Amplify Energy: 1Q 2023 Earnings Script

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Operator

Welcome to Amplify Energy's First Quarter 2023 Investor Conference Call. Amplify's operating and financial results were released yesterday after market close on May 3, 2023 and are available on Amplify's website at www.amplifyenergy.com. During this conference call, 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 18th by dialing (800) 654-1563 and then entering access code 44231417.

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

Jim Frew

Good morning and welcome to the Amplify Energy conference call to discuss operating and financial results for the first quarter of 2023.

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 Form 10-Q which 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.

Introduction

During the call, Martyn Willsher, Amplify's President and Chief Executive Officer, will provide an update regarding our year-to-date performance with a specific focus on the most recent Beta field developments. Next, Dan Furbee, Senior Vice President and Chief Operating Officer, will provide an overview of first quarter operational performance. Following that, I will discuss first quarter financial results, provide an update on our balance sheet and liquidity, and provide additional details on our hedge book. Finally, Martyn will provide a strategic update before opening the call up for questions. With that, I hand it over to Martyn…

Martyn Willsher

Thank you, Jim.

First Quarter Highlights

I'd first like to welcome Dan Furbee and Jim Frew, who joined the team as COO and CFO, respectively. Their extensive oil and gas experience and depth of operational and financial expertise will be a great asset to our organization and will enable us to deliver additional value to our shareholders.

Amplify has had a strong start to 2023. We successfully settled our affirmative claims in Southern California, received approximately $85 million in net proceeds from the settlement, and restarted Beta field production operations. First quarter Adjusted EBITDA was $25.8 million, up from $21.9 million in the prior quarter, resulting in $11.4 million of free cash flow.

With respect to the Beta field, on April 10th we announced that we had received all of the required regulatory approvals to restart operations. On April 24th, after completing the line fill process, we began selling crude to the market. Although results are still preliminary, initial production rates have exceeded our expectations. We continue to gradually bring more wells on-line and we are encouraged by results so far. The Company looks forward to recognizing the incremental cash flow from returning this asset to production.

With that, I'll now turn it over to Dan to discuss operational highlights from the quarter.

Dan Furbee

Thank you, Martyn.

Operational Update

Despite some challenges caused by adverse weather conditions and third-party compression disruptions, first quarter performance was in-line with expectations. Total production for the quarter averaged approximately 19,400 Boepd, which consisted of approximately 31% oil, 19% NGLs, and 50% natural gas. Across our assets, we are exploring opportunities to economically return offline wells to production and evaluating artificial lift and compression optimization projects to reduce production declines and lower operating costs. Our operations teams continue to develop and execute on their inventory of low-cost, high-return projects.

In addition, we remain focused on improving operational efficiencies. For the first quarter, lease operating costs were $33.0 million, gathering, processing and transportation costs were $5.6 million, and production taxes were $5.3 million. In total, these costs were below internal forecasts and down 8% from the prior quarter.

The Company's total capital investment for the quarter was approximately $9.0 million. In the Eagle Ford, we invested $5.1 million towards the completion of 10 gross (1.0 net) development projects in the first quarter, including two refracs, all of which were brought on-line at the end of the quarter. As a result, we anticipate higher second quarter production from this asset. The Company also invested $1.9 million in Oklahoma workover projects and $1.9 million in Southern California in anticipation of returning the Beta field to production.

As Martyn mentioned earlier, the team worked extremely hard to successfully and safely bring the Beta field back on production. After receiving the necessary regulatory approvals in early April, we began to methodically bring wells back online and increase production. Current production is tracking ahead of schedule, and we remain optimistic about returning the field to its full potential. Going forward we intend to continue investing in production enhancing opportunities, facility upgrades, and projects focused on emissions reductions.

With that, I'll turn it over to Jim…

Jim Frew

Thank you, Dan. I would like to discuss the following items: first quarter financial performance, balance sheet and liquidity, and hedging.

First Quarter Details

With respect to first quarter financial performance, the Company reported net income of approximately $352.8 million during the quarter, which was positively impacted by two non-recurring events. First, the Company received approximately $85 million in net proceeds from the Beta settlement. Second, net income had a one-time adjustment of $259.5 million related to the release of a substantial amount of the Company's valuation allowance. The valuation allowance release increases the Company's book value but has no impact on Amplify's current or future cash flows.

As Martyn previously mentioned, first quarter Adjusted EBITDA was approximately $25.8 million, an 18% increase compared to the prior quarter. The increase was primarily attributable to lower operating expenses and higher realized commodity prices (net of hedges), which were partially offset by lower production and lower LOPI proceeds. As a reminder, per the terms of the LOPI policy, LOPI coverage specific to the Incident ended on March 31, 2023.

With respect to costs, first quarter operating expenses were lower than the prior quarter. This result was primarily due to lower production taxes, reduced workover expenses at Bairoil and in Oklahoma, and a positive one-time production tax adjustment related to our Eagle Ford asset.

Cash G&A in the first quarter was $7.6 million, which was up from prior quarter but in-line with expectations. The Company anticipates that quarterly G&A expenses will decrease throughout the remainder of the year.

Free Cash Flow, defined as Adjusted EBITDA, less capex, and cash interest expense, was $11.4 million in the first quarter of 2023. This was in-line with expectations.

Finally, due to the significant one-time gain associated with the Beta settlement, the Company incurred approximately $12.5 million of current income tax expense in the first quarter. The Company is evaluating opportunities to mitigate this expense over the remainder of the year.

Balance Sheet and Liquidity Update

With regards to our balance sheet and liquidity, as of April 30th, Amplify had net debt of approximately $109 million, consisting of $125 million outstanding under its revolving credit facility and $16 million of cash on hand. With a borrowing base of $190 million, the Company's liquidity was approximately $81 million and Net Debt to Last Twelve Months Adjusted EBITDA was approximately 1.1x.

Of the $84.9 million in proceeds from the Beta litigation settlement, $65 million was used to pay down debt and the remainder was used to pay Incident-related expenses. The Company expects to recover a majority of these Incident-related amounts through the insurance claims process, which will positively impact working capital over the remainder of the year.

Currently the Company is working with new and existing capital providers to refinance its credit facility, which matures in May 2024. We expect to complete the refinance process in the latter part of the second quarter or in the early part of the third quarter of this year.

Hedging

Finally, I'd like to discuss our hedge book. As of May 3rd, our forecasted crude oil production is approximately 40% hedged for 2023 and 5% hedged in 2024. On the gas side, we are approximately 70% hedged for 2023 and 10% hedged for 2024. We continue to realize the benefits from the scheduled roll-off of our hedge book and have the potential to capture additional upside in the current commodity price environment. The Company will continue to evaluate opportunities to hedge more volumes.

With that, I'll turn the call back to Martyn…

Martyn Willsher

Thank you, Jim.

Forward Strategy

As we progress through 2023, we expect to increase our free cash flow profile, through prudent asset management and capital allocation, which will be further improved by the roll-off of our hedge book, lower leverage, and the contributions from Beta's return to production. Currently, our forecasted 2023-2025 production is expected to remain relatively flat and generate cumulative free cash flow of approximately $180 million at current strip pricing.

Our strategic focus near-term is to build production rates at Beta and refinance our existing credit facility. Achieving these key milestones will provide us the flexibility to pursue additional value enhancing initiatives. In the future, we will provide updates on these short-term priorities in addition to outlining our broader strategic plans.

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

Q&A

Operator

Absolutely. At this time, we will open the floor for questions. If you would like to ask a question, please press star key followed by the one key on your touch-tone phone. If at any time you would like to remove yourself from the questioning queue, please press star two. Again, to ask a question, please press star one. We'll pause a moment to allow questions to queue.

Once again if you would like to ask a question, please press star one on your touch-tone phone.

If you would like to ask a question, please press star one now. It appears that there are no questions at this time, so I would like to turn the call back to our presenters.

Martyn Willsher

Great, thank you. As we have become accustomed here, we are taking questions from investors and consolidating them and answering them as best we can so that we can do this in an orderly fashion. So obviously, the first question and most prevalent question is obviously to give as much detail as we can on the Beta return to production.

As disclosed, we started the platforms up by pushing some production from on the platform storage into the pipeline. We filled the pipeline through incremental production, and were done by essentially April 23rd, at which point on April 24th, we started selling into the market.

The good news so far is that as we've discussed before, being offline for 18 months, we weren't sure what to expect from the wells as we started bringing them back online. This is a long time for the facilities to be offline, and so there's a little bit of uncertainty there. So far, I'd say that the wells have performed extremely well, obviously, as of right now, there's only a few wells that haven't come back on out of probably the 70 or 75% that we brought back.

There is still a number to bring back online, and there's still the possibility that some may go down after 30/60 days, but so far what we've seen is just a few wells that look like they are traditional type ESP replacement projects that will need to be done over the next few months but so far, we haven't seen a rash of wells going down like we thought was a possibility as we brought the facility back online.

Production rates are doing well and exceeding where we expected to be at this point, and we still have a number of wells to bring back. As we continue to bring those back online and see the results of those, that'll have direct impacts on our thoughts on guidance on oil production, et cetera, for the rest of the year, but we are waiting a little bit longer just to see how that asset continues to respond as we go forward through the second quarter. And I think we'll have an update on guidance for what we put out after the second quarter earnings.

The second question that we got is related to taxes. There's two pieces to this tax update. There was a very large non-cash reversal of the valuation allowance. These are NOLs that are essentially restricted on an annual basis as to how much you can use. Due to the large settlement that pushed us into a position where we had to bring that valuation allowance back onto the books, it doesn't have any material near-term impact. We could still use the NOLs that we're planning to use going forward. It’s just a book adjustment that we had taken at one point and now we've reversed it.

In regard to the current income tax, $85 million in one large chunk is a significant gain for a company that hasn't spent a lot of capital traditionally over the last few years especially. So as of right now, we do have a $12.5 million dollar income tax payable due to this one-time gain. We're exploring ways to mitigate that somewhat during the rest of the year but since we received the funds in Q1, we had to take the full impact of the income tax payable during Q1 as well. So that is the result of that large $85 million one-time gain associated with the settlement.

The third question that I got the most is given the initial result at Beta and Eagle Ford, did you think about updating guidance? We did, is the short answer, but there are some moving pieces obviously, we only put guidance out less than two months ago. I do want to see how Beta responds. Eagle Ford came on slightly earlier than anticipated. So obviously, there is a little of incremental production there that started in the very tail end of Q1, but we're anticipating most of that production not coming on until 2Q. That obviously increased the capital in Q1, but it's going to help production rates in Q2 a little bit as well.

On top of that, though, in East Texas we had anticipated drilling some wells later in the year. Those are on the $2.00/$2.10 gas environment, and we may push those wells out. Those weren't intended to be completed this year; they were intended to be drilled this year and completed next year. So those are under review for whether or not those move forward in this current natural gas environment. And obviously, we're keeping a close eye on what projects makes sense, and what don't in both East Texas and Oklahoma, given the current natural gas pricing environment.

So, with all those moving pieces, I think we stuck to our original guidance so far but given a little bit more time, especially on the Beta side, we'll see how that impacts our go forward production guidance and we'll certainly look to update that in our August earnings presentation.

I think that was it for the majority of the questions. I did have one more on the supply chain and inflation. I think for the most part the impacts have slowed down a little bit on the inflation side, specific to the things that we do. The guys that drill a lot may have a different answer but our biggest issue that we've seen in the field is related to compression and the midstream guys in particular. Our projects that used to take half a day are taking a few days. It's materials, it’s equipment, it’s personnel. So that's where we're seeing the biggest impact and it has a little bit more of an impact, especially in our East Texas and Oklahoma area but it can impact if we have a part that we need in Bairoil and whatnot.

So that's where we're seeing the impact of call it supply chain/inflationary pressure, but overall, I think the impact is mitigating somewhat as prices have come down a little bit, and there's not as much of a demand for the services. So, we'll see how that continues as we move forward.

With that, I think that's the majority of the questions that we've been asked through our investor outreach. As always, if you have questions going forward, I encourage all of our investors to feel free to send those across to us. And like I said, we'll try to consolidate and answer the questions we get the most, or the most impactful questions.

Martyn Willsher

Post Q&A Wrap-Up

With that, I wanted to thank our employees, once again, for their outstanding efforts over the last 18 months. I think this has been a very difficult and trying period for everyone, but I also want to thank all of our investors that have stuck with us through this time. It's been kind of a long road, but we are moving forward and very excited about what the potential is for Beta moving forward. And with that, I will just say thank you once again, and if you have any additional questions please don't hesitate to reach out. Thank you everyone.