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BRY.OQ - Q2 2023 Berry Corporation (Bry) Earnings Call

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Charles Arthur Meade *Johnson Rice & Company, L.L.C., Research Division - Analyst*

Timothy Darin Chatard *Meros Investment Management, LP - Portfolio Manager*

PRESENTATION

Operator

Good day, and thank you for joining us. Welcome to the Berry Corporation Q2 2023 Earnings Call. (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, Todd Crabtree, Head of Investor Relations. Please go ahead.

Todd Crabtree - *Berry Corporation - Director of IR*

Thank you, Jerald, and welcome, everyone, and thank you for joining us for Berry's Second Quarter 2023 Earnings Teleconference. Earlier today, Berry issued an earnings release highlighting 2023 second quarter results. Speaking this morning will be Fernando Araujo, our Chief Executive Officer; and Mike Helm, our Chief Financial Officer.

Before we begin, I would like to call your attention to the safe harbor language found in our earnings release that was issued this morning. This release and today's discussion contain 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, including our 10-Q, which will be filed later today. 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, reflects 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 in 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 Fernando.

Fernando Araujo - *Berry Corporation - CEO*

Thanks, Todd. Welcome, everyone, and thank you for joining us. In the second quarter, we successfully executed on our strategy to maximize shareholder value and generate meaningful returns. Our operational and financial performance was strong, and we delivered on all fronts. We are excited for our pending acquisition of Macpherson Energy Corporation, which is on track to close late in the third quarter. This is another step in achieving our important objective of acquiring accretive, producing bolt-ons.

We currently anticipate that our full year 2023 results from our current operations will be in line with previous guidance, except with respect to capital expenditures. We expect 2023 capital expenditures to be approximately \$35 million lower than initial guidance. This is a result of the

reallocation of capital used to fund a portion of the Macpherson transaction. We will fully update guidance in connection with the transaction close.

We delivered nearly 7% or more than 1,600 barrels per day higher production volumes quarter-over-quarter, and we accomplished this with less capital than planned. We expect annual production from our current operations to be at or above the midpoint of our initial guidance. Our base production, which is expected to account for more than 95% of our total 2023 production, is outperforming plan. This is mainly due to the implementation of an optimized steam injection strategy in our California fields. It is a great example of what I mean when I use the term "operational excellence".

The balance of production comes from our successful workover and sidetrack campaign. Part of the production gain in Q2 was related to recovery and deferred production from Q1. Our ongoing commitment is to maximize shareholder returns while ensuring that we remain a responsible and safe producer. In accordance with our shareholder return model, this quarter, we will pay total dividends of \$0.14 per share between fixed and variable. This is in line with our goal to deliver a 2023 cash return in the high single digits based on our current stock price. Additionally, we opportunistically repurchased \$10 million of our common stock during the second quarter.

We recently announced that we've entered into an agreement to acquire Macpherson Energy Corporation, a privately held Kern County operator, for \$70 million in cash. This transaction improves capital efficiency and reallocates capital, with 80% of the purchase price funded with \$35 million from our planned 2023 capital expenditures, plus expected cash flows from the acquired assets in 2023 and 2024. Based on current projections and \$75 per barrel Brent pricing, the adjusted free cash flow delivered by the combined company, after the transaction is fully paid for in 2024, is expected to be 15% to 25% greater than Berry without Macpherson.

The Macpherson assets, which are high-quality, low-decline producing properties, are a natural fit with our existing rural Kern County portfolio. In addition to the attractive base production, we see upside for near-term production enhancement and development opportunities by utilizing existing wellbores. This is a value-creating transaction for Berry and its shareholders, reflective of our disciplined capital return strategy. We are ideally positioned to capture future consolidation opportunities.

I will now turn the call over to Mike.

Michael S. Helm - *Berry Corporation - VP, CAO & CFO*

Thank you, Fernando. As always, more information is available in our earnings release issued this morning and in our 10-Q filing available later today. But here are a few highlights.

Our financial and operational results were strong this quarter. Adjusted EBITDA totaled \$69 million compared to \$59 million for the first quarter. This 17% increase, despite the lower oil prices, is primarily due to higher production and lower lease operating expenses. Lease operating expenses, including the effect of gas purchase hedges, decreased 23% from Q1, most of which is attributable to the lower fuel costs and lower lease maintenance costs.

We also continue to implement ongoing cost-reduction initiatives during the quarter, some of which are beginning to bear fruit entering the second half of the year. An example of this is the completion of the solar project at our South Belridge property, which, in addition to reducing our carbon footprint, is expected to reduce our annual power cost by about \$300,000.

Adjusted G&A expenses were down slightly compared to the first quarter, and we expect to see continued improvement throughout the rest of the year. Second quarter adjusted free cash flow was \$34 million, which, after taking into account the use of working capital in the first quarter, resulted in a cumulative net adjusted free cash flow of \$7 million for the first half of '23. Accordingly, we have declared a variable dividend of \$0.02 per share in addition to the quarterly fixed dividend of \$0.12 per share.

As a reminder, our shareholder return model is based on annual adjusted free cash flow calculated after the payment of the fixed dividend, 20% of which is earmarked for variable dividends. The remaining 80% is intended for opportunistic debt and stock repurchases as well as strategic growth and the acquisition of producing bolt-ons.

Berry was active with share buybacks in the second quarter, repurchasing around 1.4 million shares in the open market for approximately \$10 million at an average price of \$7.04 per share. We have an additional \$190 million authorized for future stock buybacks and \$75 million authorized for debt repurchases.

To summarize, Berry is hitting its operational and financial targets and is well positioned for continued success, maximizing shareholder returns.

Back to you, Fernando.

Fernando Araujo - *Berry Corporation - CEO*

Thanks, Mike. In closing, our second quarter results have delivered on our commitment to maximize shareholder returns and achieve operational excellence. We are on track to meet our annual production goals with less capital spend and decreasing operating expenses. We are confident in our ability to enhance free cash flow and shareholder returns going forward.

We believe that the current industry and market conditions are favorable for M&A, and the Macpherson acquisition is evidence of that. Berry remains well positioned to be a consolidator, and we are actively pursuing other opportunities that align with our strategy to maximize shareholder value.

With that, I will now turn the call over to the operator for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Charles Meade with Johnson Rice.

Charles Arthur Meade - *Johnson Rice & Company, L.L.C., Research Division - Analyst*

Fernando, I want to pick up exactly where you left off there with your prepared comments about -- you said that conditions are becoming more favorable for A&D or for acquisition opportunities in Kern County. And this looks like a good deal, this first deal. But can you elaborate a bit on what are the prospects for more opportunities like this coming your way?

Fernando Araujo - *Berry Corporation - CEO*

Yes, very good question, Charles. In California, in particular, we're seeing a renewed interest in M&A opportunities, especially with the current regulatory environment. Groups are willing to have a conversation now more than before, and we are very active in those conversations with several parties. We believe the future of California, its consolidation, in order for industry to be able to achieve those synergies, those operational synergies, is available. And we, as Berry, want to be that company, that leading company that consolidates assets.

Obviously, we continue to evaluate producing properties in Kern County, but also in Utah, in other places, in all cases, properties that would align with our strategy to maximize shareholder returns. We are looking at opportunities to be able to keep production flat or even increase production in some cases. We are focusing on areas where we can see immediate operational synergies, at areas where we can apply some of our proven technologies to be able to enhance the value of those assets. So we're very active currently, Charles, looking at different opportunities. But this is the time.

Charles Arthur Meade - *Johnson Rice & Company, L.L.C., Research Division - Analyst*

Got it. So just to push on that a little bit more. If I understand you right -- or if I understand correctly, is this something along the lines of, these are family-owned businesses, public family-operated, and they've -- they've been doing the same sorts of projects for years. And now because the regulatory environment has maybe shut some of those activities down there, it's kind of forcing a reevaluation of their strategic direction. Is that -- am I understanding correctly or along the right lines?

Fernando Araujo - *Berry Corporation - CEO*

Yes, you're correct in that assumption. A lot of the smaller companies are kind of reevaluating their businesses now with the current environment. But again, we're looking at not only some of the smaller players, but are looking at different-sized companies or opportunities as well.

Charles Arthur Meade - *Johnson Rice & Company, L.L.C., Research Division - Analyst*

Got it. Got it. Okay. And then maybe just a second follow-up there. So obviously, this is -- this Macpherson is -- it's in your wheelhouse in Kern County. But most of -- in my understanding, most of your production, not all, but most is more west of Bakersfield, whereas your existing Poso Creek and this Macpherson is more north of Bakersfield. So are there -- how is the opportunity set kind of different or perhaps better with these assets since you're kind of waiting up in this area?

Fernando Araujo - *Berry Corporation - CEO*

Yes. We have -- we see opportunities both on the eastern side of Kern County, which is the case of Macpherson, and also the western side of Kern County, where most of our operations are. So we are talking to folks on both sides. Now Macpherson, as you know, is fairly close to our Poso field. So we're going to be able to realize some synergies just because of the economies of scale. But we are seeing opportunities in both sides of the basin, and then we're actively looking at everything.

Operator

Our next question comes from the line of Tim Chatard from Meros Investment Management.

Timothy Darin Chatard - *Meros Investment Management, LP - Portfolio Manager*

Just curious if -- I'm sure you're aware of California Resources and their efforts to more or less split their company into 2 businesses, E&P on one side and carbon management on the other. Is that structure at all relevant to you in your assets since you operate in somewhat similar proximity to where they are?

Fernando Araujo - *Berry Corporation - CEO*

Yes. Very, very good question, Tim. And the big difference between CRC and us is really size. Our goal, when it comes to ESG, in particular, is to be a good corporate citizen and to be able to minimize environmental impact. As far as carbon capture projects, we want to be more of a follower than a leader. So we are talking to different parties about the possibility of collecting our emissions and delivering those emissions to a third party. But we don't -- we just simply don't have the size to be able to have our own project like CRC.

Timothy Darin Chatard - *Meros Investment Management, LP - Portfolio Manager*

And it seems like they're bringing in outside capital via a partnership. So in other words, I don't think they're handling it all on their own. But I'm just -- I guess, you've answered the question, but I'm just pointing out that, yes, they're larger, but there's also outside capital that's looking for things like this. Can I ask you a separate question, whether there's been any change in the court process with Kern County timetable, with the appellate court system or anything along those lines that you can offer color to?

Fernando Araujo - *Berry Corporation - CEO*

Yes, yes. Sure, Tim. The permitting situation really hasn't changed as -- since the last time we reported with the court issuing a stay back in January, as you know. Now the appeal process is underway, and the court is expected -- the court process is expected to take a few months. So we're expecting to have a ruling at the end of the year, beginning of next year.

We're confident that the courts will reinstate the Kern County EIR, although that is obviously a risk, and it's not a given. But we'll be ready for that. We've got several -- we've got on the order of 84 Kern County permits, County cards as they call them, ready to go when that happens. But for now, there's really been no additional movement beyond what I just talked about.

Operator

(Operator Instructions) I'm showing no further questions. So at this time, I would now like to turn the conference back over to CEO, Fernando Araujo, for closing remarks.

Fernando Araujo - *Berry Corporation - CEO*

Well, thank you, everyone, for attending, and be safe and until next time. We're excited about what's going on with Berry. We're excited about the results in Q2, and we'll keep going. So thank you.

Operator

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

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