Q3 2020 Earnings Call

Company Participants

- Bard Stenberg, SVP of IR & Corporate Communication
- Gottfred Langseth, Chief Financial Officer, Executive Vice President
- Rune Olav Pedersen, President, Chief Executive Officer

Presentation

Bard Stenberg {BIO 19147078 <GO>}

Good morning, and welcome to this audio cast presenting PGS third-quarter 2020 results. My name is Bard Stenberg, Vice Presidents Investor Relations and Communications in PGS. With us from management today are President and CEO, Rune Olav Pedersen and CFO Gottfred Langseth. Before we start I would like to give some practical information. Participants on this audiocast can submit their questions via the audiocast platform. I would also like to draw your attention to the cautionary statement in today's earnings release and presentation, and the risk factors disclosed in our 2019 annual report and the Q3 2020 earnings release.

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

Rune Olav Pedersen {BIO 16158611 <GO>}

Thank you, Bard. Our third quarter 2020, we experienced in a very challenging seismic market and our revenues were of course impacted negatively by this. Also worth noting from the third quarter is that we almost exclusively did multi-client acquisition only very few days with contract acquisition in this quarter. On a more positive note in the third quarter, we realized a substantial part of the cost reduction. We have a guided on namely that we will go down to below $400 million going forward. We are more or less there. And the new organization, the new smaller organization is now fully operational. On the 25th of September, we announced agreement in principle with the majority of our lenders, deferring debt maturities and amortization by two years and last night we announced the next step in this process where we now have signed binding agreements with an even larger majority of our lenders and Gottfred will come back to this point in detail in his review.

Going forward, we expect higher revenues from vessel operations and from multi-client sales. Moving on to the financial summaries, which I will do very briefly, just pointing to the lower revenues of $116 million. This is segment numbers which obviously is low even in an historical context. Slightly more positive, we were able to deliver a segment EBITDA of $88 million on this very low revenue which is mainly driven by the fact that we have realized significant cost reductions in the quarter. The order book stood at $160 million at quarter end, which is a slight uptick from the very low level we recorded in the second quarter 2020. Of the order book approximately $52 million is relating multi-client acquisition. The vessel booking we have booked 11 vessel months in the fourth quarter. We have 6 vessel months in the first quarter 2021 and we have only booked one month in the second quarter 2021. As such it is clear that we will experience stand by time in the fourth quarter, but we obviously aim to book more vessel months also in the fourth quarter going forward. 2020 guidance and we now guide on the group cash cost below $450 million and this is still excluding approximately $30 million of restructuring costs.

MultiClient cash investments we now see at approximately $225 million and we will use approximately 65% of our active 3D vessel times in MultiClient.

CapEx we now guide below $40 million.

And with that, I give the word to Gottfred.

Gottfred Langseth {BIO 5277539 <GO>}

Thank you. First on the consolidated key financial figures on that couple of comments, the segment revenues of $116 million is in accordance with our pre announcement earlier in the month. And as you can see, this is a more than 50% reduction from the Q3 numbers or revenues last year, the segment EBITDA $88.4 million, I can observe is somewhat higher than expectations, and this is as already touched upon, related to significantly lower cost level in the quarter.

Segment EBIT, excluding impairments and other charges of $0.5 million. One last comment on this slide. The as-reported revenues and numbers to that is based on IFRS15 for revenue recognition for multi-client pre-funding are quite significantly lower both in Q3 and year-to-date compared to segment, as you're aware due to difference in when revenues are recognized. We do expect that this difference will reduce substantially in the 4th quarter.

And then the next slide Q3 operational highlights, our total segment multi-client revenues were $78.7 million in the quarter, with a pre-funding level of 89%. Late sales, $28.3 million. The contract revenues were only $9.3 million in the quarter and we virtually had no acquisition with our vessels in contracts, so only 2% of total time which is a handful of days.

We recorded other income in the quarter of $23.6 million, this is primarily Government grants. Segment MultiClient revenues by region. When it comes to pre-funding revenues, the main contributors were the areas Middle East, Europe and North America. As for late sales that was mainly contributed by sales from our library in Europe and South America.

Moving to the next vessel allocation and utilization. We had 71% active time in the third quarter. Five vessels in operation during the quarter, which is also what we plan to keep in operation going forward and through the winter season. We do expect stand by time in the fourth quarter. The next slide, cost focus. We have now completed most of our implementation of measures to reduce our cash level to below $400 million on the run rate basis. So on a run rate we are more than 33% down since the start of the year, and as you can see we are already down to $82 million in the third quarter, which is a significant reduction sequentially from the second quarter and even more so from the first quarter.

I will move to the cash flows summary. Cash flow in the third quarter obviously impacted by the lower earnings, we had cash flow from operations of $65.9 million. Otherwise one item here that may need some explanation and it may be a bit complicated, that there's an increase in non-current restricted cash related to debt service of $11.9 million in the quarter. This is result of amount transferred to retention accounts for debt service, the ECF debt service during the quarter and as such, amount remains on the locked or restricted accounts following the agreement with the ECF lenders to not pay the September installment. So the debt service amount remains on a bank account rather than having been paid to that installment.

When the debt rescheduling transaction completes the funds will be used for debt service on the ECF loans going forward and for the nearest years that means interest payments. We did receive all of this $23.2 million of government grants in the third quarter. Balance sheet liquidity reserves $194.1 million as a result of our debt being in default. As of quarter end. All our interest-bearing debts are classified as current pending the finalization of the ongoing transaction to reschedule debt. When we finalize the reclassification will be reversed to long term debt again.

Then Slide 15, summary of Debt and Drawing Facilities and these are the existing facilities and agreements before the rescheduling and just to repeat myself this as of the quarter end and as of today, the facilities are in default. There are mainly three elements of our debt summarized here, it is the term loan tranches which in total is $522 million. There is a RCF in two tranches at a total of $350 million, and then it is the -- Japanese export credit financing or ECF at an amount of $298 million. So these are important to keep in mind if you want to follow the discussion on the subsequent slides.

Then I move to the agreements to reschedule debt, and this first slide is still a little more, call it formal one with the more legal language on it, but in short we have now signed binding agreements with 79.6% of the amount of the combined RCF and TLB, and with the $300 million ECF lenders. We will work towards achieving 100% support from the TLB and RCF facilities and we have launched the transactional proposal to all of the term lenders now, and as there are a number of supporting amount up to now only consists of the ones that we have been brought private to be able to discuss the solution. So there will be a solicitation process for the term lenders over a bit more than a week. If we do not get to 100% among the RCF and TLB on aggregate, the transaction will be implemented by use of an English law scheme of arrangement.

Already to date lenders sufficient to meet the relevant scheme approval levels or majority levels have entered into a binding agreement to support the implementation of the transaction. The relevant approval levels are 75% by amount and 50% by number of lenders. If we achieve 100% support, we expect to complete the transaction in Q4. If we have to go through a scheme, we expect to complete in Q1 2021.

Then I move to main terms of the transaction and let me first say that we have been able to achieve a solution or their solution that we wanted to achieve and in reality also what we need to achieve to manage the challenging and market circumstances. There would be no scheduled debt maturities until 20 September 2022. The $350 million RCF will become TLB or term loan and the combined term loan, the existing one and the RCF that moves into becoming a term loan of approximately $870 million will have a repayment profile where $135 million is repaid in September 22, $200 million in September 23. And in addition to this, there will be a quarterly amortization which start in March 2023 of approximately $9 million. When it comes to the ECF amortization over the next two years aggregating $106 million will be or has been deferred and this amount will be then amortized or repaid over four quarters starting in December 2022.

There will be an excess liquidity sweep for liquidity over $200 million. And this sweep will be applied to the deferred amount under the ECF and the first -- the $135 million TLB amortization until they have both been repaid. After that a liquidity sweep of $175 million or liquidity over $175 million will apply towards the TLB.

The maintenance covenants have been reset starting at 4.5 times through June next year and the stepping down to 4.25 times through the end of next year. We will issue an a convertible bond of an amount up NOK116 million, the bond will be convertible into PGS shares at NOK3 [ph] and the lenders under the RCF and the TLB facilities will have a pro-rata right to subscribe for the CB against converting corresponding amount of their existing secured debt into the convertible unsecured loan. Certain lenders or under the TLB have undertaken to subscribe for or call it backstop, 80% of any unallocated amount after the lenders have made their election.

We will pay fees to lenders and across the lender groups of up to $7.6 million and in cash and up to $9.9 million or, call it, $10 million in kind and in-kind means that there is a fee that is added to the loan balance and repaid over time with the loan. We will -- these amounts exclude our costs for legal and financial advisers for ourselves and for the lender groups. I then move to PGS pro forma debt repayment profile, I will be much shorter on this Slide, it illustrates the changes to the maturities and amortization profile that I have attempted to explain on the previous Slide and in short as you can see from the bar charts, the agreements shifts all of the debt repayments due in the second half 2020 all of 2021 and first half of 2022, to the second half of 22 and later.

I then move to selected financial numbers provided to lenders.

As part of the discussions with TLB holders, we have shared certain financial modeling numbers, and we've shared exactly the numbers that are shown on this slide. Under the agreement, we are required to publish -- publicly disclose this information upon announcing the agreement, this is called cleansing. These numbers were therefore included in the slides that we put out last night together with the press release on the agreement with lenders. As you will see that this information provides indications over and above what we normally guide on or would want to guide on such as revenues and EBITDA or EBITDA percentage and certain other items. And you will be able to calculate that we forecast revenues for 2020 to be in the range of approximately $580 million and $630 million. We will not go into more detail on these financial model numbers, but if required we will be able -- we will be available to clarify in a way the definition or what is intended to be included in the various lines and particularly the ones towards the bottom of the table in the same way as we have done with the TLB lenders.

I think with that, I will give the word back to you Rune Olav.

Rune Olav Pedersen {BIO 16158611 <GO>}

Thank you, Gottfred. We'll now then move to the fleet activity in October this year. As you can see from the slides, you can see or five active, our operational, I should rather say, vessels in October 2020. We have the Ramform Titan moving to Las Palmas where she will do a crew change and get resupplies, and thereby move to the next job.

We will see the Ramform Atlas being working in Angola currently and then you will see further south, Ramform Sovereign which is currently standing by in South Africa and we are working on jobs for her in this region, but nothing has yet been secured.

The Ramform Tethys is moving towards Egypt, where she will join the Ramform Hyperion, which is currently working in Egypt and with that I'll go to the next Slide. So as I said Ramform Hyperion is moving in now working in Egypt and she mobilized for a multi-client campaign offshore Egypt early in the third quarter.

Now this multi-client campaign were primarily covers held acreage awarded in a recent licensing round. And this is an example of how our integrated service offering gives us additional opportunity to do work for our clients, which is both financially beneficial for us and for our clients. What happened was that there was a licensing round in Egypt and while the licensing round was moving through the system in Egypt towards ratification, we approached the client; the client approached us. We talked together because we have a multi-client license over this entire area. And what we agreed was that we would use our multi-client license to acquire the work program under license and acquire license in the block to be awarded and we started acquisition immediately after ratification -- formal ratification from Egypt to the client. This provides the client with a significant timing advantage. The alternative for the client would be to initiate in a tender process following ratification and which -- a process which, at a minimum takes 6 to 9 months.

Now we were able to start immediately after ratification and also of course then deliver data to the client much earlier than what would otherwise have been possible. So this is an example where we use our multi-client license to shoot an area which typically would have been shot using a contract business model. For us, it doesn't matter whether you do it, one way or the other as long as it makes financial sense.

Ramform Tethys will then move or join Ramform Hyperion and shoot neighboring blocks therefore expanding this to become a fairly large multi-client campaign covering several blocks and also some areas outside not covered by blocks and we expect them to be able to realize sales from oil companies farming into this blocks and also from the block holders who want to acquire data outside of their blocks to understand the bigger picture of what's going on inside their blocks, so this is a very good example of how our integrated service offering works so that we can create value both for PGS and for our clients. And we expect to have these two large Titan class vessels operating in Egypt into the first quarter of 2021 as there are other opportunities in the area in addition to the work we have already secured.

So moving then to the contract leads and bids volume, you should be familiar with this, but to repeat the dark blue line in the graph is the value -- the dollar value of all the bids we currently have in-house. The light blue line is the value of those bids plus the value of risk weighted value of the leads we currently see and it is encouraging to see that the leads basket [ph] the leads graph in particular is now picking up meaningfully. And this is primarily re-emerging of the work that we saw in the first quarter this year, which was pulled from the market as a consequence of the COVID-19 pandemic and the impact on the oil market, now coming back for acquisition primarily in 2021.

We have not yet seen the contracts for the 2021 in North Sea season, and we expect to see these bids trickling in, in the fourth quarter and in the first quarter and we therefore expect a similar trend to the bid activity going forward. But as we have mentioned a few times, the contract activity in the fourth quarter will be quite low.

Now moving to the supply side, we now see an average 2020 capacity, which is approximately 20% lower versus the average of 2019. In addition to that, we see deteriorating utilization levels versus 2019 in 2020. And over the winter, we actually expect less than 15 3D vessels in operation during this winter season. And that level is the lowest level of 3D streamer supply we have seen or observed in our market since the mid-1990s. So it tells you a little bit about how hard the COVID-19 pandemic and the consequences it has had on the oil market and therefore on the seismic market. Yes, it tells you a lot about the impact.

We do expect a moderate capacity increase for the 2021 summer season and we see as I explained on the previous slide, an increase in leads for 2021 which is encouraging for both the first and the second half of 2021.

Moving then to the summary, seismic market remained very challenging in the third quarter 2020. We have realized substantial cost reductions and they have -- they're showing up in our numbers already in the third quarter. Our new and leaner and more simplified organization is now fully operational. We have -- as you have heard signed binding agreements with the majority of our lenders to defer debt maturities and amortization by approximately two years. And we do expect higher revenues from vessel operations and multi clients' sales going forward.

And with that, I give the word back to you Bard.

Questions And Answers

A - Bard Stenberg {BIO 19147078 <GO>}

(Question And Answer)

Thank you, Rune Olav. We have some questions here from the people on the audiocast. So we start with John Olaisen from ABG. Congratulations on solving the short-term debt problem. Good work. May I ask what management is thinking about the current debt level in a longer term perspective? Two years will pass quickly, 2021 look likely to be great free cash flow year and then suddenly we are in 2022 when the big debt maturities will find place, has management started planning on how to tackle the big debt maturities in '22 and '23.

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

Thank you, Jon. We expect to be able to manage the debt maturities out of cash flow up to late 2022. We agreed to the first part of your question in a way as we've said fairly consistently for a couple of years. Anyway, our debt level is higher than it should be. And our goal is to reduce it to approximately half as consistently said over a couple of years.

The current situation caused by the COVID-19 has set us back a couple of years with respect to where the track we were on, which would have made us able to get to the targeted level over a couple of years that we will now be a couple of years later.

A - Bard Stenberg {BIO 19147078 <GO>}

Then we have next question from Jon Masdal in DNB Markets. Your financial guidance implies Q4 sales of $162 million to $212 million. Can you please confirm that this is still a stands? If not, what has changed your base case outlook? And how does this impact the long-term revenue outlook?

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

These projections were as I believe is implicated or indicated in the question. Obviously, we provided to the lenders earlier this year as part of the transaction. However, we would not have released them to the market today, if we did not stand by the guidance also today. So, I can confirm that this is still management's view of 2020.

Of course, these are an estimate and we are early in the fourth quarter, and as most of you listening will realize a lot of sales happen in the fourth quarter potentially, and it happens late in the fourth quarter. So there is obviously uncertainty related to any estimation at this stage. But what we stand by the numbers we have provided out to the market today.

A - Bard Stenberg {BIO 19147078 <GO>}

Now we have another question from John Olaisen in ABG. How many of the lenders of the $135 million RCF due in 2020 have accepted the proposal?

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

Should we comment on number of lenders? I think we refer to what we say in the press release from yesterday that I don't remember the exact, it is 50.7% have accepted. And then the remaining approximately 49% have not yet signed the agreement.

FINAL

Bloomberg Transcript

A - Bard Stenberg {BIO 19147078 <GO>}

Then Mr.Olaisen continues. You are right, that you expect higher revenues from vessel operations and MultiClient sales going forward. Do you have any tangible signs that Q4 late sales will be strong this year?

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

Well, when we indicate the level we are doing and as I just commented on Mr.Masdal question it's because we have a fairly healthy leads basket of -- for the fourth quarter and some of those leads are quite mature. And we expect to realize them in the fourth quarter.

So it is a combination of leads that we would have hoped to have realized earlier in this year. But is now coming to a stage where it isn't mature enough that we believe we will realize it in the fourth quarter and obviously, just a view of the total opportunity basket for the quarter, which together with our vessel operations, combined sums up to the guidance we have given. But as I said, these are of course an estimation only and we are early in the quarter.

A - Bard Stenberg {BIO 19147078 <GO>}

Then John Olaisen has more questions. How big are the costs for legal and financial advisors for PGS and the lender groups?

A - Gottfred Langseth {BIO 5277539 <GO>}

It's a little bit depending on whether we are not -- while I'm start speaking while thinking about whether I would give you a number variable. I think it's fair to -- anyway it is significant that we are talking about the advisors for the three different lenders -- lender groups including for the company. So it will be at least $10 million I can say.

A - Bard Stenberg {BIO 19147078 <GO>}

Now we have the last question from John Olaisen. You are assuming an average vessel utilization of 85% for the next four years. Is that not that optimistic given the fact that the average vessel utilization has been 79% over the last 10 years?

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

May well be. We have had some challenging year behind us, where we have in several of those years met significant headwind of having to reduce capacity. And obviously in those years utilizations are worse than what you see in a gradually improving market, which or even a flat to gradually improving market. So yes, they may be optimistic, but I don't think we're going to be far off.

A - Bard Stenberg {BIO 19147078 <GO>}

We have a question from Christopher Mollerlekken in Carnegie. With a global fleet of 15 vessels this winter does PGS plan to reduce the number of operational vessels down from current five, and if so to what level.

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

We don't know -- we have no plans to reduce our operational fleet from five. So we will keep the fleet of five operational through the winter. If we are not able to secure a full utilization on all these five vessels, we are able to take out most of the cost even though for a shorter stand by periods and the entire winter, the way we've currently set up our organization.

A - Bard Stenberg {BIO 19147078 <GO>}

And we have a question from Kim Andr Uggedal in SEB. Can you specify what is the additional collateral added to strengthen the lender security package?

A - Gottfred Langseth {BIO 5277539 <GO>}

Yes, it is primarily, anyway, collateralizing all the shares in subsidiaries and also certain other assets including inter-company receivables between certain -- of our subsidiaries.

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

To kind of specify, I always say that the lenders add share, purchase overall material subsidiaries, they now have overall the subsidiaries not only the material ones.

A - Bard Stenberg {BIO 19147078 <GO>}

Then we have a question from Sahar Islam in Goldman Sachs. You talked about improving the demand through 2021, are there particular areas, which look more resilient? And where you do you expect to see the recovery?

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

Yes, I think we will see the recovery primarily in the areas where there are fairly stable and regimes with licensing rounds and where there are proven petroleum systems working. So we expect continued activity in the North Sea area. We expect continued activity in Canada. We expect continued activity in Brazil and parts of West Africa, the more attractive parts of West Africa, in particular Angola. And also as you can see from our vessel dispositions parts of the Mediterranean. So, I think those are the areas where we would think that we will see most activity as you have the combination of licensing rounds and prospectivity which is needed to see activity in a call it a lower market or a weaker market.

A - Bard Stenberg {BIO 19147078 <GO>}

And then she also has a follow-up. On the vessel side, what do you expect industry supply and pricing to do in 2021?

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

We expect industry supply to pick up somewhat in 2021, as we expect the demand to pick up somewhat. We don't expect obviously a very -- hockey stick increase in demand or anything or supply for that matter. It's more of a call it flat to slow increase demand and I think supply will follow that, but I think we'll see the supply side, which the question was picking up somewhat into the summer season of 2021.

A - Bard Stenberg {BIO 19147078 <GO>}

Then we have a question from Amy Wong in UBS. Please talk about the type of work your clients are requesting. Has there been a notable change? More 4D, 3D different acquisition techniques? If there is a change in product and service demand how is PGS positioned for that?

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

Yes. What we can say currently is that a lot of the work being done is either I would say, 4Ds that needs to be done or exploration seismic in relation to or triggered by licensing rounds such as the activity we see in Egypt which is proper exploration seismic but it is triggered by seismic equipment in licensing rounds and the operators there, have specific targets in mind, also the activity in terms of whether it is different acquisition techniques, I would say that, we don't see the trend and that we saw when the oil price dropped from $100 to what was it now, $30 or something, where cheap seismic was the only thing that mattered. We don't see that trend now. It is clear that the money spent is Brent targeted, sometimes if you don't need a particular acquisition configuration you will, do more call it (inaudible) seismic. But when there is a target where it requires more advanced seismic, the clients will apply more advanced seismic to -- at a target. So we see more of a selective spend, I think it's driven by primarily by our licensing rounds or by necessary 4D. So what we see less of I think is the big 3D exploration seismic which is not driven by licensing around activity.

A - Bard Stenberg {BIO 19147078 <GO>}

Then we have another question from Stig Erik Kyrkjeeide in capital Kepler Cheuvreux, no segment impairment on MultiClient Libor year-to-date. Did you complete impairment tests in Q3 or would that be done in Q4? If in Q4 any comments to add on the impairment risk you see?

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

We review our portfolio surveys for impairment triggers every quarter, but in a way, the full review and full update of all different surveys with respect to sales forecasts is done annually and at year-end. Whereas in the quarters we do that on surveys where there is good reason to expect that there could be an impairment. There's always a risk of impairments of some surveys when we get to year-end. We will see that most years. Other than that we -- I don't think, I would speculate the outcome of our sort of year-end impairment review and sales forecast update for the library.

A - Bard Stenberg {BIO 19147078 <GO>}

We have a question here on whether we can tell about what we've done to reduce costs in 2020?

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

Yes, of course. There is a big suite of initiatives, obviously that were initiated more or less immediately after we understood what the COVID-19 -- the impact it would have on the oil market and the impact it would have on the seismic markets, initiated in March basically last year. The most important of those, the most painful of those obviously is that we have reduced our vessel capacity from eight vessels to five operational vessels. We have then also in that context also reduced the number of crews down to a level of more or less down to a level of 4 vessels, so that we have a flexible crew model, so that we are able to take out cost also, if we don't have all vessels in operation, even if they are standby, we can have a minimum crew on board and not pay for a crew at home.

And then we have reduced the number of office-based personnel significantly. During the year it is some 40%. I believe from where we were when we entered into the year. As part of that, we've, of course, reduced the number of consultants working in the company and that reduction of employees has taken in a place, not let's say from the bottom. So that we now have no more costly managers and less employees, it has been across the board, so that we have been able to retain the same distribution between managers and the employees as we had before. And this reorganization and we have in a way simplified and made our structure leaner.

Then we have obviously been in dialogue with our subcontractors to see whether we can find a solution which is acceptable for both parties, both us and our subcontractors. We have obviously as everyone else saved quite a bit on travel. However for us we also get an increase in travel costs, it is more expensive to move our crews around for crew shift. So the travel costs saved is also increased in the crew travel as in, therefore we believe that we don't -- we won't see a spike up again when travel gets back to normal. We have closed down offices as well and we have closed down imaging centers with the cost that comes with running a center, machines and things like that. That was at least some of the initiatives, we have done which I could go just go and comment on the back of my head here.

A - Bard Stenberg {BIO 19147078 <GO>}

Yes, thank you Rune Olav. There seems to be no further questions at this point, we can wait or pause for a minutes to allow people to type in their questions if there is any last minute questions. As it seems to be no further questions from the audience. We thank you for participating and have a nice day.