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Trinidad Drilling Ltd. (TDG.CA)

Q3 2017 Earnings Call

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Jeff Fetterly
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MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Chris, and I will be your conference operator today. At this time, I would like to welcome everyone to the Trinidad Drilling Third Quarter 2017 Financial Results Conference Call and Webcast.

All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions] Thank you.

Lisa Ottmann, Vice President, Investor Relations, you may begin your conference.

Lisa Ottmann
Vice President-Investor Relations, Trinidad Drilling Ltd.

Thank you, and thank you for joining us today.

We'll be discussing Trinidad Drilling Limited's third quarter and year-to-date 2017 financial and operating results, which we released yesterday. A full copy of the MD&A and financial statements along with a presentation outlining the quarter highlights are available on our website at trinidaddrilling.com. Our full third quarter 2017 results are also available at sedar.com.

Please note that during the call, we'll be discussing forward-looking information relating to various areas of our business, including but not limited to, the assumption that Trinidad's customers will honor their take-or-pay contracts; the ability for Trinidad to attract and retain qualified crews to operate their rigs; assumptions respecting capital expenditure programs by oil and gas exploration and production companies; assumptions made about future performance or operations of the joint ventures; assumptions made about future liquidity, future dayrates, and other expectations about future events or performance.

Such information and statements involve known and unknown risks, uncertainties, and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking information or statements. And you are cautioned to not unduly rely on such forward-looking statements. For a copy of our full forward-looking disclaimer, please refer to the disclaimer included in yesterday's news release and our MD&A.

The conference call may also include non-GAAP measures. For a definition and reconciliation of the non-GAAP measures, please refer to our MD&A.

I'm joined this morning by Brent Conway, President and Chief Executive Officer; and Lesley Bolster, Chief Financial Officer. Lesley will begin with a review of our third quarter results, followed by an update on current industry conditions and our future outlook by Brent. We encourage you to read our full quarterly report for additional details and commentary.

Please go ahead, Lesley.

Lesley Bolster

Chief Financial Officer, Trinidad Drilling Ltd.

Thank you, Lisa. Good morning.

Our third quarter results reflected improved industry conditions compared to last year and the previous quarter driving higher activity levels and increased adjusted EBITDA in the current quarter. Adjusted EBITDA in the third quarter was CAD 28 million, up from CAD 18 million in the same quarter last year and CAD 15 million in the second quarter of 2017. Adjusted EBITDA increased from the previous periods largely as a result of higher activity levels in North America, partly offset by lower dayrates in Canada and the impact of a stronger Canadian dollar against the U.S. dollar.

As industry conditions have improved in 2017, we have put a significant number of rigs back to work and operating days increased strongly, up 79% in our Canadian division and 146% in our U.S. and international division compared to the same time last year.

In Canada, higher activity levels drove increased operating income compared to the same quarter last year and the second quarter of 2017. The impact of a greater number of operating days was partly offset by lower dayrates as we've had more rigs operating on the spot market and a greater proportion of smaller rigs working in the current quarter. Operating income in the third quarter was also positively impacted by early termination and standby revenue received for the shortfall days on the three rigs in Canada.

Activity grew in our U.S. and international division compared to the same quarter last year and the second quarter with our biggest area of operations continuing to be in the Permian Basin in Texas, whereas higher activity levels in the current quarter drove improved operating income.

In the U.S. and international division, dayrates lowered from the spot the same period last year, largely due to a higher number of rigs working in the spot market, compared to legacy contracts in the prior year. When compared to dayrates in the second quarter, dayrates excluding the impact of early termination and standby revenues increased, reflecting the improved industry conditions and rigs returning to work at higher dayrates. This is the second quarter in a row we are seeing an improvement in underlying dayrates.

Operating costs in the U.S. and international division increased in line with activity growth in this quarter and were less impacted by rig re-activation and transportation costs than previous quarters.

In our joint venture operations, adjusted EBITDA in the third quarter was approximately CAD 3 million compared to CAD 6 million in the same quarter last year and CAD 4 million in the second quarter of 2017. Adjusted EBITDA in the joint venture lowered in the current quarter due to reduced activity levels. In addition, when compared to the prior year, lower dayrates in our Saudi Arabian division also negatively impacted adjusted EBITDA.

In the third quarter, G&A costs were approximately CAD 14 million, up from CAD 11 million in the same quarter last year and down slightly from CAD 15 million in the second quarter. G&A costs increased compared to the same quarter last year due to a higher share-based payment expenses, salary expenses, professional fees and costs associated with RigMinder.

We expect G&A costs excluding share-based payment expenses and third-party recoverable costs to be approximately CAD 58 million in 2017, up slightly from our earlier guidance of CAD 56 million. Expectations for G&A expenses grew slightly as a result of increased professional fees and salary costs and the addition of RigMinder.

During the third quarter, we continued to make progress on our capital upgrade program. To date, we have spent approximately CAD 111 million and completed a significant portion of the capital program. In addition, during the quarter, we acquired RigMinder, a global provider of rig technology, adding new revenue generating streams to our business.

Including the cash spent on RigMinder and on our joint venture operations, total capital expenditures to date in 2017 totaled CAD 143 million. With our upgrade program nearing its end, we expect the total capital for 2017 will be approximately CAD 175 million.

Our outstanding debt levels increased during the quarter with CAD 51 million drawn on our revolving facility at the end of the quarter. Debt levels increased due mainly to the timing of the capital program and cash paid for the RigMinder acquisition. We remain committed to maintaining conservative leverage and expect to manage our business within cash flow next year.

Now, I will turn the call over to Brent to provide some insight into current industry conditions and our future outlook.

Brent J. Conway

President & Chief Executive Officer, Trinidad Drilling Ltd.

Thank you, Lesley, and good morning, everyone.

As Lesley mentioned, industry conditions were stronger in the third quarter compared to last year, and customer demand remained firm. Activity levels have flattened out as we get closer to the end of the year, driven mostly by customers who have already completed their 2017 capital spending plans.

From the discussions we're having with our clients, we expect the activity will increase early in 2018 as new budget funds are spent. Dayrates have remained firm and we have not seen any downward pressure as customers wait on new budgets to be approved. We expect dayrates to remain stable with a strong potential for increases depending on commodity prices as we move into 2018.

As we have seen in 2017, we would expect dayrate increases in the U.S. to continue to outpace the increases in our Canadian fleet. In general, we have found the Canadian market challenged compared to the opportunities in the U.S. and internationally. We remain committed to our operations, our clients and our people in Canada. However, given current market dynamics, additional capital investment will likely be spent in other jurisdictions unless the competitive landscape improves.

We currently have 32 rigs or 46% of our Canadian fleet operating with firm commitments for several more rigs to start up during the winter drilling period.

In the U.S., our activity continues to be very focused on the Permian. This remains our busiest area with 28 rigs or 76% of our active U.S. fleet operating in this play. While the industry active rig count in the U.S. has lowered in the past few weeks, we have been able to maintain our activity levels. In fact, we've added additional – we have additional rigs starting up in the coming weeks as our upgrade program is completed and rigs go back to work. We currently have 37 rigs or 54% of our U.S. fleet operating and expect to get to approximately 40 active rigs by the end of the year.

And in the first half of 2017, we have incurred costs to reactivate and transport rigs to new locations for work. And in the third quarter, these costs had a smaller impact on the operations and we expect to see that impact lessen further in the fourth quarter.

In our Halliburton joint venture, three of our Saudi rigs are working on a well-to-well basis and one rig in Mexico is currently working. The contract on the Mexican rig is due to expire at the end of the year. We are working on several opportunities for our international rigs. These opportunities will likely involve moving the Mexican rigs to the Middle East. The tenders we are pursuing generally involve longer-term contracts and several are expected to be awarded in the coming months. We hope to be able to provide better clarification on our future plans as we get more clarity on the tenders from our clients.

We currently have 33 rigs or 22% of our fleet under long-term contract with an average term remaining of one year. Of these contracts, approximately 30% include price escalation or performance-based clauses.

Over the past two years, we have seen the industry – we have seen changes in the industry with customers increasingly demanding greater efficiency, largely at the cost of the service provider. We are focused on strategically adjusting our business model to add new revenue streams that will enhance profitability and returns. Our recent acquisition of RigMinder fits well within this strategy, adding revenue associated with monitoring and optimizing both the drilling and the directional drilling process.

Integration of the acquisition is progressing well. We have begun to implement the RigMinder EDR units onto our rigs and have 20 units currently under construction. We are actively training our sales team and key operational personnel to increase their knowledge with both the EDR units and the Criterion, the guidance technology, and we expect to continue to roll out these services in the New Year.

We are also reviewing opportunities across the drilling base to find additional ways to add value for our customers and our shareholders. These opportunities may include adding technology offerings and integration to improve efficiency and performance. They may also include additional services or products when bundled with our existing offerings that can save our clients' money and enhance return for our shareholders.

Recent improvements in commodity prices are encouraging. However, we believe that stability is a key ingredient for the market and the investors and commodity prices can't remain at their current levels for an extended period of time, but we believe industry conditions will continue to improve. Firm demand from our clients and solid activity levels and slowly improving pricing fundamentals, all point to improved operating results. With our largely upgraded fleet, broad customer base and growing service offerings, we are well positioned to succeed in these stronger market conditions.

Before I conclude, I would like to say thank you to the Trinidad team. Our people have worked very hard through the ups and downs of the industry cycle and continue to provide the best results for our customers and maintain our strong safety performance and culture. This commitment is a key factor in our performance and we appreciate their efforts and determination.

Thanking for listening. I'd like to pass the call back to the operator and take any questions that may be on the line.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from Ian Gillies of GMP. Your line is open.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Good morning, everyone.

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Good morning.

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

Good morning.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Brent, RigMinder from a PP&E perspective at transaction time was about CAD 1 million. What sort of EBITDA do you think that could generate and how much you think you need to invest to get to that CAD 10 billion noted in the previous press release?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Yeah, I can't get into forecasting. What we're going to do in terms of EBITDA, I think, for us, we view RigMinder as a very strategic step into adding and focusing on performance. We talk about performance, we talk about widening our delivery of service and products to enhance our returns. We think that's a key strategic piece to doing that.

The EDR capital spend, the returns on that investment are very quick. So, we expect to get a solid return on that. And I think it builds the platform for what we're trying to do with Criterion and on the directional side. But I can't specifically get into forecasting what EBITDA is going to be on that [ph] capital genre (12:52), I just can't do that, sorry.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Okay. Then, maybe thinking about it a different way, as you thought about the capital allocation strategy, yeah, you noted rig upgrades for a payback in 2 to 2 1/2 years and RigMinder, it seems like, it's going to be longer than that acknowledging the strategic benefits. I mean, how did you [indiscernible] (13:15) process between those two and decided to move forward with RigMinder?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

I don't agree it's going to be longer than that. I think, EDR itself is going to be quicker than that, that's what we're talking about. And I can't get into – we don't look at it just on a payback basis. We look at it as a – on a return – full cycle return, half cycle return, but as we look at that business, we certainly believe that we've got a piece of business that's going to generate attractive returns as we develop that model.

So, again, I can't get into specifically the return of the payback. Payback is a measure that we use to look at just kind of what contract coverage we have. But we should be looking at full cycle returns and that's what we look out when we look at what we're doing with RigMinder or any investment. And so, I think that's the approach that we're taking to it. But I can't again get into forecasting return models on that investments. I can't get into that.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Okay. And when you think about the full cycle and half cycle returns, I mean, does that include the acquisition price?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Yeah, absolutely. We're looking at it from a – what kind of return that's going to generate on a normal level, return model that's 10, 15 years what does that look like? What does it do for us over the first five years? We look at all those things. I think, I just can't – I can't get into the details of what that looks like on a conference call.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Okay. With respect to the JV operating margins per day, we're down again quarter-over-quarter. I mean, is that a good reflection of what the business looks like at this point in time absent any additional contract awards?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Yeah. The only guidance we can give you today is that, the rigs in the Saudi market would continue on a well-to-well basis. Certainly, right now, there's a lot of moving parts on the JV and we understand that we're actively looking at putting the Saudi rigs to work at multiple jurisdictions, staying within Saudi and extending to the existing contracts, but negotiating both directly with Aramco and Halliburton, and that's going well. So, we think – and the performance has been very well. So, they've done very good. So, I think, it's going to be just – let us get the contract and the extensions in place and then we'll give you more guidance.

The Mexico rigs, we're again in the process of multiple tenders, both within Mexico and outside of Mexico to put those to work. So, I think, there's certainly upside on that, the ability to put those to work and what those new contracts and dayrates look like, but we can't tell you that until obviously we've got them signed, but and certainly looking a lot more positive today than it has for a very long time. So, as soon as we get something obviously crystallized, then we'll tell you guys.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Okay. So, the U.S. active rig count forecast is down, JV profitability looks like it's going to probably be a bit lower than I was expecting, yet G&A guidance is up, is Trinidad considering any cost rationalization initiatives along that line item in 2018, is CAD 58 million a good run rate?

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

So, I think, the first thing for us to the 2018 G&A is just to take the Q4 and use it as a run rate for the next year until we complete our budgets and basically give you a better number.

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

But to answer your question, so the rig count in the U.S. going from 45 to 40 and that really have more to do with what's happening with commodity pricing and us not being willing to spend capital for some of the client requests that are coming out at us, given where we were with commodity price and what we're doing with our cash flow.

So, those opportunities are still there going into Q1. In fact, I think, there's more opportunities on the table. So, I think that's a – maybe a quarter delay and that's all that is.

On the international side, if these – we certainly believe these tenders are going to add to both dayrate margin and overall activity from what we got today. But if for some reason, we don't see that happening, I think we've already shown the market that we'll cut hard and we'll have to. And so, we've done it before.

I think, G&A creep that you're seeing has got more to do with just pure activity levels which are up, the RigMinder deal and some of the other noises within what we're doing. But it's not like we're going out and increasing G&A in anticipation of getting these things. I think, if for some reason they don't, there will be cuts on the G&A side to make sure we size our business to what we're doing.

Right now, I'm pretty confident that we are going to be able to put these assets back to work, we're going to be able to add dayrate, we're going to be able to add contracts and add margins. So, it's just a timing event. That's all.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Okay. Thanks very much. I'll turn the call back over.

Operator: [Operator Instructions] Your next question comes from Jon Morrison with CIBC Capital Markets. Your line is open.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Morning, all.

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Morning.

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

Morning.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Brent, can you talk about how core dayrates are trending in Canada right now across rig classes? And would you expect your rig count to ramp much more beyond where it is today as we head into the end of the year?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Yeah. I think there's a couple of things playing out in Canada. First, in the quarter, we had more rigs running, certainly, and the rig mix did impact our overall dayrate. The trends are going up, across the different rig, I would say, rig classes, especially, certainly – probably, seen the biggest movement on the high spec AC and the [ph] high hookload heavy doubles (19:28) which makes sense.

As we go into where we were in Q3 and today, we have seen a little bit of a flattening out just because guys have spent their budgets, but if we look into Q1 of next year, I can see we're going to have more rigs running than we did last year. The dayrates are up and most of, if not all, of our big high spec equipment is running, which last year wasn't. Last year, we made a conscious decision to back off on working some of that equipment because the dayrates were at such a level we just thought we're wearing that equipment and we weren't really getting any return for it. So, that's changed this year.

If I think about kind of a higher spec AC triple last year, those are in that CAD 12,500, CAD 13,500 kind of range. We just parked on, we'd not work at that level and today, those dayrates are getting up into the all-in CAD 18,000, CAD 19,000 range. So, I think it's moved significantly. The Canadian market still has its challenges in just terms of overall capital spending here. But year-over-year, it's I see where we are going to be higher rig count, dayrates have moved and we should be able to generate a pretty good Q1.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Should we be expecting early term or standby revenue to roll over much into Q4, or is all of the revenue associated with Rig 58 now largely behind the company?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

No. I think you could still potentially see some of that. We haven't got anything that tells us today that we're going to have any terminations, if that's your question. But there still could be some shortfall payments that come into Q4.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Okay. From a high level perspective, I realize you don't want to talk too deliberately about 2018 CapEx, but where's your head at on prioritizing rig upgrades and trying to gain market share where you think it makes economic sense versus growing free cash flow over the next 12 to 18 months?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

So, for us, a very much year 2017 is invest, invest in the right markets, invest with the right clients. A view, as we look out into 2018, it's a harvest mode in terms of creating free cash flow. Certainly, domestically, I don't see spending that kind of money on the capital side just because I think we need another step change and where dayrates are to justify making those investments.

Internationally, it's the one area where we will look at or could be forced to look at some investments. But, we understand what we're – what our investors are concerned about. We understand free cash flow is important. And so, and we understand we need to manage the balance sheet.

So, I think allocating capital will come at a higher standard on the capital side in terms of returns. I think we'll be conscious of making sure we do create free cash flow and also looking at overall leverage targets. I think all of those things are important. We had opportunity, we waited till dayrates moved, we waited till we got the right contracts. And so, I still think we made the right decision and I think really going into 2018, the benefits of those decisions are really going to start to pay off in what we can return to the shareholders in terms of free cash flow.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Lesley, with WTI now through $57, would you expect some dayrate escalation clauses to start kicking in for some of those [ph] commodity-linked (23:02) contracts that you've mentioned in the past?

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

Yeah. We are reviewing those right now, there is a couple we've identified and there's a couple more that will – they average out over a quarter, so we'll be looking at those for Q4.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Okay. Brent, just to go back to international, I realize that there's only so much information you can share. But based on the tenders that you have participated in specifically for the Mexican rigs in the Middle East, if you were successful with the earliest that you think that you're going to get visibility on that? And then secondly what's the earliest that we should be thinking about possibly recognizing revenue from those contract wins if they come through?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

So, we have tendered, I can tell you that. We are there in the evaluation phase, which is over the last two years with a lot of talking of tendering, it's actually happening now across different countries, different regions, different clients, so we've got multiple tenders in.

We know, generally, we are in the hunt for that, but we still have to win the contracts. The timing on some of them could be very quickly within the quarter. The other timing on some of it, it could end up getting extended into next year. But, it really depends on the tender, where we win the tender, which client, and what potential [ph] mode (24:25) we need to make to the rig to live up to their specs.

So, once we get better clarity, we will certainly make sure everybody knows, but it isn't just one tender or one country or one client, it's several and it may mean that we – the rigs in Saudi stay in Saudi and work direct for Aramco or for Halliburton, they may go someplace else, I think we're going to chase return and we've got them.

The advantage we've got now is we've been in that space for four plus years and we've been able to get a lot more plugged in, in terms of where the markets are that makes sense on return. And that's going to help us as we kind of get to renewing on these contrasts. So, I'm excited about what that could be, but I can't really get into a lot of specific guidance until I can tell everybody.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Okay. Appreciate the color. Just to follow on Ian's question, how many rigs has RigMinder on today, and has that changed over the past 2 1/2 months since you closed the acquisition, or obviously trying to push it on more of your own internal rigs?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Yeah. We've got it still on nine of our current rigs internationally that [ph] and went on all operating (25:37), but they're on all nine. And then we've got additional rigs in the U.S., I think we've probably – they had it on outside of Trinidad. There was another incremental, I think one or two they had it on, and then we are looking actively at adding it to a number of rigs focused on our strategic clients in and around the Permian.

So, we're building the 20 kits. We expect to have those deployed by the end of 2018. So, I think, today, I think it's on maybe two rigs in the U.S., our rigs and it's just being – they're being evaluated and added with clients everyday.

So, I think, it's something we're pushing. We're getting good feedback from clients. So, as we roll that out, we'll continue to update you guys, but it's still early days. But, we've got good response from clients and we continue to put the units into production that was one of the challenges. We didn't have a whole lot of units that we could put on, so we had to build somehow.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Last one just from me, I realize that I should ask this one last quarter, but can you give more color on what the rationale was to do this single rig JV with Charger Drilling Services in the U.S. and give an update on how things are progressing there since you did the deal in April?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Well, it's one very small rig. So, all of it was an asset that basically had no value, net book value. We had an opportunity to work with a local provider down there, who was actually working with a couple of our strategic clients that use it as a pre-set rig. So, it's just trying to make cash flow and return out of an asset that otherwise probably would sit idle. So, that's all it is. The actual operational side of things have gone well, the client is happy. It's not a big piece of our business, so.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Okay. Sorry, pardon my ignorance on this, but what would be the rationale to put that into a JV structure versus just pursuing those opportunities yourself? I just think of it from a high level perspective of going you guys have obviously a broad footprint, a ton of experience and a fairly meaningful market share in the Permian. So, I just, top of mind, it didn't come to me why you haven't just pursued those things yourself?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Well, couple of reasons. The partner is – they're in the pre-set rental business, they are in the lease construction business. We are struggling to find people in West Texas to just manage what we're trying to do there with rigs that we're adding. So, we're not in that business today. So, it just made sense to leverage off of their local ability to, accrue their local ability to – and what they do everyday – and maybe long-term, if it becomes a big piece of something that we can do, then we'll look at it. But, that was the rationale. It's pretty – it's a small piece of – just trying to see if this might work, that's all it is.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Okay. Appreciate the color. I'll turn it back.

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Thanks.

Operator: Your next question comes from Jeff Fetterly of Peters & Company. Your line is open.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Morning, all.

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Hi, Jeff.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

On the joint venture side, at this point, what do you expect activity to look like in 2018? The rig coming off of contract in Mexico, is it fair to assume that it will go idle?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

No. It's coming off of contract in 2018. We're actively negotiating to putting it back to work in 2018. It's coming off at the end of the year here, we're actively expecting that we're going to put those rigs back to work and we've got contracts, tenders that we're actively bidding on. So, yeah, no, I don't expect those rigs to be idle in 2018 at all.

And then the Saudi side of the equation, three rigs are running, we expect those to continue. We're also of negotiating, bidding directly with Aramco. We've got another two or three other jurisdictions we're looking at where we can put those and the other rig that's in Saudi today that's being bid into the multiple jurisdictions as well. So, no, I don't think that those rigs will be idle at all.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Let me just clarify. So, the rig in Mexico, you said in Q3, you operated one rig and the MD&A talked about that rig coming off of contract in Q4 2017. Am I missing something?

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

No. That's correct.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Okay. And so, in Mexico, do you expect to have any activity in Mexico after that rig comes off of contract?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Yeah. There are additional tenders. You probably saw then, usually it's the Pemex putout in terms of the production that they got on a well that was us, that was on that well. And so, they are looking at adding additional wells to that program, plus other wells associated with the 3,000 horsepower rig requirement. So, yeah, I think Mexico still is going to add – is still going to drill some wells and add those to their program. And we are talking with them and Halliburton to meet their needs. But it's still going to come down to contract and dayrate and margins. So, we've got multiple, I guess, fronts that we're looking at, putting those assets to work.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Okay. And on the Saudi side, the rigs that are running well-to-well, how much line of sight do you have at this point for those rigs? Is there risk that activity stops for any or all of those?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Not that we see today, Jeff. We see – the Saudi Aramco themselves put a tender out to add rigs to LSTK and then add rigs direct for oil and also add rigs to potentially go for gas which we can play in all three of those buckets. And we are actively talking to them and bidding on that. We're also looking at getting those rigs to two or three other jurisdictions.

So, yeah, I don't see those rigs going idle. We might have a staging upgrade timeline that we got to live up to just depending on where they go. But, today, we certainly believe that we're going to be able to continue working on, or put them to work someplace else if we do decide to go get a better dayrate someplace else.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Your comments earlier about potentially looking at some investments for the international rigs, how – obviously, you then could potentially have some rig moving or transportation costs, but how meaningful could upgrade costs be based on the tenders or specs that you're seeing today?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

It totally depends on where they go and what the spec requirement is. There are some stuff, obviously, if they stay in Mexico, we don't really need to do much to them, if they go to the Middle East, you might have to do more. It depends on what tender we're asked to live up to in terms of the spec.

Mobilization costs, and pretty much all of these contracts is covered. We get paid to move and so, we'll make some money on the move. So, it's not like an American model where we have and other guys have been forced to move rigs around. But in this case here, I don't see move costs being a big upfront costs, we're going to be compensated for the move. But, it's really – the capital commitment or the capital requirement will really depend on where we're asked to go.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

How important is free cash flow for you in 2018?I know you mentioned earlier the invest in 2017, harvest in 2018 concept. But if you're required to make some meaningful investments on the international side, are you willing to spend to cash flow or exceed cash flow in 2018?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

No, our goal is to live within cash flow. We know what the market – where we need to be in the market. We need to manage that. I think the challenge is, is that some of these markets will require some significant upgrades. So, we've got to balance that. And we're in a good position with a lot of these tenders where the team has worked really hard to get us on the bid list and get us – the performance to where it needs to be to be one of the preferred suppliers. So, we've got to balance that with the overall capital spend. We know we understand that.

So, I think that's the hard decisions we'll have to make. But we understand that free cash flow is important and managing debt levels are important. And we're going to live and manage the business accordingly.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

On the U.S. side, you'd previously talked about upgrading around 37 rigs this year. What do you expect the number to be now?

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

37 rigs is the whole capital program, Jeff, that was not just in the U.S.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Okay. And so, what do you expect the totals upgrade program to be?

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

It's around 33 I think just because we – when we went through the capital program a little bit when we did the RigMinder acquisition, some of those rigs came off of – we decided not to upgrade those rigs and that we wouldn't be spending the capital.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Okay. And on the RigMinder side, the 20 additional EDR units you're building, do you expect that those will be deployed on to Trinidad rigs or do you think there will be third-party rigs in there as well?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

I think it could be a combination to be honest, I think we're attacking it from both perspectives. We've got clients that are testing and we're in the process of putting them on, working with Criterion, the guidance system. So, I think it could be a bit of both. That certainly is the way we look at it in terms of where they might go.

We were really indifferent. I think, if it's a Trinidad rig, that's great, if the client wants to fit the EDR and the Criterion platform on all of their rigs, then we certainly would be willing to do that, so.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Okay. Just to clarify, you said earlier, it's nine rigs on the international side and two rigs in the U.S. that are currently running RigMinder EDR's?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Yeah, that's right.

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

On Trinidad.

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

On Trinidad rigs.

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

Yeah, Trinidad.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Trinidad rigs. And can you share how many third-party rigs are running RigMinder EDR today?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

I think it's four to five, depending on active rigs, there's been rigs up and down [ph] here as well (36:21), so I don't know for sure, but it was five. It could be less than that just because some rigs have moved around, but I think it was five, [indiscernible] (36:34) and that involve two or three clients.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Okay. And so a last question on the Canadian side, just to clarify. So, you expect Canadian activity on a year-over-year basis to be higher. Is that speaking to where your rig count peaks during Q1 or the average for the quarter, because last year, you were I think a peak of 38 rigs?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Yeah. When I talk about on the same broader activity with the right class of rigs, dayrates have improved, margins have improved, I think, generally, we're just going to be busier in Canada in Q1 this year than we were last year.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Okay. So, even though you've moved rigs out of Canada, you still expect on a year-over-year basis that strength predominantly coming from [ph] that tele heavy double (37:19) in terms of the...

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Yeah, and the AC triples. We're going to have more of the AC triples running this year than we did last year.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Okay, great. Thank you. Appreciate the color.

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Thank you.

Operator: Your next question comes from Ben Owens of RBC Capital Markets. Your line is open.

Benjamin Owens
Analyst, RBC Capital Markets LLC

Q

Hi, good morning.

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Good morning, Ben.

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

Good morning, Ben.

Benjamin Owens
Analyst, RBC Capital Markets LLC

Q

Just wanted to follow up on Jeff's question about the 20 EDR units that are on construction. How many of those 20 are already committed to specific rigs or specific customers at this point?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

I can't give you that, Ben. There's clients that are – there's multitude of clients that have requested them, that are waiting on these things. So, I can't get into specifics of how many are committed versus not committed, and it changes daily. So, even if I had the number, yesterday, I could be wrong.

So, I think that we're obviously focused on getting those 20 units out whether it's on Trinidad rigs or other rigs. And we believe that things go well, we could be back in building more units. But today, that's the guidance we're giving and we'll have those up by the end of the year, but I can't get into committed versus uncommitted today.

Benjamin Owens
Analyst, RBC Capital Markets LLC

Q

Okay. How long is the sales cycle for those units, from the time you get an order or decide to build one, to construct it and then install it on a rig? What's kind of the total time that would have lapsed there?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Well, the build cycle, I think we've given guidance on the build cycle. They're kind of 60 weeks to build sales cycle. Once you've got them on the shelf, it can be pretty quick. It's just a matter of getting the clients, they can rig up the EDR, the sensors, they can actually leverage off the fact that a lot of our AC rigs have a lot of the sensors they need. So, and they can rig up in a couple of days or a day. So, it's not really a big deal to rig it up.

So, it's really just trying to build some capacity in terms of some units on the shelf that we can actually go out and put on for clients. And there wasn't a lot of that. Once we closed the deal, we kind of pull the trigger on that. So, I think it's not this long sales cycle, I think it's a – you have the assets, you put them out there to try with the client, you test them and as they understand or they're happy with the product and then really the bolt-on with Criterion bit guidance, you just go from there.

Benjamin Owens
Analyst, RBC Capital Markets LLC

Q

Okay. Thanks. Looks like you guys are on pace for about CAD 30 million to CAD 35 million in maintenance CapEx this year. Is that a good range for next year?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Yeah. We haven't given guidance for next year yet. We haven't even finished our budget process yet, but I think we've kind of always said that we'll be in the CAD 20 million to CAD 30 million on, I would say, the preventative maintenance, sustaining CapEx side of things. I think that's still a run rate that makes sense. So, we're looking at that internally already with our divisions and working with our clients in terms of what their demands are. But I think that that generally is not a bad – it's not a bad range to be in.

Benjamin Owens
Analyst, RBC Capital Markets LLC

Q

Okay, great. Appreciate it, guys. I'll hand it back. Thanks.

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Thank you.

Operator: Your next question comes from Ian Gillies of GMP. Your line is open.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Hi, everyone. Sorry, just a few follow-ups here. With respect to RigMinder, is there an iPhone app that goes along with this, that's competitive with some of your – I guess, that would be competitive with some of the larger peers in the U.S. that are also offering similar products? And if there isn't, I mean, how are you thinking about approaching the technology piece as it seems to be increasingly important for this product line?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Yeah. It is something that's developing right now. They have a version of that that they're working with, but it's still early stages in terms of being able to deliver that. So, that's something that – the platform is built in a way that it won't be hard to get there. And we've kind of walked in and said, okay, that's important, it's a key piece of what we think of what the product offering needs to have. So, we're working on that, and it's something that today we're certainly looking at and it'll be a long way down the pathway, by the end of the year and looking at – talking and producing that and talking to clients by Q1. So, it's definitely front of mind for us as well.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Okay. And just to follow on Jeff's questions about the international rigs and bidding them out, is it all within the current JV, or is it outside of the JV? And if it is outside of the JV, is there a mechanism in place where you would have to buy back the rigs from your partner?

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

No, it's both. And it doesn't matter whether the rigs are in or out of the JV, if they're going to pursue dayrate, Halliburton is our partner, they will continue to participate as our partner. It was always set up that way that we had the ability to utilize the assets for both of our benefits. So, if that happened, Halliburton would still be our partner. There's no trigger that says we have to buy them. We would just continue to run and the return and the EBITDA that is Halliburton's percentage would go directly to them.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Okay. Thanks very much. Appreciate it. I'll turn it back over.

Brent J. Conway
President & Chief Executive Officer, Trinidad Drilling Ltd.

A

Okay. Thanks, Ian.

Operator: [Operator Instructions] There are no further questions. I'll now return the call to Lisa Ottmann.

Lisa Ottmann
Vice President-Investor Relations, Trinidad Drilling Ltd.

Thank you. Thank you for taking the time to participate in our call. We look forward to talking to you again in the future.

Operator: This concludes today's conference call. You may now disconnect.