Q2 2021 Amplify Energy CorpEarnings Call - Final

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Presentation

OPERATOR: Welcome to Amplify Energy's Second Quarter 2021 Investor Conference Call. Amplify's operating and financial results were released yesterday after market close on August 4, 2021 and are available on Amplify's website at www.amplifyenergy.com.

(Operator Instructions) Today's call is being recorded. A replay of the call will be accessible until Thursday, August 19, by dialing (855) 859-2056 and then entering conference ID 5076814 or by visiting Amplify's website, www.amplifyenergy.com.

I would now like to turn the conference call over to Jason McGlynn, Senior Vice President and Chief Financial Officer of Amplify Energy Corp.

JASON WILLIAM MCGLYNN, SENIOR VP & CFO, AMPLIFY ENERGY CORP.: Good morning, and welcome to the Amplify Energy conference call to discuss operating and financial results for the second quarter of 2021. Joining me on the call today is Martyn Willsher, Amplify's President and Chief Executive Officer. Before we get started, we would like to remind you that some of our remarks may contain forward-looking statements, which reflect management's current views of future events and are subject to various risks, uncertainties, expectations 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.

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

I'll now turn the call over to Martyn.

MARTYN A. WILLSHER, PRESIDENT, CEO & DIRECTOR, AMPLIFY ENERGY CORP.: Thank you, Jason. During the call, I will provide a general overview of our second quarter performance, including recent company highlights, give an update on operations and then review our improved full year 2021 guidance.

Jason will provide additional details regarding our financial performance, hedging program and balance sheet. Following our prepared remarks, we will have a question-and-answer session, and then I'll conclude the conference call with a few closing comments.

Second quarter production averaged approximately 25,300 BOE per day, an increase of 2% from 24,700 BOE per day in the first quarter of 2021. The quarter-over-quarter increase was largely driven by the return of off-line production in Oklahoma and East Texas caused by Winter Storm Uri in February and new well performance in the Eagle Ford.

Second quarter adjusted EBITDA of $23.8 million was approximately $1 million more than the previous quarter and exceeded internal projections due to production outperformance and continued cost efficiencies, which were further supported by stronger price realizations. As a result, unhedged cash operating margin improved nearly 20% quarter-over-quarter to 45%. Cash capital spending for the second quarter was approximately $10.9 million, an increase of [$5.8 million] from the first quarter of 2021.

The quarter-over-quarter increase was primarily attributable to Bairoil's annual maintenance turnaround, the acceleration of our rod-lift conversation program in Oklahoma and the purchase of long lead time materials for the previously announced development program at Beta.

Free cash flow, defined as adjusted EBITDA less CapEx and cash interest expense was proximately $9.5 million in the second quarter of 2021, which exceeded internal projections. The decrease of $4.1 million from the previous quarter was primarily result of the increased capital spending mentioned earlier. We continue to project substantial free cash flow generation for the foreseeable future and consequently, have increased our full year 2021 free cash flow guidance, which I will detail later on the **call**.

Now for an update on our operations. During the second quarter of 2021, we continued deploying capital towards rig and platform upgrades at Beta in addition to procuring materials for the development program. The first project, a case hole recompletion, is progressing according to schedule with initial production results expected in September.

This project will be followed by 2 sidetracks of existing wells in the fourth quarter of 2021, with preliminary production results expected by year-end. Because of the low variable cost nature of our Beta asset and the current strong commodity price environment, we believe these projects will produce significant free cash flow and add incremental reserves to our Beta asset.

Our Oklahoma workover program remains focused on high-return rod-lift conversations and ESP optimizations, which reduce operational and workover costs and help mitigate production downtime from future weather events. Due to the strong commodity price environment, we accelerated the rod-lift conversion program in the second quarter, which we expect to continue for at least the third quarter of 2021. As a result, we currently have converted nearly 45% of the field to rod lift and expect to have roughly 50% of the field converted by year-end. The strong operational results in Oklahoma this quarter stand as a testament to the efficacy of these workover projects in aligning operations in Oklahoma with our corporate strategy for production optimization and free cash flow generation.

Operational results in East Texas and North Louisiana again outperformed internal projections this quarter. We have continued to mitigate natural decline rates through cost-effective workover projects with quick payout periods. These efforts coupled with improved gas and NGL prices have yielded some of the company's best margins. The company also anticipates participating in accretive, nonoperative development opportunities beginning in the fourth quarter of 2021, which provides additional free cash flow starting in 2022.

At Bairoil, the annual facility turnaround was completed on time and under budget in June. During the quarter, we achieved strong operational reliability from injection and production facilities, and the technical team continues to refine WAG patterns and CO2 injection rates based on continuous evaluation of the reservoir.

In the second half of 2021, we expect to continue using new technologies, along with targeted workover activity to drive further operational improvements and efficiencies. Production rates from new wells in our nonoperated Eagle Ford assets continue to surpass type curves and drive incremental cash flow from the asset.

We continue to evaluate joint development projects as they arise and have elected to participate in new development projects, which are scheduled to be drilled in the second half of the year and completed in the second quarter of 2022.

On to guidance. As detailed in the **earnings** release last night, we've increased our full year 2021 guidance ranges for production, adjusted EBITDA and free cash flow. The midpoint for average daily production increased by 2% or 500 BOE per day to 24,500 BOE per day.

We have also increased the midpoint of adjusted EBITDA to $100 million, which was an increase of 11% or $10 million above our prior guidance as a result of the increase in commodity prices, strong production performance and the acceleration of our workover program in Oklahoma. Most importantly, we have materially increased the midpoint of our free cash flow guidance by 25% to $50 million, an increase of $10 million from prior guidance.

Additional guidance details are provided in our earnings release yesterday and can be found in the latest investor presentation currently available on our website.

With that, I will now turn the call over to Jason.

JASON WILLIAM MCGLYNN: Thank you, Martyn. I'll first provide details on the company's second quarter production and expenses. I'll then give an update on our hedge book and conclude with our balance sheet. As previously mentioned, production for the second quarter averaged approximately 25,300 BOE per day, an increase of 2% from 24,700 BOE per day in the first quarter of 2021 with a commodity mix of 39% oil, 16% NGLs and 45% gas. As expected, oil volumes were down this quarter due to the annual maintenance turnaround at Bairoil and should return to approximately 41% of production in the third quarter.

Lease operating expenses for the second quarter were approximately $28.7 million or $12.46 per BOE, a decrease of approximately $200,000 compared to $28.9 million or $13.01 per BOE in the first quarter.

GP&T this quarter was $5.1 million or $2.20 per BOE compared to $4.6 million or $2.06 per BOE in the first quarter. This increase was largely due to higher production volumes in the second quarter, partially offset by a decrease in the minimum volume commitment on certain properties in Oklahoma and East Texas.

Production and ad valorem taxes this quarter totaled $5.1 million or $2.20 per BOE compared to $4.6 million or $2.08 per BOE in the prior quarter. This increase is a function of higher revenue from production outperformance and sustained higher commodity pricing. Second quarter cash G&A totaled $5 million or $2.19 per BOE compared to $6.6 million or $2.95 per BOE in the first quarter.

In addition, second quarter cash G&A decreased $1.2 million year-over-year as Amplify undertook a transformative corporate expense reduction plan in 2020. Our current projected full year 2021 cash G&A estimate remains approximately $23 million. As Martyn previously mentioned, cash capital spending for the second quarter was approximately $10.9 million, an increase of $5.8 million from the first quarter of 2021. The quarter-over-quarter increase was primarily attributable to Bairoil's annual turnaround, the acceleration of rod-lift conversions in Oklahoma and the procurement of materials for our Beta development program.

Now to our hedge book. Amplify has taken advantage of the significant recovery in commodity prices to layer on additional hedges in 2022 and 2023, which had materially raised our weighted average fixed floors and ceiling prices. Across commodities, we are approximately 80% hedged for the balance of 2021, 70% hedged in 2022 and 20% hedged in 2023.

Specifically, our crude oil production is approximately 85% hedged for the remainder of the year, 80% hedged for 2022 and 30% hedged for 2023.

As we continue to monitor the market, our strategy remains focused on utilizing various hedge structures to secure an attractive baseline of free cash flow and allow for substantial upside as the forward commodity strip improves. Amplify's August 2021 investor presentation contains additional details regarding our current positions and was posted to our website yesterday under the Investor Relations section.

Moving on to the balance sheet. As of July 31, Amplify had net debt of approximately $214 million with $235 million outstanding under its revolving credit facility and $21 million of cash on hand. For the remainder of 2021, we will continue allocating the majority of our free cash flow to improving our balance sheet and reducing our total debt outstanding.

With a significant amount of free cash flow we expect to generate in the last half of 2021 and the full year 2022, we now anticipate net debt to last 12 months EBITDA to fall below 1.5x by the end of 2022.

I'll now turn the call over to Martyn.

MARTYN A. WILLSHER: Thank you, Jason. Amplify's strategy remains focused on continuously enhancing our sustainable free cash flow profile and delevering our balance sheet. With continued operational excellence and improvement in market conditions, we've materially increased guidance expectations for 2021. As detailed in our investor presentation, our internal projections currently forecast approximately $200 million in cumulative free cash flow through 2023. The substantial free cash flow should enable us to reach a leverage ratio of below 1.5x by the end of 2022 and 1.0x by the end of 2023.

Additionally, our year-end 2020 total proved reserves now have a PV-10 value of $1.1 billion with $835 million of proved developed reserves at strip pricing as of July 30, 2021.

With our significant reserve value and strong free cash flow outlook, we believe that Amplify remains substantially undervalued in the current market. Our dedication to enhancing corporate and operational efficiencies, coupled with our diverse and mature asset base differentiates Amplify as a leader in generating sustainable free cash flow. Amplify's strong free cash flow and leverage outlook will also enhance our ability to create significant long-term value for shareholders through asset reinvestment, accretive transactions and return of capital initiatives.

With that in mind, operator, we are now open for questions.

Questions and Answers

OPERATOR: (Operator Instructions) Your first question is from John White of ROTH Capital.

JOHN MARSHALL WHITE, MD & SENIOR RESEARCH ANALYST, ROTH CAPITAL PARTNERS, LLC, RESEARCH DIVISION: Congratulations on the new guidance. It's always nice to see improvements in your business.

MARTYN A. WILLSHER: Thanks, John.

JOHN MARSHALL WHITE: Using the old guidance, I don't mean to get too much in the weeds here. But using the old guidance, I've got an EBITDA number of almost $90 million. So it's going to be pretty easy to get to your $100 million number. So it sounds like things are going well on Beta and given the -- where that asset is in its life cycle, it looks to me like you could be doing workovers there well into the next several years. Do I have that correct?

MARTYN A. WILLSHER: John, yes, this is Martyn. So obviously, we've got projects planned out through the middle of next year.

But assuming the successful -- success on those projects, we have the opportunity to keep going for as long as we want. There's capacity at the -- both at the platforms for up to 20,000 barrels a day. So there's a lot of additional redundancy and capacity within the system. So like I said, we have ample opportunities to keep going.

We've only, like I said, started with this initial phased development that we call Phase 1A and 1B, which is the 3 projects this year and 2 projects in the first half of next year. But assuming, like I said, the success and we can keep going from there and permitting is obviously not an issue, so we're very excited about getting the first project completed this quarter and moving on from there to the 2 additional projects shortly thereafter.

JOHN MARSHALL WHITE: Good. Just the type of low-risk development situation, I'd like to follow up. I noticed in your new company presentation on 2 slides, you mentioned return-of-capital initiatives.

So as you delever, as you get production for continued higher, am I correct in assuming that's something that's taking a more important place in your list of priorities for the company?

JASON WILLIAM MCGLYNN: Yes, John, I'll take the first part of that, and if Martyn wants to add in on the back side. Yes, this is -- we were a return of capital story kind of before it was in vogue with everybody back in 2018 and 2019. After the transaction early into '20, obviously, everything changed last year, so it put a hold on that. But specifically when looking at the credit agreement, we have to have 25% availability on the credit agreement and less than 2.5x leverage ratio after a distribution. So that's what's precluding those from right now, but it's always a part of our capital allocation strategy to evaluate that.

We're targeting being in a position to potentially do it in the middle of 2022 type of time frame. We also are exploring various ways to potentially accelerate that time line given this is all subject to Board approval and would have to be approved at that point in time when we look to do it.

But that is something that we are evaluating and discussing for the future for sure.

MARTYN A. WILLSHER: Yes, I'll just add that, obviously, like Jason said, this has been -- this is kind of in our DNA to return capital to shareholders. That's -- kind of the whole methodology of the company is to be sustainable free cash flow that could ultimately be returned to shareholders.

And so like I said, there's -- we've been out of it just for the last year or so because of the pandemic issues, but obviously, getting back to that, especially with a lower leverage level, which we delever very rapidly as we go through the end of this year and into the beginning of next year and create substantial additional liquidity, which really opens up the window of opportunities for how and when we start to return that capital.

Like Jason said, it's all subject to Board approval, but -- like I said, I think that's something thing that's clearly on our radar. And if there's an opportunity to bring that forward a little bit, we're certainly looking at those options to do so.

JOHN MARSHALL WHITE: Good to hear. And of course, your conventional asset base with its low decline rates really lends itself to that kind of corporate activity. I'll turn it back to the operator in case someone else is waiting, but I'll probably come back with another question or 2.

OPERATOR: There are no other questions in queue. I'd like to turn it back to Martyn **Willsher** for any closing remarks.

JASON WILLIAM MCGLYNN: It looks like John has a couple of...

MARTYN A. **WILLSHER**: It looks like John has a couple of questions.

OPERATOR: Okay. John, your line is open.

JOHN MARSHALL WHITE: So I wouldn't want to let you go without asking for an update on what you're seeing in the M&A market and how you would describe activity in that area of the business?

JASON WILLIAM MCGLYNN: Absolutely. We always monitor what's going on in the market and looking at various things in the lower 48, specifically around our operations in the Mid-Con and East Texas, but keep an eye on everything.

I would say since our last conference **call** in May that the activity has picked up. I mean there's a lot of things coming to market with pricing where it is and was limited volatility until the last couple of weeks that people are really trying to see what they can get for assets and some things are starting to shake loose, so a lot of private equity-backed type of packages and smaller things along those lines.

And Obviously, there's always talk of corporate transactions. But I will say, as we look at it and evaluate it, we have a really high internal hurdle rate to issue equity. So we look at everything against that. A transaction would absolutely have to be accretive to the shareholders, to EBITDA, leverage, a lot of different metrics along those lines. But we do continually look at things and are involved in process. There's just nothing to discuss at this point in time. But it has definitely picked up from both a quality and a number of packages on the market at this point.

MARTYN A. **WILLSHER**: Yes. And Jason addressed the A, I'll just address the D side of this as well is, obviously, we always have the option as well given just how substantially we are undervalued in the market. But the opportunity to potentially divest a smaller asset such as the Eagle Ford and use that to accelerate the capital return program potentially is 1 avenue that we're obviously looking at and there's other assets that could work as well. But like I said, those are -- that's an option for us as we move forward. But like I said, that's just 1 of many options that we're looking at.

JOHN MARSHALL WHITE: Okay. Very good.

OPERATOR: There are no other questions in queue. I'd like to turn it back to Martyn **Willsher** for any closing remarks.

MARTYN A. **WILLSHER**: In closing, I'd just like to express my appreciation to all the company's employees for their outstanding efforts and dedication. I'd also like to thank all of our stakeholders for their continued support. As always, please don't hesitate to reach out if you have any additional questions. Thank you for joining us today.

OPERATOR: Ladies and gentlemen, this concludes today's conference **call**. Thank you for your participation. You may now disconnect.

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