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Trinidad Drilling Ltd. (TDG.CA)

Q4 2017 Earnings Call

CORPORATE PARTICIPANTS

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James A. Spicer
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Jeff Fetterly
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MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Emily and I'll be your conference operator today. At this time, I'd like to welcome everyone to the Trinidad Drilling Year-End and Fourth Quarter 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 of 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 Fourth quarter and year-end 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 year and fourth 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 a strategic review process, 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. You are cautioned to not unduly rely on such forward-looking statements.

For a full copy of our 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 fourth quarter results, followed by an update on current industry conditions and our future outlook by Brent.

We encourage you to read our full MD&A and financials for additional details and commentary. Please go ahead, Lesley.

Lesley Bolster

Chief Financial Officer, Trinidad Drilling Ltd.

Thank you, Lisa. Our fourth 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 fourth quarter was CAD 36 million, up from CAD 24 million in the same quarter last year and CAD 28 million from the third quarter of 2017. Adjusted EBITDA increased from the previous period, largely as a result of higher activity levels in North America and lower operating costs in our U.S. and international division.

As industry conditions have improved in 2017, we have put a significant number of rigs back to work and operating days increased strongly in the fourth quarter, up 87% in our U.S. and international division and 21% in our Canadian division compared to the same time last year.

Towards the end of the fourth quarter, we saw some customers stop working earlier than we had expected, once they had completed their 2017 capital spending plans. Activity levels have since rebounded and as 2018 capital spending plans are now in place for our customers. Activity grew in our U.S. and international divisions compared to the same quarter last year and the third quarter, with our biggest area of operations continue to be in the Permian Basin in Texas. Our activity levels combined with lower operating cost drove improved operating income in the quarter.

In the U.S. and international division, dayrates were in line with the same period last year and up 4% from the third quarter, as the impact of rigs rolling off legacy contracts was offset by rigs signed up on newer contacts.

Underlying dayrates excluding the impact of early termination and standby revenue continue to improve and were $400 to $500 higher than the same quarter last year and the third quarter of 2017. We estimate that the spot market rates for high spec rigs in the U.S. are up $4,000 to $5,000 compared to the same time last year.

Operating costs in the U.S. and international division grew at a strong – at a slower rate than operating days in this quarter. As we were less impacted by rig reactivation and transportation costs than in the previous quarters and demonstrated improved cost management.

In Canada, higher activity levels drove increased operating income compared to the same quarter last year. The impact of a greater number of operating days was partly offset by lower dayrates. When compared to last year, as we have more rigs operating on the spot market and a greater percentage of smaller rigs working in the current quarter.

In contrast, the increase in operating income in Canada, when compared to the third quarter, was driven by higher dayrates in the current quarter as reactivated more high spec rigs and received extra revenue for winter drilling equipment. Activity levels were relatively unchanged from the third quarter.

Operating income net percentage or gross margin in the fourth quarter was also positively impacted by standby revenue received for shortfall days on three rigs in Canada. The shortfall revenue we received in the quarter was all for days that would have been worked in the fourth quarter. All three of these rigs remain under contract, but two of them now are back at work.

In our joint venture operations, adjusted EBITDA in the fourth quarter was approximately CAD 2 million, compared to CAD 7 million in the same quarter last year, and CAD 3 million in the third 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 fourth quarter, G&A costs were approximately CAD 13 million, down from CAD 15 million in the same quarter last year, and down slightly from CAD 14 million in the third quarter. G&A cost decreased compared to the same quarter last year due to lower share-based payment expenses partly offset by higher salary expenses, professional fees and costs associated with RigMinder.

Early in 2018, we reviewed our cost structure and made several changes to lower our G&A expenses. These changes included reducing head count, rolling back executive salaries and board feels and overall tightening on our expense management. Following these changes, we expect G&A costs excluding share-based payment expenses and third-party recoverable costs to be approximately CAD 43 million in 2018, a 26% reduction from what we incurred in 2017.

We completed our 2017 capital upgrade program in the fourth quarter and have identified a smaller number of rigs to upgrade in 2018, largely part of our redeployment of rigs to the Permian Basin that we announced earlier this year.

Our capital program totaled a CAD 163 million in 2017, with the vast majority of our capital spent on upgrading existing assets to meet growing customer demand. In addition, we spent CAD 4 million on our joint venture asset and CAD 31 million on the acquisition of RigMinder. In total, this was slightly higher than we had anticipated due to growing customer demand and increased maintenance and capital required to reactivate equipment.

In 2018, we expect to spend approximately CAD 94 million in capital expenditures, just over a half of this will be spent on the [indiscernible] (07:24) capital as we anticipate ongoing strength in our activity level.

The growth capital of our capital program is largely related to the deployment of eight rigs to the Permian Basin from areas of weaker demand, including two rigs moving from Canada, three rigs moving from Saudi Arabia and three rigs moving from less active areas within the U.S.

Our outstanding debt levels increased during the quarter with CAD 85 million drawn on our revolving facility at the end of the year. Debt levels increased due mainly to the completion of the capital program.

We remain committed to maintaining conservative leverage and expect to manage our business within the cash flow in 2018.

Now, I'll 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 fourth quarter compared to last year. Although we did see a slight slow down towards the end of the year as client capital spending programs still slightly at year-end.

Activity levels have rebounded so far in 2018 and we are seeing upward momentum for dayrates in the U.S. particularly for high-spec rigs. Dayrates have remained firm in Canada, but have not seen the same ability to put through increases we've seen in that in U.S.

As we saw in 2017, we would expect dayrate increases in the U.S. to continue to outpace increases in our Canadian fleet. In general, we have found the Canadian market challenged compared to opportunities we have in our U.S. and international divisions, which is the main driver for our relocation of rigs from Canada to the U.S.

In the U.S. division, our activity continues to be very focused in the Permian. This remains the busiest area of 31 rigs or 80% of our active rig fleet operating in the play. The industry active rig count in the U.S. has increased since the end of 2017 and we continue to see strong demand from our customers. We currently have 39 rigs or 59% of our fleets operating in the U.S. In addition, we have 39 rigs or 57% of our Canadian fleet operating 6 percentage points above the industry average.

As always, activity levels towards the end of the first quarter will be very dependent on weather conditions. As we look into the summer, visibility is still quite limited as customers moderate commodity prices and differentials against their budget plans.

In our Halliburton joint venture, as Lesley mentioned, three of our Saudi rigs will be moving to the U.S. where we expect them to begin working in the third quarter of 2018. The remaining rigs from our Saudi operations is currently working, as we're moving to Bahrain where we expect to be given work early in the second quarter.

We are working on several opportunities for international rigs. These opportunities will likely involve moving some or all of our 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 from the tenders as we work with our clients.

We currently have 31 rigs or 21% of our fleet under long-term contract with an average term remaining above one year. We are currently working with customers to negotiate contracts on the rigs being deployed in the Permian.

The roll-out of the RigMinder's products is going well. Criterion RigMinder's directional advisory software is currently being used by customers in both Canada and the U.S. and encouraging results point to adding additional customer deployment as we move forward.

Our Canadian customer is also currently working a partnership at Trinidad to test and evaluate the GMXSteering frac optimization software, as well RigMinder now has in place several agreements to provide integrated tool solutions, including agreements with multinational suppliers and download tools. We have begun to market their service to our clients and are encouraged by customer interest levels. In addition, we're continuing to add RigMinder EDRs to our rigs.

Despite the improving industry fundamentals and recent steps, industrial fundamentals and recent steps we've taken to improve shareholder value, we do not believe that our current stock price reflects the value of the company. As a result, our board of directors have recently initiated a strategic review in an effort to enhance shareholder value.

In connection with this process, the board intends to undertake a comprehensive review of a broad range of alternatives and the potential to enhance shareholder value including a sale of select assets, a merger, a corporate sale or a strategic partnership in various capital or redeployment opportunities.

This review is not a reflection of our financial or operational situation. We remain in a strong financial position generating free cash flow from our core business to fund our capital program and we have additional liquidity through our existing credit facilities. There is no guarantee that the strategic process we are undertaking will result in a transaction. To that end, we will continue to manage our business carefully with a focus on enhancing returns.

We will remain focused on providing customers with the strong performance they have come to expect from Trinidad, while also maintaining our commitment to safety of our crews and the condition of our high performance equipment.

We have not set a definite schedule to complete this review and do not intend to disclose developments unless the board has approved a specific contraction or an action plan or to size the disclosure is necessary or appropriate.

Thank you for listening. I would 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 Benjamin Owens from RBC. Your line is open.

Benjamin Owens
Analyst, RBC Capital Markets LLC

Q

Hi guys, congrats on a good quarter.

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

A

Thanks Ben.

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

Thanks.

Benjamin Owens
Analyst, RBC Capital Markets LLC

Q

So on the eight right that you announced you're going to move to the Permian can you tell us how many of those already have a contract?

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

A

Well, there is I can tell you there is four or five different clients, and we are in the final strokes of finalizing those contracts, but can't get into the specifics but we're fairly far advanced.

Benjamin Owens
Analyst, RBC Capital Markets LLC

Q

Okay. Sticking with the U.S. curious where do you expect operating cost to shake out in the first quarter versus the fourth quarter? In the fourth quarter period you had a pretty clean quarter but obviously in the first quarter you've got some rigs moving along, so just curious if those costs would move back up a little bit?

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

A

Yeah, I think our, I think our overall number for the year was in the 12,500-ish range.

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

Per day.

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

A

On a per day basis. I think we are finally seeing and I think the world's finally seeing the efficiencies around cost controls and getting a lot of the rig startups behind us. Starting up one or two rigs a quarter really impacts our op cost in an operating quarter when you've only got 12 rigs running, right.

So I think it's really we are starting to see the benefits of what you're doing on the cost control side. So, I would expect that we could bring down the average closer to kind of the midpoint between where we were in Q4 and where we were on an annualized basis and we're going to keep pushing to improve that. I think there are still things we can do and to manage that op cost structure and I think we are finally starting to get some of the cash generating capability from these activated rigs that is actually showing up as we expected it would.

Benjamin Owens
Analyst, RBC Capital Markets LLC

Q

Okay that's helpful. Given all the moving pieces with the joint venture rigs, do you have an estimate of how many of those JV rigs you expect to working through the first quarter?

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

A

Well we've obviously got our Bahrain rig going back to work, we expect that we'd be able to put one rig to work [indiscernible] (15:08) here very shortly and then we're going to have the three rigs in Saudi that will be moving to the U.S. So there is other opportunities there that we just haven't, we can't talk about it yet, but, I think those are the ones that are the minimum, we do expect to – we've got good near-term visibility on that they are going to be working.

Benjamin Owens
Analyst, RBC Capital Markets LLC

Q

Okay and then the last one from me on the international rig tenders you spoke about. Do you think it is likely that your potential customers would pay for the relocation cost to move the rigs from Mexico over to the Middle East?

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

A

Yeah, they will absolutely that's part of the contract, it's built into the contract that they will pay the relocation and from a way you step back and look at what that is and what those contracts are, we've got cash in the JV to use to do what we need to do on the upgrade side. So we're committed to, we get the rig contract and we get the right timing, you move the rigs to a better market, better contract term, better returns. We still understand and are managing to living within cash flow and it's just a good piece of business in terms of enhancing returns for on the assets and getting ourselves real focused on what we're doing internationally.

Benjamin Owens
Analyst, RBC Capital Markets LLC

Q

Okay thanks, I appreciate the color. I'll hand it back.

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

A

Thanks Ben.

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

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Good morning, everyone.

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

Good morning.

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

A

Good morning Ian.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

In the U.S. with respect to dayrates, I mean the sequential changes have been reasonably stable over the last couple of quarters. Are you seeing any change in the rate of change in the U.S. dayrates, like should we be expecting it to getting any better any worse as we go through coming quarters here based on what you're seeing today?

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

A

Based on what we're seeing today that rates are moving, they're moving up. We're getting clients that are again talking about either doing stepped up dayrates to get to a two-year deal or a higher blended rate. So, what I can tell you from a client perspective is that we are getting lots of request to contract – the typical thing is when they think pricing is going to move they want to contact, they want to contract longer and they want a fixed price we're not doing that. We're going to be very careful what we contact. We want to make sure we've got leverage to the upside and we want to make sure that where we can they've got skin in the games.

So it has changed probably in the last 90 days as they've I think got to their new capital budgets. I think they are still in the same situation where they're living within cash flow, but obviously commodity pricing has improved, they're getting really focused on what they need to do. And so they want to make sure they have got the right I would say rig spec and he right performance metrics in their contracts, but the pricing is moving.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Okay. With respect to the Permian, I didn't quite catch all Lesley's comments and where all those rigs that are coming, but with those eight rigs going in are they going to be incremental work for customers, are you capturing market share and pushing out some existing rigs as well. I guess what I'm getting trying to get a sense for is, I mean do you think Trinidad captures market share over the 12 months, if the rig count were to remain flat?

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

A

I think it's a combination of both Ian, I think there is some where we are adding rigs to clients that are spending more money and then in other cases we're actually displacing others. So, it's a bit of a blend. So it's kind of – there is a few moving parts it is that is little tough for us to give you complete visibility, but I know it's a blend from the clients that and what they are asking us to do.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Okay and Lesley did you say in your prepared comments I heard three rigs are coming from in the U.S. what were the other numbers in that comment, my apologies, I just missed it.

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

So it was three from the U.S. two from Canada and three from Saudi.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Okay. And then last one from me given your exposures to [ph] money (19:36) and in some respect dry gas what's the leading edge commentary from your customers at this point in time around activity not just for when it may pull back in Q1, but what it may look in the back of the year?

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

A

I think they are all facing the same issue across the board. There is, they've got trapped gas, they've got trapped oil, the differential is still wide. They're living in a world where their cost are going up, our cost are going up in terms of just drilling contractors and what we are being asked to do with our workforce. I think it is in the Canadian space, everyone's going to be real tight to make things work economically. So they'll be very selective in they do as well will happen. I think, there is a dynamic there that is still pretty challenging for Canadian E&P producer.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

Okay and just to clarify when you talk about higher cost with respect to labor is that in relation to the new overtime laws in Alberta.

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

A

Well there is that and then how we have to pay it, there is that part of it. There is, we've got a tax regime that's gone the wrong way, we're good pipeline we are talking about situations where E&Ps actually going out and talking over buying railcars so they can get more product to market. So it's – I think there is a lot of things that drive cost up for producers, for us – it's more specific to labor but as we get pushed t and Canada too has their pumps 7,500 psi all that stuff pushes on consumables and we've got be able to push on dayrate we've been able to do that in the U.S. and the Canadian market. Our guys have done a good job of controlling the cost, but it's still just going to be a challenge.

Ian B. Gillies
Analyst, GMP FirstEnergy

Q

No, I certainly agree. Thanks very much for your color, Brent. I'll turn it back over.

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

A

Thanks Ian.

Operator: Your next question comes from the line of Jon Morrison from CIBC Capital Market. Your line is open.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Good morning all.

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

A

Good morning John.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Just in terms of the U.S. dayrates is the movement that can be on the horizon a function of improvement in the spot market or is it more the benefit of the 2017 CapEx investment that you've made.

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

A

I think it's both, we've got rigs that have rolled up contracts where we're going to be able to bump dayrates and then it's the spot rates, spot rates have moved again. Given a certain class of rigs, given a certain spec the rates have moved, so it's a bit of both. I think both are happening at the same time I guess I what I should say.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Okay, I guess I was a little bit surprised that the Canadian dayrate being a touch below where we may have thought that it was going to come in. Was that a function of rig mix specific to Q4 or would you just highlight Canada is being ultracompetitive right low for rates?

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

A

I think part of it is the rig mix for sure, you know, I think interested or not, it does just happen in terms of what rigs that makeup that parentage, I don't want to get into the specifics of it, but I think it had a lot to do with rig mix. I know year-over-year given a class in Canada the rates are up slightly but rig mix plays obvious into that average. Everyone looks at the average dayrate as an indicator of where the market is going but sometimes rig mix can mask trends so we're trying to be careful to make sure people understand what the trends are.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

I realize it's really tough to predict but when you think about rates from a 2018 perspective is the current line of sight for fair flattish pricing ex-winterization and all that noise.

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

A

In Canada?

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Yeah.

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

A

Yeah, I think it's flat I think we've got some potential on the upside there's just so many moving parts like I said to Ian, they are making it tough on the Canadian producers that it's just tough.

I think they will get real focused on what they're doing that will demand a certain rig class, we have the right rigs, we are in the those rig classes so I think we've got opportunity to continue to be fairly busy with our rig fleet. But it's not going to be certainly a broad-based increase in rates of utilization and activation like we're seeing in the U.S. that's for sure.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

And just in terms of early term standby revenues is there anything we should be thinking about factoring into our numbers for Canada or the U.S. or the JV going forward? I realize it's hard to predict and sometime these things are unforcastable, but is there any rigs running in Canada right now that we should be thinking about generating or move across in the JV that will be a tailwind in the next couple of quarters?

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

A

I can't give any guidance right now. The one thing I would say is that you know the numbers that are in Q4 are standby, those days would hit Q4 anyway, so there is really no out of period early term that really impacts the numbers. So I think that's a key point that everyone has to I guess has to take note of.

And then the early term going forward we're kind of past the point where a lot of that is going to come at us. I think a lot of the contracts that we're signing, there is a few still out there that are legacy contracts, but now that the market moved down and now we're back up in a lot of cases lot closer to those dayrates so I don't see big early term being a big part of what hits us here year over the next few quarters.

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

If anything you will see Jon the large rig in the [indiscernible] will continue to be on standby for now.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Okay, okay that was one of things I just wanted to make sure. In terms of the JV and line of sight right now is it fair to think about the JV probably not generating a lot of cash in the next couple of quarters just because you're moving the rigs back to the Permian and fixed cost absorption will probably be a bit of a headwind in next three to six months?

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

A

We are going to be working in Bahrain, I think there is a very good chance we'll have a rig working in Mexico and then the three rigs moving from Saudi obviously will be on a move, so the rest of the rig fleet where those are ones we're actively looking at in terms of where we put on it, some of these new tenders. So I guess all I can tell you is it's once we know more, we'll let you guys know more.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Okay. Last one just from me Brent on the Permian relocations you said that they're fairly advanced conversation. Is it fair to assume that pricing term is probably already captured in those advanced conversations, but it's just other things that will be worked through at this point?

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

A

I would say, yeah, that's pretty fair. One of the challenges we've got is, we've got a number of clients that are trying to get leases ready to actually move the rig on and we don't want to end up spending mobilization and neither do they, so we're just trying to get some leases prepared so we can move the assets on and get drilling. But generally, we're pretty close on term and we're pretty close on dayrate and even kind of mobilization. So they're pretty far advanced.

Jon Morrison
Analyst, CIBC World Markets, Inc.

Q

Okay. Thanks for the color. I'll turn it back guys.

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

A

Thanks.

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

Thanks.

Operator: Your next question comes from James Spicer with Wells Fargo your line is open

James A. Spicer
Analyst, Wells Fargo Securities LLC

Q

Hi good afternoon. I'm just wondering in the context of some of the strategic options that you're looking at how the balance sheet fits into your thinking, are there parameters, for example, in terms of leverage metrics that are important to you and you consider alternatives and are there potential scenarios where leverage goes higher as you pursue some of these options?

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

A

Yeah, I think honestly, we as a management team and the board has very clearly stated that the balance sheet is important to us. We were looking – we'll look at alternatives that add value to the shareholders. We don't – I wouldn't say sitting here today that adding debt to the balance sheet would be something that our shareholders would value. So I think, we'll look at when we are, it's fairly early in the process, we're looking at all options. But creating something that would deteriorate the balance sheet is not something that would make a lot of sense.

James A. Spicer
Analyst, Wells Fargo Securities LLC

Q

And are there specific leverage metrics that you are still targeting I think you're around 4 times today, is that sort of a safe level to think about going forward?

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

A

Yeah, we certainly, we've voiced to the market that we want to get down to kind of something closer to 2:1 with growing EBITDA and paying down debt, I think that's still a goal we're going to work towards but we're certainly not going to do anything that creates an event that causes us to get off side on the balance sheet.

James A. Spicer
Analyst, Wells Fargo Securities LLC

Q

I understand. Thank you.

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

A

You're welcome.

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

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Good morning, everyone.

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

A

Good morning Jeff.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

First question on U.S. margins. I know you touched on that earlier, but was there anything in Q4 that benefited the margins in terms of cost reductions or reversals?

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

A

No, I think the really, the benefit in Q4 was what I said, it's the cost reduction initiatives that we've taken on is managing our cost structure and it's – it was also during Q4 we had clients that – we had basically recovered more from clients on certain mobilization and/or some of the maintenance stuff that we were doing and so that's really what impacted Q4. But I think, we are starting to show what we've been talking about for the last three or four quarters that our cost structure is going to improve and our margin outlook once we get a lot of these rigs activated is going to get better, and so that's what you saw.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

So there were some mobilization and other things collected in Q4 that benefited like when I look at your cost per day you were under CAD 16,000 in Q4 and your annual number was about CAD 17,500. So your comment earlier that you'll be, you expect to be somewhere between the Q4 number and the 2017 annualized number, is that, did I hear that correct?

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

A

Yeah. I'm using U.S. numbers, so U.S. annualized we are around CAD 12,500, I guess and then in Q4 we're closer to...

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

CAD 11,600.

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

A

CAD 11,600. So yes, I am saying use the, kind of that middle midpoint is our go forward run rate. But we were telling or I guess what we're saying is that it had very little to do with noise in the quarter. There is a little bit of recovery, enhanced recovery than what we initially expected from clients. But it's also – it's mostly driven by cost cutting and just good cost management.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Okay from an activity standpoint in the U.S. with 39 rigs currently where do you expect your rig count to get to with the transfers combined with any incremental activity?

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

A

Well, we just announced we're going from 39, we've announced the 8 rigs that would get reactivated moves. And at this stage of the game that is as far as we are ready to commit in terms of staying anymore. I think there are other opportunities. We've got more client request than the eight but from our standpoint we want to make sure that those activations and the capital associated with those activations still allows us to live within cash flow.

So, I think, there is some other initiatives that we are undertaking that will help us lower capital cost and dayrates move a little more and we'll see where it goes. But at this stage of the game that's, we'll commit to that. And then as we have more opportunity, if that develops, then with the combination of, we have cash available to spend, we think it makes sense to spend based on return and that we can execute on the timing that our client needs then we'll take a look at that and see if it makes sense.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Is it fair to assume that to go beyond 47 rigs in the U.S. would require incremental capital investment?

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

A

Well, you are going to have to spend money to activate rigs. Yeah, is that what your question is?

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

More around the rig upgrades and other sustaining capital requirements?

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

A

Well if we're going to activate more rigs than the eight we've told you about then yes, we would have to spend more capital.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Okay.

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

A

Yeah.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

In terms of rates in the U.S. are you seeing pricing power extend beyond the highest spec rigs at this point?

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

A

Yeah, actually there this is kind of the four classes, we've got pricing power on the ultra-high end which is kind of our ultra-rig which is a high-spec three pump four gen moving system 7,500 psi we've pricing power there. We've also got pricing power on the two pump three gen type spec which is still high-spec rig even on a SDR rig where we've got two pumps with the moving system or without a moving system.

And then we've got pricing power on our high hookload tele-doubles we've got most of those rigs running, we have got couple left, but you know the dayrates on them are up sequentially kind of on a spot market basis those are up CAD 3,000 or CAD 4,000 a day from where we were say this time last year, so I think it's kind of across the board.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Is it safe to say though the capital you're investing to upgrade rigs this year you view as being a higher return to move those rigs into the highest class of – or probably as highest category versus just retaining them within a lower spec and taking the pricing power in the market?

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

A

We look at it both ways Jeff. We look at it from a client wanting us to go all the way the ultra spec and what that incremental dayrates needs to be, or leaving them in kind of high-spec territory and what that looks like, what the capital looks like and what the incremental dayrate looks like. We also look at our client list and you look at where, who holds what land and what they are going to need for rig specs and ultimately where that capital makes sense to spend. So, we look at it both ways, we just don't go, take the easy path and say let's make them all ultra-high spec and spend that money. We look at it by customer, by play and then capital specific on what they're asking us to do versus what they're willing to pay for.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Okay two last questions, first on the JV. Do you expect to have any rigs running in the first quarter within the JV?

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

A

Yeah we'll have, we expect that we'll have the rig running in Bahrain.

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

So there is one still operating in Saudi right now.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Okay and you made a comment earlier that there is potential for a Mexican rig to be running in the near-term?

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

A

Yes.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Okay. So when we think about Q1 it would be a rig in Saudi and a rig in Mexico?

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

A

Yeah, and the rig in Mexico it just depends on the timing of the contract.

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

And then it may not be for the full quarter depending on when the Saudi rig moves to the U.S.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Okay. Last thing just around CapEx, so your guidance coming into the quarter for 2017 was CAD 175 million capital program. Your spending came in CAD 25 million higher than that. Can you walk us through the delta tied to that and also why your 2018 capital program didn't come down with the acceleration of spend in 2017?

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

A

Well, 2017 essentially we talked about in the press release, basically it was maintenance capital that hit us, we had some stuff that hit us in the JV around some camp purchases we had to buy. But essentially it's a mix of resets, pipes stuff that we had to buy related to client programs and we knew some of that was there, we ended up having enhanced some of that because of the types of wells the clients are asking us to drill. So it really was specific to what we were doing in 2017 and what our clients were asking us to do in terms of the contracts and the types of wells they were asking us to drill.

2018 capital we were very conservative when we opened with our maintenance capital numbers and now it's really just the incremental rigs so, in 2017 it doesn't really impact what we are necessarily doing in 2018. It was really more with what came at us with clients in 2017 that impacted that number.

Jeff Fetterly
Analyst, Peters & Co. Ltd.

Q

Thanks for the comments.

Lesley Bolster
Chief Financial Officer, Trinidad Drilling Ltd.

A

Thanks Jeff.

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

A

You're welcome. Thanks.

Operator: [Operator Instructions] There are no further questions at this time. I turn the call back over to the presenters.

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

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

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