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BRY.OQ - Q2 2022 Berry Corporation (Bry) Earnings Call

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Cary Baetz

Trem Smith *Berry Corporation - Chairman & CEO*

CONFERENCE CALL PARTICIPANTS

Michael Farrow *Johnson Rice & Company*

Steve Busch

PRESENTATION

Operator

Good day, and thank you for standing by, and welcome to Berry Corporation's Q2 2022 Earnings Conference Call. At this time, all participants are on a listen-only mode. After the speakers' presentation, there will be a question-and-answer session. (Operator Instructions). Please be advised that today's conference is being recorded. I would now like to hand the conference over to your speaker today, Dani Hunter, General Counsel. You may begin.

Danielle Hunter - *Berry Corporation - Executive VP, General Counsel & Corporate Secretary*

Thank you. Welcome, everyone. Thanks for joining us for Berry's Second Quarter 2022 Earnings Teleconference. Earlier today, Berry issued an earnings release highlighting the second quarter results. Speaking this morning will be Trem Smith, Board Chair and CEO; Fernando Araujo, Chief Operating Officer and Executive Vice President; and Terry Bates, Chief Financial Officer and Executive Vice President.

Before we begin, I want to call your attention to the safe harbor language found in our earnings release. The release in today's discussion contains certain projections and other forward-looking statements within the meaning of federal securities 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 are contained in the earnings release in 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 reconciliation making all adjusted measures mentioned in today's call and the related GAAP measures. We'll follow our 10-Q later today and 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 - *Berry Corporation - Chairman & CEO*

Welcome, everyone, and thank you for joining us this morning. We delivered solid results in the second quarter of 2022, and the year is trending in line with our expectations. Berry continues to be a cash flow machine. We have a strong track record of returning capital to our shareholders as we remain on pace to deliver top-tier returns going forward. Berry is uniquely positioned to continue returning capital well beyond the current cycle. Last quarter, we delivered our first variable dividend through our new shareholder return model. We are excited to report that we are delivering an even larger dividend this quarter. For the quarter, our combined dividend variable and fixed is \$0.62 per share, more than 3x larger than last quarter's return. This position is one of the highest returners of capital in the industry. We still anticipate the cash dividends for the fiscal year 2022 will be in the range of \$1.60 to \$1.90 per share based on the current plan and commodity strip prices.

As a reminder, our shareholder return model is based on discretionary cash flow we generate, which is calculated after the payment of the regular fixed dividend and then allocates 60% of that discretionary cash flow primarily in the form of cash variable dividends. The remaining 40% is for

discretionary capital to be used opportunistically, including in the form of share repurchases. We generated \$74 million of discretionary cash flow in the second quarter, which means we are delivering \$44 million or \$0.56 per share to our shareholders for the variable dividend on top of the fixed dividend of \$0.06 per share.

In the second quarter, we also repurchased 2 million shares for \$23 million, utilizing a portion of our board-approved share repurchase authorization of \$150 million in aggregate. Over the last few years, we have repurchased more than 7.5 million shares or almost 10% of Berry's outstanding shares. Since going public in July 2018 and inclusive of the \$0.62 per share dividend that will be paid in August, we will have returned more than \$225 million to shareholders in the form of dividends and share repurchases, which is more than 2x the \$110 million of net IPO proceeds. This includes the \$92 million announced so far this year.

Looking forward to the remainder of the year, we see our production holding relatively steady and our discretionary cash flow remaining strong. In addition, we expect full-year capital to be at the lower end of its guidance range due to a shift in our development plan to focus on reusing existing wellbores, further optimizing our use of capital. Fernando will expand on this further.

Fernando Araujo - *Berry Corporation - Executive VP & COO*

Thank you, Trem. For details of our operational performance in Q2, please refer to the earnings release and 10-Q. Here are a few key achievements I'd like to highlight from Q2. Production remained essentially flat from Q1 to Q2, net of our Colorado divestment in January. We improved our capital efficiency by allocating more resources to work in over existing wellbores in Q2, which is our most efficient use of capital. So far this year, we have completed 169 workover jobs with our rate return greater than 100% for the program. Also in Q2, we began implementing a robust surveillance program, which includes enhanced data gathering and reservoir management. The program helps us maximize oil recovery from our fields, has generated additional workover scope, and is helping us optimize new wealth placements. This is another effective way to enhance base production performance. We expect that on average, the base production will account for more than 90% of our total production this year.

Non-energy operating expenses increased quarter-on-quarter mainly driven by higher inflationary pressures. Also, we identified and executed expense workover activity in Q2 above and beyond what we have done in previous quarters. We plan to continue the current pace of workover activity for the remainder of 2022 as it generates additional oil production today.

Energy OpEx decreased quarter-on-quarter by \$2.19 per BOE. This was mainly driven by additional gas hedges realized in Q2. We currently have 2/3 of our demand hedged at \$4 per MMBtu, and we plan to have most of our demand hedged in Q4. Also, additional physical natural gas line capacity in the Kern River line covers up to 80% of our total gas demand. This pipeline brings a reliable supply of gas from the Rockies to California at prices that historically have been less expensive. All of these measures help us mitigate the volatility in the gas markets.

To summarize, we have delivered production according to plan year-to-date, and our production guidance remains unchanged. During the quarter, we accelerated the pace of our workover activity, which delivered outstanding results, and our operating margins significantly increased quarter-on-quarter, both in Utah and California.

I will now pass it to Cary.

Cary Baetz

Thank you, Fernando. We achieved strong discretionary free cash flow this quarter and further demonstrated our commitment to delivering top-tier yields and total returns. Our second quarter variable dividend met our expectations, and we are well positioned to have strong payout for the rest of 2022 as well as over the next few years based upon the current strip. One house-keeping item; we have aligned the record date and payable date of the fixed and variable dividends going forward as highlighted in our earnings release. Regarding hedging, we have roughly 60% of our planned production swapped at about \$77 a barrel Brent for the rest of this year. This provides certainty around our free cash flow and leaves upside pricing for a significant portion of our production as we anticipate continued strong oil prices throughout the rest of the year and over the near term. Please look at Slide 19 of the investor presentations for more detail on our hedging program.

Our guidance ranges remain in place. However, operating expenses are tracking on the higher side of guidance due to the increase in workover expense. We will also incur some additional costs associated with our improved surveillance program for existing wells to optimize our base production. We expect slightly lower capital expenditures due primarily to the increase in reusing existing wellbores and due to the anticipated lower overall new well count for the year. In closing, we continue to provide investors with strong predictability and visibility into our cash flows. With that, we have the confidence to plan for and deliver significant cash returns and to deliver additional value to shareholders. Back to you, Trem.

Trem Smith - *Berry Corporation - Chairman & CEO*

Thank you. Very strong team continues to deliver on its promises, generating strong cash flow, distributing best-in-class returns, and successfully executing our plan. Before we take your questions, I'd like to briefly highlight three more items of note. First, we are extremely proud to report that our C&J Well Services team won the Energy Workforce and Technology Council's Gold Award in Group V for the 2021 safety record, which will be presented tomorrow at the Council's summer meeting. C&J has won this award 20 times over the last 23 years.

Second, we continue to focus on reducing our carbon footprint. Notably, we have signed letters of intent with operators of major carbon capture and sequestration projects to capture up to 80% of our current direct operational CO2 emissions in California. These are long-term projects in the early stages of definition and planning.

Finally, we have some exciting news regarding our thermal diatomite production. We have encouraging results from early testing of two new horizontal wells. The wells target our thermal diatomite reservoir in North Midway-Sunset field, using a new development concept that takes advantage of existing reservoir energy. In short, the wells leveraged the heat from existing thermal steam operations and, therefore, do not need new steam injection. This application opens up a lot of exciting potential and with continued success represents an important opportunity for Berry. Now I'll open it up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Michael Farrow from Johnson Rice & Company.

Michael Farrow - *Johnson Rice & Company*

I appreciate the color on the thermal diatomite. That was going to be my first question regarding if you still needed to inject steam, but that's -- it seems like that's a good advantage to use the current energy that's already down there. So in regards to this new development program, is it too early to determine how that's going to have an impact on production or the number of locations that this could be applicable to?

Trem Smith - *Berry Corporation - Chairman & CEO*

This is Trem, and I'll let Fernando follow, if necessary. It is too early to overall production. However, with continued success, this opens up hundreds of opportunities for us in terms of well locations throughout our dynamite acreage.

Fernando Araujo - *Berry Corporation - Executive VP & COO*

Yes. And we have very encouraging results from the first two wells that we've drilled. We're moving fluids. We're producing oil. We're getting heat to the wells. We have a fracture system that's connecting the heat to the wells, and we're gathering lots of data. So it's very, very exciting opportunity that we have. And the next phase of that opportunity is to continue with the development program, and we're in the middle of preparing that next phase right now. So it's very exciting.

Michael Farrow - *Johnson Rice & Company*

My next question is how does it look like -- or what does the path look like going forward to actually developing more than just a couple of test wells for these thermal diatomite wells in regards to the current regulatory environments or other challenges that you might face?

Trem Smith - *Berry Corporation - Chairman & CEO*

Very simply here, Michael, good question. This is something we will be doing in light of the fact that it's successful. It does not take away from our desire to see the high-pressure cyclic steam moratorium lifted, which will give us opportunities to build safely and efficiently more steam injection capabilities, which would just increase this opportunity even more. We looked at these activities in parallel and not one excluding the other. And that's where we're headed in terms of the planning. And the additional item to note is this entire area is already covered by CEQA process. In other words, new drill locations are available to us in this area, while the Kern County EIR is finalizing its reentry into the regulatory world. Does that make sense, Michael?

Michael Farrow - *Johnson Rice & Company*

That does make sense, actually. I appreciate the information.

Trem Smith - *Berry Corporation - Chairman & CEO*

That's a very good thing for us.

Michael Farrow - *Johnson Rice & Company*

It sounds like, and I'm looking forward to hearing more about the development of these thermal diatomite prospects going forward.

Trem Smith - *Berry Corporation - Chairman & CEO*

So are we.

Operator

(Operator Instructions) And one moment for questions. Our next question comes from Steve Busch from Everglades.

Steve Busch

Steve Busch: Could you just give us an update on the permit situation in California?

Trem Smith - *Berry Corporation - Chairman & CEO*

Sure. The permit update, we are -- the current county EIR is in final stages of being put in an adequate position that hopefully, the court system will approve its reentry and allow us to move forward with the new drilling well opportunities throughout the San Joaquin Basin in Kern County, in particular. And so that's going on. In the meantime, we currently get any -- all the workovers, sidetracks, and plugging and abandoning permits we need because these are reentries into existing wellbores, and we have, over 2,000 wells with workover opportunities that we know of today. So that's a very positive outcome because that's a great use of capital. And then there's a large area in North Midway-Sunset as I just responded

that has CEQA coverage already approved, and we're able to get new drill locations there, which includes our Potter Sandstone trends as well as our thermal diatomite.

Steve Busch

So would you say if the permit process loosens up, you have potential upside this year? Or you're pretty much...

Trem Smith - *Berry Corporation - Chairman & CEO*

We have upside in terms of drilling activity. Remember, sometimes it takes a little while for the actual production to ramp up from new wells. But yes, that would be upside that would extend into early 2023 and beyond. Yes, sir.

Steve Busch

And on this thermal diatomite process, is this something you guys developed or you developed with someone else? Is it a technology patentable or anything like that?

Trem Smith - *Berry Corporation - Chairman & CEO*

We have done a -- this is something that was developed internally. Looking at the reservoir, it's a result of an increased surveillance program in terms of the reservoir characterization. And one of the outcomes was there should have been, and it turns out there is, some stored energy and migratory path inside the reservoir, which allows these wells to flow. So no, it was just good reservoir and geologic work that led to this technique.

Operator

And one moment for our next question. And our next question is a follow-up from Michael Farrow from Johnson Rice & Company.

Michael Farrow - *Johnson Rice & Company*

I thought I'd have a quick follow-up just regarding the full-year cash dividend expectation range of \$1.60 to \$1.90 per share. Can you clarify what the oil price assumption is being used in that range?

Cary Baetz

Yes. We still look at it based upon our hedge position and the current strip.

Operator

And I'm showing no further questions. I would now like to turn the call back over to Trem Smith for closing remarks.

Trem Smith - *Berry Corporation - Chairman & CEO*

I want to thank everybody for taking the time. It was a good quarter for Berry, and I hope everybody appreciates the significant impact of the variable dividend. Thanks, and have a great day.

Operator

This concludes today's conference call. Thank you for participating. You may now disconnect.

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