Berry Corporation (bry) (NASDAQ:BRY) Q4 2020 Earnings Conference Call
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Company Participants

Todd Crabtree - Manager, Investor Relations
Trem Smith - Chief Executive Officer
Fernando Araujo - Executive Vice President and Chief Operating Officer
Cary Baetz - Executive Vice President and Chief Financial Officer

Conference Call Participants

Leo Mariani - KeyBank
Charles Meade - Johnson Rice
Nicholas Pope - Seaport Global

Operator

Thank you for standing by and welcome to the Berry Corporation Q4 and Full Year 2020 Earnings Call. [Operator Instructions]

Thank you. Mr. Todd Crabtree of Investor Relations, you may begin.

Todd Crabtree

Thank you, Andrea and welcome to everyone. Thank you for joining us for Berry's fourth quarter and 2020 full year earnings teleconference. Yesterday afternoon, Berry issued an earnings release highlighting full year 2020 and fourth quarter results, as well as our ongoing response to the COVID-19 uncertainties.

Addressing these and other issues this morning will be Trem Smith, Board Chair and CEO; Fernando Araujo, Chief Operating Officer and Executive Vice President; and Cary Baetz, Chief Financial Officer and Executive Vice President.

Trem will discuss our 2020 performance as well as our expectations for 2021. Fernando and then Cary will share further details on how we are addressing the operational and financial aspects of our business. Before turning it over to questions, Trem will make a few concluding remarks.

Before we begin, I want to call your attention to the safe harbor language found in our earnings release. The earnings release and this discussion today contain certain projections and other forward-looking statements within the meaning of Federal Security Laws. These statements are subject to risks and uncertainties that may cause actual results to differ materially from those expressed or implied in these statements. These include risks and other factors outlined in our filings with the SEC. Our website, bry.com, has a link to the earnings release and our most recent investor presentation.

Any information, including forward-looking statements, made on this call or contained in the earnings release and that presentation reflect our analysis as of the date made. We have no plans or duty to update them, except as required by law. Please refer to the tables in our earnings release and on our website for a reconciliation between all adjusted measures mentioned during today's call and the related GAAP measures. We will also post the replay link of this call and the transcript on our website.

I will now turn the call over to Trem Smith.

Trem Smith

Thank you, Todd. Good morning, everyone, and thank you for joining us today. As you all know, 2020 was a year unlike any other. We faced numerous challenges, including the economic issues spurred by the COVID-19 pandemic and the OPEC+ created oversupply as well as fraught political environment. But despite these remarkably difficult and ever evolving headwinds, Berry delivered on its commitment it made in early 2020 to all of its stakeholders that we would enter 2021 in a strong position poised for growth.

In 2020, as planned, our production for the year was essentially flat compared to 2019, with California production up for the year. We generated $131 million in levered free cash flow for the year. And currently, we have more than $100 million in the bank and no debt. Part of this is due to the significant sustainable cost reductions we achieved in both non-energy OpEx, which was down about 9% year-on-year and energy OpEx, which was down about 13% year-on-year. We were confident we will continue to reduce our OpEx in 2021, and this is fully integrated into our budget.

As OPEC+ was making its decision to oversupply the market in March of last year, we had adeptly hedged 100% of our oil production for the remainder of 2020 at slightly less than $60 per barrel Brent. Quick data-driven decision-making is a hallmark of Berry. Even in a downturn our fundamental principle of living out of levered free cash flow did not change nor will it change in the future.

The health and safety of our employees and the environment have always been critically important. And the COVID-19 pandemic highlighted its importance even more. We never shut down operations throughout this difficult year. I'm thrilled to report in 2020, our total recordable incident rate, or TRIR was 0.5. Our lowest rate ever. This is well below the United States average for all industries, which is a TRIR of 3.0.

Tuning to 2021 now. With the oil price strip well above $50 per barrel Brent and our drive to return value to our shareholders, a key financial tenant for Berry, we are pleased to announce that the Berry Board recently approved reinstituting a quarterly dividend at $0.04 per share beginning in the first quarter.

Operationally, we remain focused on our value adding California portfolio. We are planning to keep company-wide year-over-year production flat and anticipate a strong -- a very strong fourth quarter exit rate compared to 2020. We have realized month-to-month production improvements following our fall reorganization then included the addition of our new COO, Fernando Araujo.

Our current plans include a total capital budget of $120 million to $130 million in 2021. Included in the budget is our renewed focus on workover activity on existing wells. This activity is something that is extremely judicious in California and is a highly efficient use of our capital dollars. In addition, as mentioned, we are continuing to reduce costs across the organization. I am confident we will be successful. Fernando will expand on all of this more in a moment.

Finally, and importantly, we are laser focused on increasing our scale. Our growth strategy continues to be directed toward conventional low corporate decline assets with strong cash flow.

I'll now turn it over to Fernando.

Fernando Araujo

Thank you, Trem. As I completed my first full quarter with Berry, I want to emphasize the safety protection of the environment on operational excellence remain our top priorities. We will continue to create value by optimizing the performance of our current assets and generating meaningful growth in conventional and predictable place.

I am proud to report that we achieved excellent environment, health and safety results in 2020, exceeding all of our targets. In 2020, we did not have a single lost time incident. Trem noted, we had our total recordable incident rate of 0.5, which translates to only two recordable incidents all year. In 2021, we will continue to dedicate the necessary resources to protect the safety of our employees and contractors, to safeguard and respect the environment, to meet all regulatory commitments and to guarantee the integrity of our infrastructure.

Moving to performance. I'll start with production. Our California oil production, which constitutes about 80% of our total production, was up by 1.3% in 2020 versus 2019. We paused drilling activity from April through October of last year, which resulted in a 3.6% decline in production from Q3 to Q4. Drilling assumed during the fourth quarter, as we drilled 22 wells, all in thermal sandstone reservoirs in California. We anticipate big production for this 22-well package later this quarter.

Our average production in Q4 was 26,600 barrels a day and we exited the year producing nearly 27,000 barrels a day. Our plan in 2021 is to keep production flat year-on-year, with a positive year-end exit rate compared to last year with continued growth in California.

Next, let's turn to operating expenses. In 2020, we averaged an operating expense of $18.51 per BOE. This is a $1.81 per BOE improvement when compared to 2019. We used non-energy OpEx by 9% with improvements in all major categories. And we reduced energy OpEx by 13% driven by a 16% reduction in steam rates. Importantly, we achieved this without affecting production.

Non-energy operating expenses are expected to be sustainable for a total OpEx of around $18 per BOE for 2021. We are dedicating resources. We improve our cost structure even more through a combination of optimizing contracts, generating ideas from the field and executing facility projects that can reduce LOE in the long-term. We are determined to become the lowest cost operator in the basins where we operate.

Now, let's turn to capital. CapEx in Q4 and for the full year was in line with our plan at $12 million and $69 million, respectively. We maintain our plan for reduced capital investments in 2020. However, as mentioned before, we restarted our drilling campaign in October.

I want to highlight the 15 wells drilled in Q4 in the Tillery sandstone reservoir in our Hill property in California. This is a clear example of a shallow mature steam flood with predictable geology on low decline. Peak production for these 15 wells is higher than pre-drill estimates with drilling and completion costs 26% below the 2019 development campaign. As a result, the field is currently producing at a 30-year high.

Our capital program in 2021 will be in the $120 million to $130 million range. We'll drill approximately 185 development wells and performed roughly 200 workovers and recompletions. We're putting a strong emphasis on workovers this year compared to previous years. Workover activity is some of the best capital investment in terms of the capital efficiency.

We continue to be fully committed to our obligations under the California mandated Idle Well Management plan. In 2020, we exceeded our idle well abandonment commandments spending $17 million to abandon 194 wells, well above the required 164 wells. The additional 30 wells were abandoned to accelerate production.

Similarly, in 2021, we intend to plug an abandoned approximately 280 wells, of which 223 wells are required and 57 are to accelerate production at a total cost of $20 million.

The Lawrence Livermore technical study on high pressure cyclic steam operations in the thermal diatomite reservoir is complete and under review by CalGEM. We've been told by CalGEM this study will be released by the end of Q1. We anticipate the opportunity to further work with CalGEM to obtain new permit approvals for future thermal diatomite operations.

Remember, our 2021 plans do not include new thermal diatomite development. Our anticipated development program for 2021 is targeting sandstone reservoirs and only in California where we enter the year with almost 200 new permits in hand.

And with that, I'll turn it over to Cary.

Cary Baetz

Thank you, Fernando. As the pandemic impacted the global economy in 2020, we delivered on the promise that we made last spring to successfully bridge to the end of 2021. At the time, we planned for a two-year down-cycle in our industry. We immediately began to cut costs, reduce planned capital and leverage our strong hedge position in effort to preserve cash for 2021. Our efforts were and continue to be successful.

At the end -- at year-end, we had more than $80 million of cash in the bank, and we continue our cash build in 2021. As Trem mentioned, we currently have more than $100 million in the bank. By managing our costs and capital, we generated more than $130 million of levered free cash flow for 2020.

Our business model is unique for the industry and our 2020 results highlight the benefits of the Berry model. In these extraordinary times, we maintained our total production level, which was nearly flat year-over-year, and we even grew our California production, while we generated cash.

I'm extremely proud of our team and the results we generated. We are in an excellent position to manage our development plans for the year and to return capital back to our shareholders.

On another liquidity note, in November, we completed our scheduled semi-annual RBL borrowing base redetermination, which resulted in reaffirmed borrowing base and the company's electric commitment of $200 million. As of December 31st, 2020, we had liquidity of $273 million consisting of cash on hand and the RBL borrowing availability. As a reminder, we primarily use the RBL facility to manage working capital fluctuations, have no outstanding on the borrowing on the line today.

Due to lower SEC pricing, our 2020 reserves were down. However, I want to reaffirm that for 2021, we anticipate to see a substantial improvement in our calculate reserves as the current strip prices are more than 40% higher than the SEC prices used for 2020 reserve calculations, assuming current prices hold.

Our 2021 capital of $120 million to $130 million should keep our production relatively flat on annual basis going back to 2019, with an accelerated exit rate in 2021. Like 2020, this year we planned to see oil growth in our attractive basins in California. At the current strip pricing, we expect to fund our development plans with cash flow from operations.

We currently have oil sells hedges of approximately 19,000 barrels a day at nearly $46 per barrel in the first half of 2021 and approximately 14,000 barrels in the second half of 2021. We recently added 3,000 barrels in the second half of 2021 at $58 a barrel as we have seen recent oil price strengthened this year, improving our average hedge positioned to $49 in Q3 and Q4.

We will continue to hedge our natural gas usage. As shown in our latest investor presentation, we are well hedged through October of this year. And throughout the year, we will opportunistically look to build our 2022 position to fully hedge -- hedge position for natural gas.

Returning capital to our shareholders continued to be one of the key financial tenants and is being demanded by investors within the energy space. We promised to revisit the quarterly dividend when oil prices strengthened, with the price environment and the business fundamentals for oil improving, as well as our long-term liquidity position we feel comfortable in reestablishing an attractive quarterly dividend. Last week, the Board approved a $0.04 per share dividend for the first quarter of 2021. Our 10-K will be filed later today, if you want a deeper dive into the financials.

And now turn it back over to you, Trem, for final remarks.

Trem Smith

Thanks, Cary and Fernando. I want to close with speaking about our ESG efforts and about the legislative and political environment in which we operate.

First, we continue to be very committed to our work in ESG. We accomplished a lot in 2020 in regards to developing initiatives and we are putting together our first ever environmental social and governance report this spring. It will serve as a baseline report that will show our progress and results, as well as highlight areas for opportunity. The report will be part of Berry's annual report. As I've said before, we are committed to providing locally produced affordable energy in an environmentally friendly manner.

On a national level, as we all know, a new federal administration took office on January 20th, 2021. The impact of the new administration on us so far is low. While there is a temporary moratorium on federal drilling permit issuance, it does not impact current Berry activity.

On a state level, we had an uneventful 2020 legislative session. There were no bills passed that severely impacted Berry, exemplifying that our approach to working with the state and aligning our goals with those of the state has been fruitful and has created great value for all our stakeholders. As we enter into the 2021 legislative session, we will continue to work with legislators and regulators to ensure the state prioritizes policies, that support energy sources that are reliable, affordable, and equitable for all Californians,

To conclude, we fully expect 2021 to be a year of value creation through the dividend, improved capital efficiency, continued cost reductions, and ideally accretive growth.

I will now turn it over for questions.

Question-and-Answer Session

Operator

[Operator Instructions]

Your first question comes from the line of Leo Mariani of KeyBank.

Leo Mariani

Hey, guys. Morning. Wanted to follow-up on comments you made about M&A being a priority for Berry here. Just wanted to -- trying to get a sense, if you guys have been able to start to identify any potential targets, just trying to get a sense of where you might be in the process? Are you guys confining yourself to California versus just a much broader search?

Cary Baetz

Leo, this is Cary and I'll let Trem fill in on the holes. The answer is, we've had -- we've always had identified assets out there and opportunities we want to look at targets. The bid/ask has always been a little wide that we continue to work on managing that. Scale is very important. As you know the market is looking for larger. They're looking for more liquidity. They're looking for companies with larger floats, secure balance sheet. So I'd say it's very high on our priority list. But again, it's got to work for Berry. Identify targets, yes. Opportunity, yes. TBB on execution.

Leo Mariani

Okay.

Trem Smith

And then, Leo, we continue to maintain our strategy, which is conventional -- basically focused on what we're good at, conventional, low corporate decline, oily assets with strong cash flow. It's not a matter of geography, as much as it is a matter of that. Okay?

Leo Mariani

Got it. Okay. And then, I just wanted to ask about the current legislative session in California. I guess, I recently saw that there's a new Senate bill that's been proposed that contemplating a potential frac ban in the state. I think there was also some language around there that was contemplating, eventually banning cyclic theme operations as well.

Just wanting to get a sense of, what you guys may have heard locally and in California from legislators or the governor's office. And you think this bill having real legs?

Trem Smith

Leo, this is Trem. I'm going to answer this because this is not a surprise question. The bill was long anticipated. Senator Wiener telegraphed very early that he was going to be proposing such a bill. It is much broader than maybe he had originally intended. The -- let me just say that the time it will take for that bill to get through the whole legislative process is extensive. And we fully expect that bill to be amended significantly as we move forward. And we are working ourselves obviously, but also with all the industry groups and labor groups to make sure it has minimal impact on Berry and the industry in California.

Leo Mariani

Gotcha. Okay. That's helpful. And I guess, you're talking about the ones that are more steady, sounds like coming due next month in terms of when you guys will receive it here. Do you have any early indications from other them directly or in the governor's office, or you just still wait and see mode here?

Trem Smith

Leo, what we -- we've been told by CalGEM that will be released at the end of the first quarter. I think Fernando said that. And we'll see -- hopefully they'll deliver on that. But we've also been told by CalGEM that they -- they're developing a process to evaluate those operators and those assets that are least troublesome to them. We don't know where we stand on that list, but we fully expect to be high on the list in terms of being contacted by CalGEM.

Does that make sense?

Leo Mariani

Yes, for sure. Thanks for the color.

Cary Baetz

Thanks, Leo.

Operator

[Operator Instructions]

Your next question comes from the line of Charles Meade with Johnson Rice.

Cary Baetz

Good morning, Charles.

Charles Meade

Good morning to you and your whole team there. I have to say I really liked Leo's questions because I had written down on my piece of paper to ask also. But let me just ask a couple of questions following up on the Livermore. On the Livermore question is, I guess it's kind of a two-part question. One, if assuming you can -- assume Berry can go back to doing some of your thermal diatomite development, would that be attractive to not enough that it would compete with some of the sandstone projects that you currently have slated for 2021? And if it is attractive enough, would it possibly slot into 2021, or is that more something we should look forward 2022?

Fernando Araujo

No. That's a very good question. And our thermal diatomite development is very attractive in terms of a rate of return. And it competes very, very well with the rest of our portfolio. So, if we do have the ability to do some work in the thermal diatomite in 2021 in the second half of the year, we would. But as you heard in the call -- by the comments that I've made, currently our plans do not include any thermal diatomite development in 2021, but we expect to have a development in 2022.

Charles Meade

Okay. Thank you for that, Fernando. And then, perhaps as my follow-up, maybe a derivation off that. I think the conventional wisdom is that -- and it certainly seems to fit what we've seen in A&D over the last 12 months is that as oil prices rise, like they have done for the last month and a half, and we're happy to see it, but it makes the bid and ask get a little wider in the A&D market.

And so, I wondered if you guys are seeing that and that -- that some of these possibilities of receding on the A&D side. And if maybe there aren't other dynamics at play, particularly in the California market, like if you have this -- I think Trem, you mentioned that CalGEM might have one way of dealing with less troublesome operators and another way of dealing with more troublesome auditors that maybe if it plays out like that, that might shake some assets loose out of some operator's hands, and if that might be an opportunity?

Cary Baetz

Yeah. I will say on oil prices, Charles, a rising tide lifts all boats. But again, I think -- again, people understand the importance of scale. People understand the importance of cash flow, living with the cash flow, even the resource guys are having to go that route. So I think there is still some willingness regardless of where prices are to -- for combinations to get larger. So, I don't think that's impacting the market from an A&D perspective, as far as we see at this point in time. And again, investors are looking for companies that are bigger, lower cost and scaled gets you there. So.

Trem Smith

And Charles, I'll add to that. This is Trem. The -- remember, there's over 400 operator entities that report production in California, as an example. And consolidation is for that industry to really survive long-term consolidation is a requirement. Many of those companies have gotten themselves into financial difficulty last year and are available regardless of the price. So, I'm not sure the rising price is going to impact it. I think it's brought a lot of people to the table.

Charles Meade

Got it. Thank you, Trem. Thank you, Cary for your comments.

Cary Baetz

Thanks, Charles.

Trem Smith

Thanks, Charles.

Fernando Araujo

Thanks.

Operator

Your next question comes from the line of Michael Shelton with FRC.

Cary Baetz

Hi, Michael.

Trem Smith

Hi, Michael.

Michael Shelton

Good morning, guys. Hey. So, I'm a family office and have a stake in Berry. And I just want to try and reconcile a few things. It looks as though the RSUs that you guys deployed yesterday for your exec team, amount to about $3.5 billion in value to the executive team. And the dividend distribution looks to be about $3.2 million for the period.

And I just want to know, many oil companies in this space have sort of offered to take discounts in their compensation. And I'm wondering how do you reconcile that for your shareholders and trying to figure out your capital allocation going forward for the stock buyback that's still outstanding from the previous board approval process.

So I appreciate if you could just talk to all that in terms of understanding what you're going to do on those initiatives?

Cary Baetz

Yeah. Good question. The LTIP, again, it is that -- the shares that were issued were associated with the annual LTIP plan. Year-over-year, we're going to see about a 30% reduction in LTIP. So that is a good question. And actually below requirements under contractual obligations under employment contracts. So compensation from LTIP is coming down.

As far as the dividend, I think we had a very attractive dividend prior to the downturn. It's still attractive today. I think we want to build back into a sustainable dividend. Don't forget the market has just recently turned around and it's gotten very bullish. But again, when we were looking at this in 2020, we were looking at a black hole. We put the company a good position to manage through 2020. It's in good position to manage through 2021. But again, with our heads -- our current hedges and all that, we'd like to see a little more running room before we get a lot more value back into the dividends. But we'll also look at returning shareholder value in other ways, as we bought back shares in the past and also looked at debt in the past as well.

And limitation on debt, we did not -- we were restricted for awhile based upon RBL covenants that we have that removed to be able to go forward. But I think again, overall, we've demonstrated that we do return capital. I think over prior to cutting the dividend, we had returned over $120 million of capital back to investors. So, for a company our size, I think that's been fairly attractive and something that -- again, it's a financial tenant for us and it's something that we will continue to move forward with.

Does that answer?

Michael Shelton

Hey, Cary -- I think that was Cary, right?

Cary Baetz

Yeah, it was.

Michael Shelton

Yeah. Thanks for that detailed response. So that just leads to one other follow-up. In terms of your debt structure, I don't know -- I took this out of context, but Trem had mentioned that there was no debt earlier in the call, which -- I think you guys got approximately $400 million of debt outstanding that's refinanceable at this point in time. And it's sitting at about a 7% interest rate.

Is there an opportunity to restructure that debt? And if so, is it available at a better rate? And can you structure it and time it out as opposed to having one lump sum due in 2026?

Cary Baetz

Again, I think the focus for us is to keep the balance sheet fairly simple. The unsecured debt at 7%, still a very attractive rate today. Obviously, a high yield market's been attractive. But for E&P names, it's still not wildly attractive. There were some hesitant is still probably the highest yielding industry sector out there from a high yield point of view. I think as we look at going forward, and if there was a major transaction out there, that gives you the opportunity to do something different with the balance sheet and keep it clean.

But again, from our point of view, keep it as simple, our story, simple. I want to keep the balance sheet simple and the unsecured structure -- the unsecured nature of the high yields always very attractive for us.

Michael Shelton

All right. Thank you guys.

Cary Baetz

Thanks. Appreciate it.

Operator

Your next question comes from the line of Nicholas Pope with Seaport Global.

Nicholas Pope

Good morning, guys.

Cary Baetz

Good morning, Nick.

Nicholas Pope

Morning. I had a little quick question on the reserves numbers and I know there's going to be more detail on the K. But it looked to me like the PDP reserves had dropped a bit more than production. And I was trying to understand -- I'm looking at kind of last year's K, it seems like maybe some PDP and P had been taken out, or maybe that's not included in this year's number. So, I was trying to get a little bit of a -- little help on the reconciliation from the -- just PDP drop from year-over-year.

Cary Baetz

I think most of it is really on -- there were some PUD drop, but that's the only location. Obviously, if any PDP fell off it within -- it would be in the Rockies area where pricing was challenging based upon -- the returns were challenging based upon the current pricing at that -- on the SEC pricing. We did lose some PUDs in California, that we expect that to come back. And part of the PUD loss was associated with the thermal diatomite and the moratorium put out there and the five-year requirements under the SEC pricing and guidelines.

So, I think it's just a little bit of time as Lawrence Liver -- If the Lawrence Livermore study turns out to be positive, obviously those PUDs come back and as pricing comes back we see a substantial amount of reserves come back.

So, does that help Nick?

Nicholas Pope

Yeah.

Trem Smith

Hey, Nick. Let me -- Nick, This is Trem. Let me just add some color to that, please. The -- 91% of our drop in reserves was due to price, the SEC pricing rule. Just to be clear, that's the 12-month trailing average, which drives some of us a little bit nuts. Okay?

And then -- but the other rule that's out there remember is the commitment to spend capital over a five-year period. And that's what impacted our Rockies in particular. Okay? So, we're -- as we were focused in California. So we expect with the price to have well over 90% of that comeback. But it won't be complete given the five-year commitment rule.

Cary Baetz

And the five years also is what guides the thermal diatomite, just because of the moratorium.

Trem Smith

Yeah. Does that help?

Nicholas Pope

Yeah. That's helpful. I'll probably follow up with whenever the K comes out tomorrow.

Trem Smith

Yeah. And if you have more questions, call us.

Nicholas Pope

And one other item, just a clean-up item. The last two quarters you've had a non-recurring component of G&A, which I think was part of just management changes. And how much is left of that non-recurring? How long should we expect that number? Because I think we've seen a couple -- several million each of the past two quarters that you all are kind of categorizing as non-recurring in the G&A.

Cary Baetz

Yeah. I think it -- there'll be just a minimal amount this quarter, as all of those contractual obligations are finished up. But that should be in it.

Nicholas Pope

Okay. That's all I had.

Cary Baetz

Thanks. Appreciate it.

Nicholas Pope

Thanks for the time.

Operator

[Operator Instructions]

Your next question comes from the line of Jeff Robinson of Water Tower Research.

Trem Smith

Hi, Jeff. Jeff?

Operator

Jeff, your line is open.

Cary Baetz

Must've dropped.

Operator

At this time, there are no audio questions. I would like to turn it back over to management for closing remarks.

Trem Smith

Thank you very much. Thank you everyone for listening today and look forward to any further questions. The 10-K will be out shortly and we really appreciate the interest in the company. Thanks. Bye.

Operator

Thank you for your participation. This concludes today's call. You may now disconnect.