Amplify Energy: 1Q 2019 Earnings Script

May 9, 2019 / 10am CT

Operator

Welcome to the Amplify Energy First Quarter 2019 Investor Conference Call. Amplify's operating and financial results were released earlier today and are available on Amplify's website at www.amplifyenergy.com. During this presentation, all participants will be in a listen-only mode. Today's call is being recorded. A replay of the call will be accessible until Thursday, May 23rd by dialing 855-859-2056 and then entering conference ID #7860565 or by visiting Amplify's website, www.amplifyenergy.com.

I would now like to turn the conference over to Martyn Willsher, Senior Vice President and Chief Financial Officer of Amplify Energy Corp…

Martyn Willsher

Good morning and welcome to the Amplify Energy conference call to discuss operating and financial results for the first quarter of 2019. We appreciate you joining us today. Ken Mariani, Amplify's President and Chief Executive Officer, will begin the call by updating our stakeholders on the company's recent merger announcement and first quarter operating results. I will follow with an update on our first quarter financial results.

First, we would like to remind you that some of our remarks may contain forward-looking statements and are based on certain assumptions and expectations of Amplify's management team. These remarks reflect management's current views with regard to future events and are subject to various risks, uncertainties and assumptions. Although management believes that the expectations reflected in such forward-looking statements are reasonable, it can give no assurance that such expectations will prove to be correct and undertakes no obligation and does not intend to update these forward-looking statements to reflect events or circumstances occurring after this earnings call. Forward-looking statements include, but are not limited to, our statements about and discussion of, second quarter and full-year 2019 guidance. Please refer to our press release and SEC filings for a list of factors that may cause actual results to differ materially from those in the forward-looking statements made during this call. In addition, the unaudited financial information that will be highlighted here is derived from our internal financial books, records, and reports. For additional detailed disclosure, we encourage you to read our Quarterly Report on Form 10-Q, which we expect to file later today.

Also, non-GAAP financial measures may be disclosed during this call. Reconciliations of those measures to comparable GAAP measures may be found in our press release or on our website at www.amplifyenergy.com.

With this in mind, I will now turn the call over to Ken Mariani. Ken…

Ken Mariani

Introduction

Thank you, Martyn. I appreciate our stakeholders joining us today. My remarks on this call will provide an update on our recently announced merger with Midstates, operational performance in the first quarter, and our updated guidance for 2019.

Midstates Merger

In the last year, our organizational focus has been to explore any and all opportunities to create value for Amplify's stockholders. This process began with a commitment to expand the processing plant at Bairoil and continues today as we are in the early stages of completing our previously announced merger with Midstates.

As was mentioned on our merger announcement call, we believe that this strategic merger has substantial advantages for the stockholders of both companies. The combination improves each company's asset base with a diversified platform of long-life, shallow-decline assets, and initial identified cost synergies of approximately $20 million per year will provide an immediate value uplift to the combined company. In addition, we will have a more diverse, lowrisk, PDP-focused asset base with a top tier free cash flow profile. The positive free cash flow generation and low leverage of the combined entity will provide additional capacity to accelerate capital returns and will position us for further potential market consolidation opportunities. Martyn will have some additional comments on the financial benefits of the deal in his remarks, but we encourage all of our stockholders and potential investors to review the merger presentation materials that were posted on our website. As a management team, we remain committed to creating shareholder value and look forward to executing on this tremendous opportunity.

Operations

Turning to operations, we performed slightly below our expectations in the first quarter due to production delays in our California and non-operated Eagle Ford producing areas, as well as an unfavorable adjustment to our non-operated production volumes in East Texas. As a result, we generated $19.0 million of Adjusted EBITDA in the first quarter, which was slightly below our guidance range of $20 to $24 million.

Production for the first quarter averaged approximately 21,500 Boe/d, which was below the low end of our guidance range for the quarter. As previously mentioned, first quarter production was primarily impacted by adjustments to non-operated East Texas volumes, along with a delay in completion activity for ten non-operated Eagle Ford wells and a slower response than anticipated to our California workover program. The East Texas adjustments were made in the first quarter 2019 but also impacted 2018 production volumes, resulting in a larger adjustment recorded in the first quarter production numbers.

Ten Eagle Ford non-operated wells were anticipated to begin producing in February, but were not brought online until the end of March. When they were ultimately brought online, production from these wells was in line with our expectations with an average IP30 of approximately 1,700 Boe/d. An additional ten Eagle Ford wells will be on production in May as originally anticipated. In California, Amplify continues to work over certain higher volume wells, which we now anticipate will be brought back online by the third quarter. These timing delays primarily impacted our first quarter results, and as such, Amplify is maintaining its full year guidance for Adjusted EBITDA, excluding the impact of the merger.

During the second quarter, we will also be executing a planned shutdown of the Bairoil plant for approximately 14 days for the annual turnaround and to install key equipment in advance of the Bairoil plant expansion scheduled to be completed in the fourth quarter.

Lease operating expenses in the first quarter were $28.9 million, or $14.96 per Boe, which was reduced from $29.8 million in the fourth quarter. LOE was in line with expectations on a total dollar basis, but missed guidance projections due to the lower production volumes that were previously described.

Capital spending for the first quarter was approximately $13.1 million, compared to $10.2 million in the fourth quarter of 2018, and below the low end of our guidance range of $14 to $16 million. The reduced capex was primarily due to a short-term increase in expense workover projects at Beta, which caused a deferral in capital workovers, and a well conversion project at Bairoil that was deferred to later in the year.

2019 Guidance

Earlier today we issued our updated guidance expectations for 2019, including forecasts for production, capex and free cash flow. We are currently forecasting full year production of 20,500 to 22,600 Boe/d, down from our prior forecast of 21,200 to 23,500 Boe/d. We anticipate production increasing with the completion of our Bairoil plant expansion project in the fourth quarter of 2019 and are evaluating additional projects from our portfolio of opportunities.

Our revised capital forecast range for 2019 is $58 to $66 million, with approximately 51% of the capital spending allocated to our Bairoil plant expansion. We also anticipate spending approximately 18% of our capital budget on the development of our non-operated Eagle Ford properties. The remainder of our budget will be allocated to capital workover and facilities projects across our portfolio. While this budget does not include a capital allocation for drilling at our Beta or East Texas properties, we are continuing to evaluate these opportunities and may supplement our capital budget later in 2019.

Free cash flow, which we define as Adjusted EBITDA, less capex and cash interest expense, is expected to be in the range of $12 to $24 million in 2019. Management and the Board will contemplate the best uses for our 2019 free cash flow, which may include funding additional development opportunities, further reducing our debt and / or returning capital to stockholders.

Outlook

As I look forward to 2019, I am excited for our future following the combination with Midstates. The pending merger provides us with a stronger and more diverse asset base, minimally levered capital structure and enhanced production and growth opportunities. Additionally, we will have increased optionality and capability to pursue external growth targets that are accretive to our platform. We believe this combination will create significant value for all of our investors, and we will continue to keep our stockholders apprised of our progress.

With that in mind, I would like to turn the call over to Martyn to discuss our financial results…

Martyn Willsher

Thank you, Ken.

Benefits of Midstates Merger

I'd like to start by discussing some of the financial benefits of the Midstates merger, followed by a review of our quarterly financial results, additional details on our liquidity, updated hedge position and revised guidance for the year.

In regards to the merger, the combined company's pro forma enterprise value of approximately $729 million indicates a significant discount to the pro forma proved developed reserve value of $960 million. We believe the combination of substantial synergy realization, consolidation of free cash flow generating assets, and quality reinvestment opportunities will help lead to value enhancement and close the disconnect between our assets' reserve value and combined company enterprise value.

The transaction also achieves benefits of scale through improvements in our production, EBITDA, and free cash flow profile. On a combined 4Q18 annualized basis, our two companies generated 40,000 Boe/d of production, $241 million of Adjusted EBITDA and $165 million of free cash flow. In 2019, we expect to generate at least $65 million of combined free cash flow, resulting in a top tier levered free cash flow yield of 15-25%.

In addition, the transaction is expected to result in significant cost savings realization with approximately $20 million of annual G&A savings. Based on FY 2018 results, our combined Cash G&A expense would decrease significantly for the combined company to $1.64 per Boe, which is less than half of the average of our peer group.

Furthermore, the combination of the two companies will result in a stronger balance sheet with a leverage ratio of approximately 1.2x on a 4Q18 annualized basis. The combined company will differentiate itself by its ability to generate greater than 10% free cash flow while maintaining leverage less than 2.0x. Our free cash flow generation, strong balance sheet and favorable liquidity position will provide us with flexibility to make capital allocation decisions that are in the best interests of our stockholders.

Financial Results

Moving on to our first quarter results, Net Cash from Operating Activities was $10.8 million, which was lower than our fourth quarter results of $25.2 million. This decline was due to lower Adjusted EBITDA for the quarter and working capital adjustments.

Adjusted EBITDA for the first quarter was $19 million, which was slightly below the guidance range of $20 to $24 million. This result was driven by the lower than expected production discussed earlier, along with some additional G&A costs due to severance payments and increased advisor fees.

G&A in the first quarter was $9.3 million, which included $1.9 million of non-cash compensation expenses and $0.5 million of one-time expenses primarily related to the merger. Excluding these one-time expenses, cash G&A was $6.9 million, or $3.55 per Boe, for the first quarter which was below our expectations. We expect that base cash G&A excluding merger related costs will be approximately $5.5 million per quarter for the remainder of 2019, which will be subject to change as we integrate Midstates' assets into our platform. We anticipate that we will generate at least $20 million of annual G&A savings from the merger, with cost reductions to be phased in over the remainder of 2019 and early 2020.

Free Cash Flow, which we define as Adjusted EBITDA less cash interest expense and capital expenditures, was approximately $2 million for the first quarter, which was at the low end of guidance.

Open Market Share Buyback Program Update

Prior to the merger announcement, Amplify had continued its open market equity repurchase program and had repurchased 169,400 shares at a weighted-average price of $7.35 per share for total consideration of approximately $1.3 million. Due to the pending merger, the Company has terminated the open market repurchase program.

Spring 2019 RCF Redetermination Update and Liquidity

The Company's spring 2019 borrowing base redetermination was moved to May 2019 in order to incorporate Midstates' assets into a revised credit facility. Amplify anticipates finalizing the consolidated credit facility in June 2019 and expects it to be effective at the closing of the merger transaction. Midstates' existing credit facility will be terminated at closing, with any remaining borrowings paid down from the combined Company's credit facility.

As of May 3rd, Amplify's borrowing base on its revolving credit facility was $425 million, with $265 million outstanding. Liquidity was $179 million, consisting of $21 million of cash on hand and available borrowing capacity of $158 million, which includes the impact of $1.65 million in outstanding letters of credit.

Moving on to our latest hedge position…

Hedging

Since our last earnings call, Amplify has been further accumulating its portfolio of hedges. Our new hedge positions are a combination of swaps and costless collars, which will allow us to maintain additional upside while limiting our downside. As of May 3rd, our current hedge mark-to-market value was a net liability position of $8.9 million. It is important to note that our hedges lock in downside pricing on over 80% of our proved developed producing reserves through 2019. Amplify's first quarter 2019 hedge presentation contains additional details on our current positions and was posted on our website earlier today under the investor relations section.

Guidance

Our second quarter and revised full-year guidance issued earlier today reflects first quarter timing events and our outlook for the remainder of the year. Full year capex has been slightly increased by approximately $2 million at the midpoint. We are maintaining our Adjusted EBITDA range of $90 - $102 million for the full year, but the midpoint of our 2019 free cash flow guidance decreased by $3 million due to the increase in capex and a small increase in cash interest expense. Despite the adjustment, Amplify's 2019 free cash flow remains strong with a midpoint estimate of $18 million.

I will now turn the call back over to Ken for closing remarks.

Ken Mariani

Thank you, Martyn. We are very pleased to be moving forward with the Midstates merger, and look forward to closing the transaction in the coming months. Moreover, I'd like to thank all of our stakeholders in advance for their continued support during the integration process.

This concludes our prepared remarks. Thank you for joining us today and as always, please don’t hesitate to reach out to us with any questions.