time but that is almost half. So obviously quite a bit of that is pricing but the pricing is mainly on the contract part of the order book obviously. So most of it is activity driven.

**Q - Unidentified Participant**

Thank you.

**A - Bard Stenberg** {BIO 19147078 <GO>}

Okay, if there's no further questions from the audience in Oslo, we'll go to the people on the webcast. We have a question from John Olaisen in ABG. regarding the eighth vessel months you have booked for Q2 2020. How much of that is contract work?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

Yeah, clearly the majority of it, I'm not -- can't remember whether that was everything or whether there was some MultiClient there, but clearly the majority.

**A - Bard Stenberg** {BIO 19147078 <GO>}

Let me ask a couple of questions, which has already been addressed earlier. In addition, he also asks, could you elaborate on the evaluating options to address 2020 and 2021

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maturity sentence? What could such options be?

**A - Gottfred Langseth** {BIO 5277539 <GO>}

I think we prefer not to go into the details of that at current.

**A - Bard Stenberg** {BIO 19147078 <GO>}

Then we have a question from Christopher Mollerlokken in Carnegie. He also has a couple of questions which have been addressed. But in addition, he also asks, with marine contract pricing being up for 40% and most clients keeping their exploration spending flat. Do you experience increased pushback from oil companies for the price increases you are demanding?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

I think the best answer to that is to look at the booking. And so no, we don't.

**A - Bard Stenberg** {BIO 19147078 <GO>}

Next question is from Matthew Dickinson from Capital Structure. Do you think your refinancing package will be similar to the mix you brought in to the market in May?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

I think we can only say what we have said that we are evaluating several options. So some of them similar to that and others probably more different from that. But we don't want to publicly get into a discussion on the various alternatives we're looking into.

**A - Bard Stenberg** {BIO 19147078 <GO>}

Next question comes from Morten Nystrom in Arctic Securities regarding the refinancing. What kind of interest levels are acceptable in terms of refinancing given that you decide to withdraw in June?

**A - Gottfred Langseth** {BIO 5277539 <GO>}

It is more or less the same answer, I don't think we want to comment on that currently.

**A - Bard Stenberg** {BIO 19147078 <GO>}

Next question comes from Lillian Starke in Morgan Stanley. On the pricing increase of 40% mentioned in the presentation, could you share how much of it comes from a better mix, potential in terms of 40s serving and how much comes from the general market improvements?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

I don't have a -- let's say I don't have a concrete and very precise answer to it. But the majority clearly comes from a better market improvement. But we are also doing quite a bit more 40s. So there's a mix of both of them in there but we have seen our competitors

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also reporting maybe not this high but they are still reporting significant price increases year-over-year. So I would say majority comes from the market improvement. And then there is some element of the increase productivity in there.

**A - Bard Stenberg** {BIO 19147078 <GO>}

Next question comes from Sahar Islam in Goldman Sachs. Now that the contract market has consolidated, how do you expect the key competitors to add capacity in the market next year and how could this impact rates?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

I'm not going to speculate too much about what our competitors will do. We believe that we will see a continuing type market next year with higher activity and then we will see how our competitors react to that.

**A - Bard Stenberg** {BIO 19147078 <GO>}

Next question comes from Stig Erik Kyrkjeeide in KeplerCheuvreux. You have had some expectations for late sales, which shifted from first half to second half to 2019. Can you give an update on how this has turned out in Q3 versus your expectations? And if the opportunity set for 2019 has changed on the way or the other, one way or the other?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

And this is related to the same topic, we -- I addressed on the first question. We, as we say, are delivering enlightenment into our expectations that means our sales are -- in Q3 are in line with what we thought and quite strong, but some of those sales or quite a few of those sales show up in the bucket of pre-funding instead of the bucket of late sales, and therefore it could appear that our sales are lower than what they actually are, but that is what drives the very high pre-funding level of 125%. So, sales are in line with our expectations for the second half.

**A - Bard Stenberg** {BIO 19147078 <GO>}

Then we also have another question. How would you describe the book situation for overall industry compared to last year?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

My impression is that also for the industry, the book position is quite a bit stronger compared to last year, where in the fourth quarter last year we had low utilization and one of our main competitor hardly had work as far as we could see. And that is not the situation we currently see for our competitors as well. Whether they are fully booked yet or not, I couldn't say but the overall industry booking is quite a bit better, seems good.

**A - Bard Stenberg** {BIO 19147078 <GO>}

Then we don't have any further questions from the web. I'm not quite sure if there's any further questions from the audience in Oslo.

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**Q - Terje Fatnes** {BIO 4311623 <GO>}

Terje Fatnes, SEB. Follow up to Gottfred on refinancing in cash flow in Q4. With the majority of fleet working on the contract side. And obviously you have with your guidance on pre-funding, very high pre-funding rates for Q4. How do you see cash collection in Q4? As it looks, EBITDA will be then north of \$200 million for the quarter.

**A - Gottfred Langseth** {BIO 5277539 <GO>}

Actually, we expect strong cash flow in Q4. I do not want to quantify it and it obviously could be impacted by working capital status over the year and which doesn't matter so much in the reality, but in a way would obviously impact the exact number for the quarter but we expect to deliver strong cash flow in Q4 and we say over the next two quarters.

**Q - Terje Fatnes** {BIO 4311623 <GO>}

And final one on the high yield, is one alternative really to just repay the high yield since you will have more than enough cash to do that in December next year?

**A - Gottfred Langseth** {BIO 5277539 <GO>}

There are a number of alternatives and I think we will stick with our plan and not to start discussing these individually.

**Q - Terje Fatnes** {BIO 4311623 <GO>}

Okay, thank you.

**A - Bard Stenberg** {BIO 19147078 <GO>}

Any more questions from the audience in Oslo? If not, we have one last question from Morten Nystrom in Arctic Securities on the web. Somewhat related to what we've discussed before, but based on the MultiClient projects, which still are in processing phase and the MultiClient projects you will acquire in Q4. What kind of pre-funding levels do you expect for the fourth quarter?

**A - Rune Olav Pedersen** {BIO 16158611 <GO>}

Yeah, I think we will just repeat that we expect full year 2019 pre-funding to be in the high end of the target range of 80% to 120%. And the actual refunding level in the fourth quarter will also depend on the same topic we have discussed how much of a -- the sales will happen in surveys which are in the processing phase and how much will happen -- sales will happen on let's say service which are completed. So there is a little bit of swing factor, but we still see a high pre-funding level for the year given where we are today.

**A - Bard Stenberg** {BIO 19147078 <GO>}

If there's no further questions, that concludes the Q3 2019 presentation. So thank you all for coming. And thank you all for watching us on the webcast, and have a nice day.

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