

## Q1 2020 Earnings Call

### Company Participants

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

### Presentation

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

Good morning and welcome to this Audiocast presenting PGS First Quarter 2020 Results. My name is Bard Stenberg, Senior Vice President, 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 presentation and the risk factors disclosed in our 2019 Annual Report and the Q1 2020 earnings release.

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

#### **Rune O. Pedersen** {BIO 16158611 <GO>}

Thank you, Bard, and good morning, everyone. The first quarter 2020 obviously became a very strange quarter and highly impacted by the Coronavirus, COVID-19 pandemic and the consequences thereof, but it started out quite positive and we had a good outlook. We were seeing increasing prices, we had a strong backlog, and we, in January, successfully completed the refinancing and equity raise, and looked set for good 2020.

In Q1, we also experienced strong cash flow from operations, which obviously mainly came from the revenues we generated in Q4 of '19 and we executed on all acquisition programs according to plan, with eight vessels in full operations. Then, in late February, early March, the Coronavirus hit and it all turned around for us and all the companies in our industry.

MultiClient revenues suffered more or less immediately and the late sales suffered from no commitment in March, which is the last month of each quarter, where we make most of our late sales. Everything was pulled out and we also saw delayed sales and delayed engagement related to pre-funding and delayed governmental processes, which also impacted our pre-funding revenues. And more importantly, we are now facing a very

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challenging medium-term market outlook and we need to reduce cost and capital expenditures going forward.

So then to the financial summary. I am going to be brief here. Segment revenues of \$168 million. And then, I can just point to the fairly strong cash flow from operations of \$176 million. Before I move to the next slide, the order book.

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The order book stood at \$217 million at as of March 31, 2020, and that is a fairly large decline from the levels we saw in Q3 and Q4 of '19, obviously, impacted by the fact that all the work and all the negotiations we were doing, the exclusive negotiations where we believe we would land contracts, pre-funding going forward, in March, have most of it been delayed and we have not been able to conclude it and put it into the order book.

You can see that in the vessel booking as well. In the Q2, we have booked 18 vessel months. So we are more or less fully booked for the quarter. In Q3 '20, we have looked only nine vessel months, and in Q4 2020, we have not booked any vessel months. So obviously outlook for the second half of 2020 is very weak and it is uncertain what we will do when we get to that time frame.

So next slide, impact of COVID-19 and low oil price. Energy companies deferring investments to next year is the main heading here and what we are seeing a lot of. Substantial reduction on medium term seismic demand, most new projects have been postponed or negotiation substantially delayed, and increase in request for delayed payment terms we are also experiencing.

So how are we responding to this. You have seen us earlier a few weeks ago that we made an announcement that we will cold stack two of our eight vessels already in Q2. We also plan to warm stack one additional vessel in Q3. And we will assess further capacity adjustments continuously and we are prepared to react quickly. We will focus on keeping utilization high over keeping a lot of vessels in the market. So we are ready to go even deeper than this if necessary.

Our 2020 gross cash cost reduction is as of today, at least, \$100 million and further reductions are likely to come in the coming quarters. This is the process, which are currently ongoing and therefore, we are today communicating what we have done so far and we expect to communicate more in the coming quarters.

This comprise obviously of less capacity in operation. We will instigate temporary layoffs over the next days. There is a 2020 salary freeze across PGS, so no salary increases in 2020. We have canceled the 2020 bonus plan. We do get some benefits from exchange rates and fuel cost, obviously, and there are multiple other initiatives both implemented and under assessment.

So capital expenditures, we are reducing with at least \$30 million. Obviously, there are CapEx already committed as we had thought 2020 would look very different. And therefore, currently we are communicating that it is down only \$30 million. And we are reviewing alternatives to preserve liquidity, which we will also come back to later.

So with this, we are updating our 2020 guidance. Group gross cash cost below \$500 million; MultiClient cash investments in the range of \$150 million to \$200 million; and approximately, we believe, 50% of our active 3D vessel time allocated to MultiClient. I must emphasize that this is obviously fairly uncertain. You saw the booking numbers for the second half, which are fairly low. So where we will end up in this interval is as of today unclear.

Capital expenditures below \$50 million and we will target to be cash flow positive before debt repayments for 2020.

And with that, I give the word to you, Gottfred Langseth.

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

Thank you. Key financial figures, I will revert to several of these in later slides, but a few comments here. A relatively muted quarter due to the challenging last month, still revenues for the quarter, \$168 million, is up 15% compared to last year. EBITDA of \$80.5 million is up 21%.

Segment EBIT for the quarter was a loss of \$15.8 million. We did record an impairment charge on vessels going to cold stack of \$51.4 million and a \$25 million impairment of the equity stake in Azimuth in the quarter.

On the operational highlights, total segment MultiClient revenues \$74.2 million. We had a significant slowdown of sales in March due to the pandemic reducing customer availability and slowing governmental block award processes, as well as obviously the significant oil price reduction. The pre-funding was 68% in the quarter, negatively impacted by delay of block award ratification relating to specific project that we have or had ongoing.

Late sales for the quarter at \$33.5 million. Contract revenues \$85.4 million, good production on the fleet through the quarter. MultiClient revenues by region, in Q1, the pre-funding were primarily from projects in Asia-Pacific and Africa. Europe was the main contributor to late sales.

Vessel utilization, high utilization in Q1, 90% active vessel time, all eight vessels more or less in full operation. From early Q2, we will go down to six vessels in operation with the cold stacking of Sanco Swift and PGS Apollo. The current base plan is to warm stack one vessel in the third quarter. Further capacity reductions will be implemented if required.

Moving to cash cost, Q1 gross cash costs of \$154 million impacted by high activity level with full operation of eight vessels and on average operation in relatively high cost areas. For the full year, cash cost will be below \$500 million and we will see a significant sequential decline in the second and third quarter.

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Cash flow, Q1 cash flow was strong. Cash flow from operations of \$176 million, the key driver was the significant release of working capital as already discussed when we released the Q4 '19 numbers. We do expect some pressure on working capital for the remainder of the year as some customers are seeking delayed payment terms to get projects off the ground now in 2020.

Balance sheet, net interest bearing debt has reduced \$131 million in the quarter to end at \$876 million. Liquidity reserve increased to \$266.9 million, fully held in cash. We are glad that we managed to successfully complete the equity raise and refinancing in Q1. With the outlook at the time, this refinancing would with quite a large headroom bridge us into the capital structure that we strategically aim for.

With the dramatic subsequent changes after completion, the refinancing puts us in a stronger position to manage a challenging period ahead. We are currently reviewing alternatives to preserve liquidity, including possible extension of scheduled RCF reduction, amortization holidays and other debt related initiatives.

This next slide shows firstly overview of our debt and drawing facilities. I will not review the details here, since this is well known to most of you, but note that the \$350 million revolving credit facility was fully drawn by end of the first quarter.

Gross cash costs, our initial cost guidance for 2020 was \$600 million. The updated guidance based on implemented initiatives is a gross cash cost below \$500 million. The primary drivers for the reduction are illustrated and shown on the graphics on the slide. We are working with further cost measures and further reductions are likely in coming quarters.

CapEx, with the lower activity level and less vessels in operation, we are reducing the 2020 CapEx from initially \$80 million to below \$50 million. With the cold stacking of two vessels our need for seismic equipment is significantly reduced and which should make us able to keep CapEx low.

I will stop there and give the word back to Rune Olav.

**Rune O. Pedersen** {BIO 16158611 <GO>}

Thank you. Gottfred. Next slide is the fleet activity in April 2020. And as you can see, we have started in the North Sea with the Ramform Tethys on a MultiClient survey in East of Shetland. We have our Ramform Titan in Brazil doing work there and we have the Ramform Vanguard steaming to the North Sea.

Sanco Swift is steaming to Norway for stacking as we have communicated. Ramform Sovereign is in Angola. And Ramform Atlas and PGS Apollo both doing contract work in South Africa currently. And the Ramform Hyperion is in PNG completing a job there.

If we move to the next, we can see that we will see a significant demand drop. The decline in the seismic contract leads and tenders is driven by lower investments among our energy companies. And when looking at the curves, you can see that they are dropping, but really not dropping to the extent that I am communicating.

And the reason for that is, more or less that projects currently have been delayed rather than canceled. So what we are hearing from our clients currently is that, they are delaying their projects into 2021 and not canceling them. Therefore, they remain as of today in the curves, but it is important to point out that what we're seeing in the very near term is more dramatic than what you can read out of curves. Contract prices are also expected to drop and the price decline is not reflected in the curves either, which is also normally the effect when going up.

So just to repeat, we have limited visibility for the second half of 2021, but right now, it looks somewhat more positive until 2021 as these projects have been delayed.

On the supply side, we expect the average 2020 capacity to be lower than the 2019 capacity. And I must say, we do expect significant supply reductions from now on. We are taking out, as you've heard, two vessels in Q2, and we plan to take out of the third vessel in Q3. We expect the remaining players in the industry that they have to adjust capacity to the new demand level as well. And the seismic industry has proven in the past that it response rapidly to drops in demand.

So the COVID-19 pandemic delays our financial strategy. As most of you know that follows us, we have a financial strategy with three pillars: profitability before growth; return on capital employed; and capital structure to sustain a future downturn. This last pillar includes a strategy of debt reduction, and obviously the COVID-19 pandemic postpones this strategy.

Our longer-term view is that, what we are now experiencing is a temporary imbalance in the oil market, which spills into the seismic market. It is caused by the dramatic drop in demand for oil caused by the current pandemic and how the world reacts to it.

Our longer-term view is that, when the world normalizes and gets back to more normal activity, demand will continue to increase in the long term and oil and gas will be an important part of that mix. When that happens, we also expect a recovery in the seismic market and that recovery maybe strengthened by the fact that the seismic players we expect them to take out capacity now during the short term.

So in the short term, we will focus on securing sufficient liquidity, protecting our cash flow and in the short term, we cannot continue the planned debt repayment strategy, but when the market returns, and we believe the market will return when the world normalizes, we will obviously regain our position to continue on the planned strategy on debt reductions. So we are committed as a Company to get through this and we're committed as a Company to continued debt reductions when we are through it.

So in summary, Q1 successful, completed equity raise and refinancing, experienced weak MultiClient sales, and most important, we have a very challenging market outlook with substantial near-term exploration and production spending reductions.

We are in the process of implementing significant cost and CapEx reductions. And as I've said, you should expect to see more than what we are today announcing going forward. We will focus on preserving our liquidity in the near term. We will target to be positive cash flow before debt repayments in 2020, and we will resume our debt repayment strategy when the market recovers.

And with that, I hand over to you for Bard for Q&A.

## Questions And Answers

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

Yeah. Thank you, Rune. We have some questions from the web already. First question comes from Terje Fatnes in SEB. When do you have to make a decision on the first option for charter extension of Sanco Swift and what are your current thoughts?

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

The Sanco Swift is on charter until 2023, the option exercises are I believe six months ahead of the end date.

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

Next question comes from John Olaisen in ABG. Are you already in negotiations with banks regarding possible extension of RCF reduction, amortization holidays and other debt related stuff?

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

We are in dialog with the banks. We are in the early stage of working with the proposed -- we're working with alternative solutions.

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

Next question comes from Monika in Societe Generale. Where globally do you see the most stress, most pushback from clients?

### A - Rune O. Pedersen {BIO 16158611 <GO>}

I think it's not easy to identify any region over another. What we have seen in this, call it, early phase of this crisis is that companies have pulled back their budgets everywhere and we expect, obviously, that would be the first phase. The first thing that happens is, all budgets are gone. And then, the second thing is that, new budgets are redistributed, new lower budget redistributed out to our clients and then some sort of activity will resume. It is difficult for me to say which regions, if any, will be hit harder than others at this stage.

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

Then we have a question from Jorgen Lande in Danske Bank. Of the \$217 million backlog, can you indicate the split between contract on pre-funding?

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

The pre-funding is \$89 million that we quote in the quarterly financial statement. And the rest is primarily contract. There is an element of imaging, which is to the tune -- a bit over \$10 million.

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

At this stage, we don't have any further questions, but feel free to post questions in the audiocast platform. So send me email by my direct email address or use the ir@pgs.com email address. We have one more question from Morten Nystrom in Arctic Securities. On your working capital commitment, does this imply that you expect working capital changes in Q2 and Q3 to impact liquidity negatively?

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

So we will not comment specifically on the quarters. We will only enter into agreements with deferral of -- parts of the payment into early 2021 to the extent that that is inside our liquidity capacity. For the remainder of this year, in a way, the working capital development will depend obviously on our revenues and our ability to keep the DSO at a modest level.

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

We have another question from Jorgen Lande in Danske Bank. Still early days in Q2, but can you comment if pre-funding negotiations and late sales discussion have restarted?

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

I think it's, as you say, early days in Q2. What I can say is that, we are engaging with our clients regarding new projects both on the contract side and on the pre-funding side. So I'd say, the immediate shock of no interaction has passed and we are once again discussing programs and funding with our clients. But it is too early to indicate anything to what extent that will impact either the second quarter or the third quarter, but there is client engagement again.

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

Then we have a question from Christopher Mollerlokken in Carnegie. Could you describe how do you plan to make crew changes going forward given the travel restrictions?

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

Yeah. That is a very good question and very challenging, clearly. We are, as you know, operating all around the world and we are operating in areas where it is possible to do crew changes. We have done one crew change last week, I believe, it was, full crew change in Europe. So we were able to do that with obviously several measures put in

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place to make sure it was safe from a health perspective. And then, there are other areas of the world where we have more problems doing crew changes. So we have agreed with our crews to stay on for extra terms in several of the vessels. And the crews in PGS are very motivated and supportive of the Company. We are very fortunate that way. So we have found a great support from our crews of staying on for longer durations in this crisis situation we are in. But crew changes is and will remain a challenge, but there is moving parts all the time here. And in some Western countries they have opened up for necessary travels for people like crews of the seismic vessel.

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

Then we have another question from Christopher Mollerlokken. Have you received the pre-funding, you missed out in Q1?

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

No. We have not and block is still not ratified. I mean the agreement is signed with the client, obviously, and the block is still not ratified. We hope and expect that will happen shortly, but these are extraordinary times.

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

Then, I have a question from Stig Erik Kyrkjeeide in KeplerCheuvreux. How much cannibalization will take place on Swift and Apollo when being cold stacked? And how challenging to eventually bring them back in 2021, 2022?

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

We will clearly use streamers of those two vessels and other seismic equipment into our pool of streamers. And as you see CapEx are reducing quite a bit, part of that is because we can defer buying new streamers and as you will say, cannibalize parts of the streamer sets of Apollo and Swift. I think it's fair to assume that we can probably bring in one of them fairly quickly. And the question of bringing in both back for example in summer of 2021 is a question of whether we will have enough streamers and other seismic equipment at that stage, or whether we would need to supply with new streamers full or partly or there are call it eight vessel.

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

Then we have another question from Stig Erik Kyrkjeeide. You are fully booked on the six active vessels in Q2. Can you comment on pricing you expect in the contract portion of that booking maybe comparing to pricing in Q2 last year?

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

No. I don't think I'll comment on pricing. What we have said is that, we obviously expect pricing to come down. And I must I guess stress that, in Q2, we have a lot more MultiClient ongoing than contract, but I am not going to comment on pricing, but we do expect it to come down year-over-year.

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

Then we have a another question from Christopher Mollerlokken. Will (inaudible) Sanco Sword leave the PGS fleet when the charter expires this summer?

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

We will communicate that when that decision has been made. I think you can make your own assumptions on what we are likely to do in that capacity.

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

Then we have a follow-up from Monika in Societe Generale. Do you still have 4D contracts and are you still having premium pricing on those jobs?

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

The answer is, yes. We still have 4D contracts. And I think it's too early to say whether yes or no. Yes, we still have premium pricing on those or not because we haven't seen a lot of contracts award in this, call it, new environment, but we obviously expect 4D and especially 4D where a GeoStreamer is a clear benefit, which is a lot of the 4Ds to carry at pricing premium going forward.

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

Then we have a follow-up from John Olaisen in ABG. \$500 million in cash costs and only five vessels in operation equals daily OpEx of \$270 per boat. I realize that you have cost related to MultiClient and processing, but first question is, if we are going to run only five, six boats on a permanent basis, then what would the run rate for the group cash cost be roughly?

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

Well, clearly lower than the \$500 million, which is obviously the 2020 guidance and includes the first quarter of running eight vessels and then second of six, plus the two vessels we are still have in operations or one in operation, one in streaming. I don't think we're ready to comment on the run rate cost for an operation like that just yet. As I said, we are in the process of implementing cost reduction and we expect our cost to come down even at the five to six vessel level. So it's a bit early for us to comment on that question, but it clearly will be lower than \$500 million.

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

Then we also have a question on MultiClient work in the order book, which is answered that's \$89 million? And then, you also one, there is how much of the nine vessel months booked for Q3 I guess related to MultiClient?

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

It is a majority of the Q3.

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

There is contract in there as well, obviously, but probably majority MultiClient.

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

Then we have a question from Morten Nystrom in Arctic. You're talking about improving liquidity. Are you also targeting reduction of the Japanese export credit financing facility, or is this primarily related to the revolving credit extension?

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

We will not go into this in a way this specifics of the options that we are evaluating at this stage.

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

Then Morten Nystrom in Arctic Securities also have a question regarding the MultiClient season in Canada this year. If we are planning to do MultiClient in Canada in 2020?

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

Yes, we are

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

Then we have a book keeping question from Mr. Mollerlokken in Carnegie. What's the impairment on Azimuth booked on results from associated companies? So total impairments in Q1 were \$76 million.

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

Yes. That is correct. The vessel related impairments, the \$54 million, is in line impairments and gain/loss on sale of assets. The Azimuth impairment is included in the line share of results from associated companies. So the total impairment is the aggregate of both.

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

Then we have a question from Samantha Osborne in UBS. What is the annualized cost saving on warm stacking a vessel?

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

We do not go into the details of that, but as an -- when we cold stack, more or less all of the costs are same and minute new sort of cost is to keep the vessel in stack, so all of the cost go away. With warm stacking the project related costs are gone and then quite a bit of the operating costs, so let's say, around two-thirds of the cash cost typically.

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

Then we have another question from Morten Nystrom in Arctic Securities. Are you concerned that we could see cancellations on pre-funding in Q2 and Q3 as clients refuses

to stick to their commitments?

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

I don't think that is very likely, no.

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

Then there is not any more questions at the moment. We can pause for a minute to allow you time to type any further questions you may have. Okay. That seems like there is no further questions from the audience. So thank you all for participating and goodbye.

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