FINAL TRANSCRIPT

Enerplus Corporation

Q1 2022 Results Conference Call

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CORPORATE PARTICIPANTS

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CONFERENCE CALL PARTICIPANTS

Patrick O'Rourke
ATB Capital Markets — Analyst

Eric Nuttall
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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Enerplus Q1 2022 Results Conference Call. At this time, all lines are in a listen-only mode.

Following the presentation, we will conduct a question-and-answer session.

If at any time during this call you require assistance, please press *, 0 for the Operator.

This call is being recorded on May 6, 2022.

I would now like to turn this conference over to Mr. Drew Mair, Manager of Investor Relations. Please go ahead.

Drew Mair — Manager, Investor Relations, Enerplus Corporation

Thank you, Operator, and good morning everyone. Thank you for joining the call.

Before we get started, please take note of the advisories located at the end of our first quarter news release.

Our financials have been prepared in accordance with US GAAP. Our production volumes are recorded on a net after deduction of royalty basis. And our financial figures are in US dollars unless otherwise specified.

I'm here this morning with Ian Dundas, our President and Chief Executive Officer; Wade Hutchings, Senior VP and Chief Operating Officer; Jodi Jenson Labrie, Senior VP and Chief Financial Officer; Shaina Morihira, VP, Finance; and Garth Doll, VP, Marketing. Following our discussion, we will open up the call for questions.

With that, I will turn it over to Ian.

Ian Dundas — President and Chief Executive Officer, Enerplus Corporation

Thank you, Drew. Good morning and thank you for joining us today.

I'll start with the key takeaways from our first quarter release.

We remain well positioned relative to our 2022 plan to deliver robust free cash flow growth and meaningful cash returns to shareholders.

We expect to generate approximately $675 million in annual free cash flow in 2022, assuming rest-of-year prices of $85 West Texas and $5 NYMEX.

Based on current strip prices, our free cash flow estimate increases to approximately $900 million.

Consistent with our multiyear track record, we plan to allocate a substantial portion of free cash flow to shareholder returns. We have committed to returning a minimum of $350 million or 50 percent of annual 2022 free cash flow, whichever is greater, through dividends and share repurchases.

In connection with this plan, our board has approved a 30 percent increase to our quarterly dividend, effective with the June payment, and an increase to our share repurchase program. Based on current market conditions, we expect to repurchase the remaining authorization under our normal course issuer bid by the end of July and renew the NCIB in August for another 10 percent of shares outstanding.

Our framework for share repurchases continues to be based on our evaluation of the Company's intrinsic value, using our mid-cycle price view compared to our trading value. Using this approach, we continue to see compelling value in our business, which we believe is not being reflected in the market value of our equity.

The remaining 50 percent of our 2022 free cash flow not allocated to shareholder returns will be prioritized for reinforcing the balance sheet, which has consistently been a highly strategic asset for the Company.

Moving on to operations. The execution of our capital program remains on track. Strong operating performance and continued optimization of our program is supporting a higher production forecast compared to our initial guidance. As a result, we have increased our annual guidance by 500 BOE per day at the midpoint.

On the capital cost side, we are seeing upward pressure driven by the inflationary environment, as well as higher levels of non-operated activity. Due to these factors, we have revised our 2022 capital spending forecast higher by $20 million or 5 percent, again, based on midpoint guidance.

Importantly, we have secured the services, equipment, and supplies we need to execute our operating plan efficiently, with no plans to increase activity levels or chase higher, less efficient growth. We are committed to maintaining capital discipline and will continue to focus on cost control and strong execution to help mitigate and offset inflation where we can. Of course, higher oil and natural gas prices are also driving much higher earnings and free cash flow.

I will leave it there and now turn the call to Wade for an operational update.

Wade Hutchings — Senior Vice President and Chief Operating Officer, Enerplus Corporation

Thanks, Ian, and good morning, everyone.

I'll start with a review of our operating results and then provide some visibility to the outlook for the rest of the year.

In the first quarter, total production was just over 92,000 barrels of oil equivalent per day. As is typical for Enerplus, the first quarter production was lower compared to the fourth quarter of 2021 due to the timing of our completions program in North Dakota.

We brought our last 2021 pad online in early November, and our first pad this year started producing at the end of March. So we went over a quarter without bringing any wells online.

As Ian mentioned, operationally, the year has started out strong and on plan, despite the fact that we faced some additional challenges in the form of severe weather in North Dakota. Although we consider winter impacts in our base plan, these recent snowstorms were well above the scale and impact we planned for. On balance, we estimate that we lost about 1,000 BOE per day of annual average production due to recent storms.

Today, the vast majority of our production has been restored, and we expect to be producing at full capacity over the next couple of weeks.

Despite these temporary weather-related impacts, our strong operating performance and optimized development plan has more than offset the production downtime from the storms. As a result, we are tracking ahead of our original production forecast and have increased our annual guidance range to 96,000 to 101,000 BOE per day.

We are currently running two drilling rigs and have an active completions program ongoing until our onstream program finishes in the fourth quarter.

The second quarter will likely be our busiest in terms of wells brought on production, where we expect to bring online 18 to 21 net operated wells. Given the weather impacts in April, second quarter volumes are expected to be roughly flat to Q1, and then we expect strong growth into Q3.

Like our competitors, we are also seeing upward cost pressure due to the impacts of inflation and supply chain tightness. Frankly, we've been struck by the differences in messaging about inflation this earnings season between service companies and E&Ps.

We believe we are very well positioned to mitigate many of the impacts of inflation on our 2022 program through our early approach to contracting last year, strategic partnerships, and the technology-driven efficiency gains we continue to experience.

Nevertheless, we have experienced some inflationary pressures, largely in consumables, which is impacting our drilling and completion costs in the Bakken. We now expect our Bakken well costs to average $6.5 million per well, up from our previous estimate of $6 million.

The components most exposed to inflation are diesel and steel, which, combined, represent over 80 percent of the expected well costs to increase. Diesel costs will continue to be a function of the oil price environment as the year progresses, and we now have more certainty on steel costs in 2022, having recently secured the remaining casing requirements for the program.

The strong commodity price environment has also led to higher levels of non-operated activity in our portfolio, which is another reason we moved capital spending guidance higher.

In summary, we are committed to maintaining capital discipline. And because of our strong execution, we've been able to increase our production guidance despite the impacts of one of the worst April weather events we've seen in our North Dakota operations.

Touching briefly on activity in our non-operated Marcellus position, we participated in 25 wells, which were brought on production during the quarter with an average working interest of 6 percent. Well performance continues to be solid with initial 30-day production rates of approximately 30 million cubic feet per day per well.

I'll leave it there, and now I'll pass the call to Jodi.

Jodi Jenson Labrie — Senior Vice-President and Chief Financial Officer, Enerplus Corporation

Thanks, Wade.

I'll start with our pricing realizations. In the Bakken, our realized first quarter oil price differential was $0.35 per barrel below WTI. This is an improvement of almost $3 compared to the first quarter last year.

The continued strength in Bakken oil prices is being driven by an improving supply-and-demand balance, significant excess pipeline capacity in the region, and strong prices for crude oil delivered to the US Gulf Coast.

Currently, we are seeing Bakken oil prices trading above WTI, and as a result, we now expect our 2022 realized Bakken oil prices to be at par with WTI.

Marcellus pricing was also strong during the first quarter, reflecting seasonal demand, including our exposure to the Transco Zone 6 non-New York market, which averaged $1.42 per Mcf above NYMEX during the quarter. And as a result, our first quarter Marcellus differential was $0.01 per Mcf above NYMEX.

We expect Marcellus differentials to widen for the remainder of 2022 due to the seasonal impact on natural gas prices in the region and have, therefore, left our full year 2022 guidance of $0.75 per Mcf below NYMEX unchanged.

Operating costs were just above $10 per BOE in the first quarter. As noted during our last earnings call, operating expenses in 2022 are expected to be higher than 2021, due to the increased oil weighting of our production, inflationary impacts, and higher well service activity.

With some additional costs incurred recently in response to restoring operations following the winter storm, we’ve moved the bottom end of our operating expense guidance range up 3 percent, and it now is sitting at $9.75 to $10.50 per BOE.

Although we are seeing inflationary cost pressures, our margins remain solid. Before hedges, our first quarter netback more than doubled compared to the same period in 2021, significantly outpacing the move in commodities.

Moving down to the bottom line, our first quarter adjusted net income was $146 million, and adjusted funds flow was $262 million.

With capital spending of $99 million in the quarter, we generated free cash flow of $163 million. We will continue to prioritize returning capital to shareholders and strategically reinforcing the balance sheet with our free cash flow.

As Ian covered earlier, the board approved an increase to our return-of-capital plan for 2022, which is a minimum of $350 million or 50 percent of free cash flow, whichever is greater. And so our intention is to return this capital through dividends and share repurchases.

Lastly, as a result of the higher commodity price environment for both oil and natural gas, we are updating our 2022 current tax guidance to $20 million to $30 million or 2 percent to 3 percent of adjusted funds flow before tax from $10 million previously.

I'll leave it there, and we'll turn the call over to the Operator and open it up for questions.

Q&A

Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. Should you have a question, please press *, followed by 1 on your touch-tone phone. You will hear a three-tone prompt acknowledging your request and your questions will be polled in the order they are received. Should you wish to decline from the polling process, please press *, followed by 2. And if you are using a speakerphone, please lift your handset before pressing any keys. One moment for your first question.

Your first question comes from with Patrick O'Rourke with ATB Capital Markets. Please go ahead.

Patrick O'Rourke — ATB Capital Markets

Oh. Hey, guys. Good morning and thank you for taking my question.

Just curious here. You've obviously made an adjustment to account for inflation in 2022. You've got the number out there, $400 million to $450 million in the long-term plan beyond that. Just wondering what sort of your outlook or what sort of considerations you're taking into account on the inflationary side. And what you can offset by way of efficiencies sort of as we get out into the 2023 and then beyond that, medium and longer term with this five-year plan you have in place.

Ian Dundas

Morning, Pat. Maybe I'll just make a high-level comment and then hand it over to Wade.

I guess you've got two drivers there. You've got controllables and uncontrollables. On the controllable side, we've got procurement strategy and we've got execution.

And so we got in front of 2022 quite early through procurement. That allowed us to secure quality equipment or quality service providers, maintain operational continuity, and we continue to execute really well. So I think we're doing all we can on that front, and it's showing up in our numbers this year. We don't like talking about weather very much, but it was quite the impressive weather event, and we haven't missed a stride.

As we think into the future, you do have broad inflationary impacts that we won't be able to mitigate entirely. And those are going to be a function of the market, and oil price and gas price is going to be a big piece of that.

So, as we think about a multiyear outlook, it's probably not—I guess we wouldn't have the confidence to make a long-term inflationary call. I think it's hard. I think if we stay, if we settled into a $70 or an $80 world, it would be very different than if we stay in a $100 world.

But I can tell you, the scope of our program, our balance sheet, our track record, our relationship with service providers, I think are all going to put us in pretty good stead to help perform on a relative basis.

Wade? Is there any more detail you'd offer Pat?

Wade Hutchings

Yeah. Sure. Happy to. Good morning, Patrick. Thanks for the question. Maybe I'll start off on the execution front and give a few more thoughts.

Today, we have two rigs in the field, and one frack crew, and we've actually been working with these group of contractors now for well over a year. And the level of efficiencies that we're achieving with these crews and this equipment is really on just a steady well-by-well improvement pace.

So if you just ignore the inflationary impacts and just look at execution from an efficiency perspective, we're pleased with where we're at. We're actually really starting to hit our stride this year. And so, I'm fairly confident we're going to keep that multiyear track record that we've demonstrated of well-by-well, year-by-year improvements in pace, which ultimately does translate into lower costs on an inflation normalized basis. So that's going really well.

Without going into every detail of what we're working on, one of the things we're very focused on is offsetting some of these consumables that, to Ian's point, are really sometimes out of our control. So, for instance, looking for ways to offset diesel use in a lot of our operations to drive that part of the cost inflation a bit lower in terms of total impact.

Maybe a comment just to build on what Ian noted around procurement. The same types of things we did last year to proactively secure services equipment and supplies for the 2022 program, we're now in the middle of doing again for next year's program. And so I think that will serve us well again.

We clearly are benefitted today by that work. Even though, as we've noted, we've saw upward pressure on some of these consumables, a lot of other parts of our cost structure have remained fairly tight to what we were able to secure last year.

Ian Dundas

Wade, I think people might be a bit interested. Maybe you could expand a little bit upon diesel and how we're thinking about that. I mean this is a really good example of where our ESG goals are intersecting with improved profitability, thinking specifically about the drilling rig and fuel.

Wade Hutchings

Yeah. Happy to.

So, one of the fairly significant technology trends that's going on in the industry today is the types and nature of engines being used on both drilling rigs and pressure pumping crews.

So, I'll actually start on the frack side. We're using a set of engines that allows us to use some degree of CNG in place of diesel. And so today, we're probably in the 30 percent range where we're replacing diesel. But that clearly is saving us money today, given the spread between CNG prices and diesel prices.

The bigger shift we're about to make is this conversion of engines on our drilling rig where we're moving to dual fuel engines and even a fairly leading-edge environmental package that allows better power management of the engines on the rig. And so, in addition to being able to displace we're thinking upwards of half or more of the diesel used on a rig, we'll also be able to optimize the engines. There's some environmental package comes with a set of batteries that helps you better balance the load between the engines.

And so all of those things, to Ian’s point, help us reduce emissions through reduced diesel use. But they also, of course, drive down our costs given the spread today.

And then one last point I’ll make is, in the longer cycle, this will help us around emissions because we’ll be able to actually capture some of the gas that we can’t send down a pipeline, compress it, and then use it again in our operation.

So it’s an exciting area for us to continue to push on and expect more updates from us in the future.

Patrick O’Rourke

So I guess the broad takeaway then is that you’re very comfortable still with that 400-to-450 level in the five-year plan?

Ian Dundas

No. That wouldn’t be the point we’re trying to make.

I think the two takeaways. I think we are going to perform well relative to others. And then I think the biggest call you’ve got to make is tell us where the commodity is. I think you have to tell us where the commodity is. And in a $100 oil world, I don’t think our 400 to 450 is—the 450 is probably not a good number; I think we would exceed the outside of that. How much past 450 are we going to be at? I’m not sure. And I think $100 looks a lot different than $75 or $80 as well. That 400 to 450 was based on a $70 deck, and I think that’s probably a good number to think about in that context.

Patrick O’Rourke

Okay. That’s fair. I would assume the cash flow outpaces that inflation anyways.

Maybe just a quick philosophical question.

Ian Dundas

Absolutely.

Patrick O'Rourke

Maybe just a quick philosophical question in terms of capital structure and return to capital management. I know, Ian, from past experience, it seems like you love philosophical questions. So I'm wondering here, even looking at our numbers with where cash flow is going here, even with the 50/80 percent return of capital structure that you have, you're hurdling very close or very quickly towards being in a net positive cash position.

And I'm just wondering, we've seen a few companies recently come out, they've set long-term nominal debt targets that are above zero and been able to provide a line of sight to say return of capital philosophies that approach 100 percent. And I'm just wondering, from an Enerplus perspective, and appreciating that all asset bases are a little bit different, how do you think about that balance sheet management what the ultimate right level of leverage is? And where's the potential to even further accelerate the return of capital?

Ian Dundas

Well, the good news is, we put out this release this morning, and we had 15 minutes of having a 6-month outlook. So as we think past there, the principles that we're dealing with are all consistent: a resilient business, attractive total returns to people, combination of growth and cash in their pocket.

So in terms of ultimate debt, I guess you're questioning, would we take it to zero. We really haven't crossed that bridge yet. The outlook for this year will reduce debt and it will provide double-digit returns with the buyback and the dividend. But we're in a wonderful place relative to leverage. But we're still just under $600 million in net debt on the balance sheet. So we still will have debt at the end of the year.

And if you just step back, we think reducing debt in periods of high commodity prices de-risks the business and puts us in an advantaged position when we hit the next downturn.

So relative to building cash, that's not our objective. So I guess the outlet is we're going to continue to look to increase returns as that debt moves lower.

Patrick O'Rourke

Okay. Great. Thank you, guys.

Ian Dundas

Thanks, Pat.

Operator

Your next question comes from Eric Nuttall with Ninepoint Partners. Please go ahead.

Eric Nuttall — Ninepoint Partners

Morning, guys. I just want to follow on Pat's question on return of capital framework going forward. You guys are buying back stock. You bought back 10. You've told us that you're going to buy another 10. You held a great Investor Day to assuage some concerns that some people had on inventories. You clearly show that's not a problem. But there's still a massive disconnect between share price and intrinsic value.

So with the asset sale in the next couple of months, we've got you debt-free by end of Q1. Would it be reasonable to think that you clearly don't need to delever? You're debt-free by the end of Q1. So would you entertain maybe doing a special with the proceeds, given we've got you trading at 1.5 times cash flow, which is ridiculous?

Ian Dundas

Yeah. Good morning, Eric. I think that one and a half probably assumes the 100 stays flat. But no. We're certainly open-minded to that.

So on the divestment side, so assuming success, which you've done, we have said divestment proceeds go to returns and primarily to paying down debt and returns, maybe with a little bit of reallocation.

So then what's the outlet for that? It's either share buyback or it's dividend increase. And we think both of them make sense. We're leaning a little bit more into share buyback now because we agree with you. We see the disconnect in the valuation. But we think they're both outlets. So I think that's—your premise, yeah, I think it's valid, and that would be our plan.

Eric Nuttall

So you're constrained by the pace of the NCIB. So just going back to you again, would a special be on the table? Is that something you would consider?

Ian Dundas

Yeah. So far, we haven't been constrained by the NCIB. It's been a pretty valuable tool, actually. So I think if people are concerned that we will be constrained by our willingness to put cash out the door because of the structural nature of the NCIB, that concern is misplaced. We'll absolutely consider either special dividends or one-off buybacks.

Eric Nuttall

Okay. And then looking to next year, if we can dare to dream and current oil price persists, again, we've got you at a 40 percent-plus free cash flow yields. You're debt free.

So you've said you want to moderate, offer both growth and yield. But we've had other companies, like Cenovus, and they pledge 100. What do you think is reasonable going forward for expectation on investors' share for the free cash flow going forward? Is 75 percent reasonable in a debt-free state?

Ian Dundas

I think the—Eric, as you know, we've been very consistent with principles. We've been very consistent with our actions. I think we have a longer track record returning capital to shareholders than almost any other company out there. So we're very committed to this strategically.

We haven't been completely prescriptive in the formula for a few reasons. Things change. But I suppose that the second reason, when you look into the market, you see different approaches. You can't see any particular approach that is compellingly causing one company to outperform. And I think partly that's because things do evolve.

And so what's the right percentage? I think you need to tell me oil price, and then you need to tell me cost structures. And then we'll know what comes out of that because the thing that is more important than anything is that we have a sustainable resilient business.

So when people talk about 100 percent payout of free cash flow, I think about 2007 a little bit there. A hundred percent doesn't quite feel like the right number for a lot of companies. You need to replenish resource and those sorts of things.

Now we're in a wonderful place relative to the acquisitions that we executed a year ago. We've replenished the inventory. We have a very sustainable long-term business. But 100 percent? Hmm. Yeah. I don't know about that. And so for us, is 75 percent a good number, that feels pretty good. Again, tell me where cost structures are going to be. Tell me where commodities are going to be. And we want to ensure that this business sustains.

Eric Nuttall

Good. Okay. Thank you.

Operator

Ladies and gentlemen, as a reminder, if you do have any questions, please press *, 1.

There are no further questions at this time. Please proceed.

Ian Dundas

Well, thank you, everybody. I know it's a busy day, lots of reporting going on there. Appreciate everyone's attention this morning and enjoy your weekend. Thank you very much.

Operator

Ladies and gentlemen, this concludes your conference call for today. We thank you for participating and ask that you please disconnect your lines. Have a great day.