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Enerplus Corporation

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CORPORATE PARTICIPANTS

Drew Mair
Enerplus Corporation — Manager, Investor Relations

Ian Dundas
Enerplus Corporation — President & Chief Executive Officer

Wade Hutchings
Enerplus Corporation — Senior Vice-President & Chief Operating Officer

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

CONFERENCE CALL PARTICIPANTS

Greg Pardy
RBC Capital Markets — Analyst

Patrick O'Rourke
ATB Capital Markets — Analyst

Cody Kwong
Stifel — Analyst

PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Enerplus Q2 2021 Results Conference Call. At this time, all lines are in listen-only mode. Following the presentation, we will conduct a question-and-answer session. If at any time during this call you require immediate assistance, please press star zero for the operator. This call is being recorded on Friday, August 6, 2021.

I would now like to turn the conference over to Drew Mair. Please go ahead.

Drew Mair — Manager, Investor Relations, Enerplus Corporation

Thanks, 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 today's news release. Our financials have been prepared in accordance with US GAAP. All discussion of production volumes today are on a gross company working interest basis and all financial figures are in Canadian 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 & Chief Executive Officer, Enerplus Corporation

Thank you, Drew. Good morning, all.

Our second quarter results reflect the increased scale of our business following our acquisitions along with strong operational momentum. We achieved record quarterly production of over 115,000 BOE per day in the second quarter, 26% higher than the prior quarter. We expect another meaningful sequential increase to production in the third quarter, which will be the first quarter that fully reflects our two Bakken acquisitions, which closed in the first and second quarters of the year.

The second quarter was our most active period of the year in terms of drilling and completions activity and the execution of our capital plan remains on track. We moved the midpoint of our annual production guidance higher by 500 BOE per day following strong execution and outperformance year to date and we continue to operate within our capital spending guidance of $360 million to $400 million.

Our free cash flow profile is continuing to move higher, driven by the improved commodity prices since the start of the year, our increased production outlook, and our disciplined capital allocation. We now expect to generate over $450 million in free cash flow in 2021 based on forward strip commodity prices. For the remainder of this year, we will continue to prioritize directing the majority of this free cash flow for debt reduction. We have highlighted a $400 million debt reduction target, which aligns with our net debt to funds flow ratio target of 1x or less in a $50 WTI oil price environment. At current commodity prices, we anticipate achieving this target by mid next year.

With the step change in our cash flow generation driven by our significantly higher production base and the line of sight to hitting our long-term debt target, we elected to increase the dividend for the second time this year, consistent with our approach of sustainable dividend increases. Our board also approved a renewal of our normal course issuer bid. Under our framework, we expect to allocate approximately 90% of our free cash flow after dividends to debt reduction while we progress our deleveraging plan. With the remaining 10% we will continue to evaluate incremental shareholder returns, including through further potential dividend increases and share repurchases. Looking ahead, as we achieve our long-term debt target, we expect to be in a position to meaningfully increase our allocation of free cash flow to shareholder returns.

I will leave it there and turn the call over to Wade for his comments.

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

Thanks, Ian, and good morning, everyone.

Our operational performance this year continues to be solid. We completed and brought 23 wells on production in the Bakken in the second quarter and our completions efficiency is averaging approximately 13 stages per day, up from 9.5 last year. Our drilling performance has also been strong. We set a Company record in the second quarter drilling a two-mile lateral section in 48 hours. On the back of this performance, we updated our 2021 well cost estimates in the Bakken to a US$5.7 million compared to our previous estimate of US$6.1 million. This represents a significant reduction in our cost structure over the last couple of years. We're down 10% compared to last year and 25% compared to 2019.

As Ian noted, we achieved record quarterly production in the second quarter, which was driven by higher volumes in the Bakken following the closing of our acquisitions and our active completions program. Total Williston Basin production was over 72,000 BOE per day in the quarter, 53% higher than first quarter production. In the second quarter we completed our first pad of wells that were acquired in connection with the Bruin acquisition. This was an eight-well pad in Fort Berthold adjacent to our legacy acreage. The wells are tracking expectations with peak 30-day rates of approximately 1,900 BOE per day on average per well based on the six of the eight wells that have had more than 30 days online.

We anticipate the third quarter to be another record production quarter for Enerplus. We expect to see strong Bakken production growth following another quarter of active completion operations and the full production impact of the assets we acquired from Hess, which closed in mid Q2.

I'll now pass the call to Jodi.

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

Thanks, Wade.

Our second quarter adjusted funds flow was $184 million with capital spending of $130 million and resulting in free cash flow of $54 million. Our realized Bakken oil price differential averaged US$2.76 per barrel below WTI in the second quarter. Refining demand was strong and there continues to be significant available pipeline capacity in the basin, supporting pricing.

Effective August 1st, we have increased our committed capacity to deliver crude oil from North Dakota to US Gulf Coast via the Dakota Access Pipeline as part of its broader system expansion. The

pipeline's capacity was recently expanded from 570,000 barrels per day to 750,000 barrels per day based on comments from the pipeline operator. Enerplus now has approximately 10,000 barrels per day of firm transportation on DAPL. Based on our year-to-date realizations in the Bakken and improved outlook for differentials given DAPL's expansion, we've narrowed our annual differential guidance to US$2.35 per barrel below WTI from US$3.25 per barrel previously.

Turning to the Marcellus, our realized Marcellus natural gas price differential was US$0.89 per Mcf below NYMEX in the quarter, significantly weaker than the prior quarter due to a combination of normal seasonality we see in the US northeast markets and unplanned regional pipeline maintenance. As a result, we have widened our annual Marcellus natural gas price differential guidance to US$0.65 per Mcf below NYMEX from US$0.55 per Mcf previously. We expect differentials to remain relatively weak in the third quarter and then strengthen through the fourth quarter as regional demand increases heading into winter.

We recorded a current tax expense of $ 4.2 million in the second quarter, primarily consisting of US federal tax, as a result of higher income expected in the US in 2021. For the full year, we expect income tax expense of between US$5 million and US$7 million.

Turning to our free cash flow outlook, we expect free cash flow generation to materially increase in the second half of the year. On a full-year basis, we estimate that we will generate over $450 million based on current commodity prices. With $117 million in free cash flow generated during the first half of 2021, that points to over $330 million in the second half of the year.

Priority number one for this free cash flow is the balance sheet, as we work toward reducing our current net debt at June 30th by $400 million. Although we are prioritizing debt reduction, we remain in a strong financial position today, and this gives us the flexibility to enhance our return of capital to shareholders in the near term.

We announced a 15% dividend increase today and we also announced that we would allocate 10% of our free cash flow after dividends to incremental shareholder return opportunities while we are progressing on our deleveraging plans. This could come in the form of additional dividend increases and/or share repurchases and, as Ian mentioned, our board has approved the renewal of our normal course issuer bid for up to 10% of our outstanding shares.

Finally, as an update to the five-year plan that we introduced in April, we have updated 2021 to reflect the year-to-date commodity prices and forward strip for the balance of this year. The remaining years, 2022 to 2025, continue to be based on a flat $50 to $55 WTI oil price. With this update, our cumulative free cash flow estimate over the five-year period increased to $1.5 billion to $2 billion.

I will 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 star followed by one on your touchtone 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 star followed by two. If you are using a speakerphone, please lift the handset before pressing any keys. One moment for your first question.

Your first question comes from Greg Pardy from RBC Capital Markets. Greg, please go ahead.

Greg Pardy — Analyst, RBC Capital Markets

Thanks. Good morning. Maybe just the first question might be for Wade, and from everything you're saying in terms of the reduction in D&C costs, it really sounds like it's just increased efficiency, like less time. But I'm wondering if you've made any changes to either the well construction or how you're completing these wells. Just curious there.

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

Sure. Happy to address that. The wells that we drilled and completed in the first and second quarters of this year really follow the design that we've had for the last several years, so there's no material change there.

When we look at the rate of change from last year that kind of dropped from 6.3 to where we're projecting this year to be at 5.7, we're seeing about half of that on the drilling side and half on the completion side. Most of that is from just improved efficiencies on multiple stages, multiple aspects of drilling and completions. I would note that there is an important part of that on the drilling side that's come from essentially a new contract with the existing super-spec rig that we've been using for the last several years, and so we're benefitting from kind of the change in the market rates for that as of earlier

in this year relative to several years ago when we signed that up. So we're certainly pleased. We've actually saw improvements in our completion efficiency and drilling efficiency at a faster pace than we were even anticipating.

Greg Pardy — Analyst, RBC Capital Markets

Okay. Terrific. Thanks for that. And then maybe just shifting to the cash taxes, I'm wondering if there's a rule of thumb we can use maybe. This is more about 2022, Jodi, but I'm wondering is there like a percent of pre-tax we should think about in terms of cash tax next year?

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

Yeah, I think maybe if you just want a rule of thumb you could think of, call it, 1% of net operating income in the US. That would be in the ballpark.

Greg Pardy — Analyst, RBC Capital Markets

Okay. Okay, great. And last question for me is kind of, Ian, I mean strategically, other things being equal, would you prefer to consolidate further in the Bakken or is the Company maybe approaching a size where you're thinking more about basin diversity? And I'm thinking oil and liquids basin diversity more so than the Marcellus

Ian Dundas — President & Chief Executive Officer, Enerplus Corporation

Good morning, Greg. Well, with your set up, everything being equal, more Bakken, I think, clearly fits the bill. We've got an established footprint. We see value and scale. We think the setup in the

Bakken is really pretty encouraging. Costs are under control, differentials are tightening, and so, yeah, that would clearly be the focus areas today.

Greg Pardy — Analyst, RBC Capital Markets

Okay. Terrific. Thanks very much.

Ian Dundas — President & Chief Executive Officer, Enerplus Corporation

Thanks, Greg.

Operator

Your next question comes from Patrick O'Rourke from ATB Capital. Patrick, please go ahead.

Patrick O'Rourke — Analyst, ATB Capital Markets

Good morning, guys. Just wondering, now that you've had your hands on the steering wheel for, you know, call it a quarter here with the new assets, I'm wondering if you can give us your view on kind of where the Bakken base decline is sitting. Obviously, it seems like you have some comfort with it in order to increase the lower end of the production guide for the year. And then wondering, with where the well costs are now, it appears that you're offsetting any sort of inflationary pressures with efficiencies, as you mentioned with the last question here, where you would see the maintenance capital level at a corporate level right now.

Ian Dundas — President & Chief Executive Officer, Enerplus Corporation

Good morning, Patrick. So, to decline, it's consistent with what we had forecast, corporately low 30s. And I guess that was part and parcel of bringing up bottom in the guidance. There's a lot of things that moved there though, obviously, relative to the timing of on streams and then downtime and everything else.

Maintenance capital, you know, we don't have a firm number out there, but we pointed to, I think, $500 million next year sets up 3% to 5% growth sort of start back off that growth and around $400 million. I think it's a good round number to think about.

And just (inaudible) comment, our ability to offset inflationary costs, I think we're actually doing a very good job on it. There is a bit of pressure in the market, and you're hearing other producers talk about it as well, Steel and like, and so if you really got under the hood and you looked really closely at year-to-date well performance, we'd be a bit ahead of that number that we're putting out there. So, we have built in, we've anticipated some modestly higher costs over the course of the year, and then that gets you to that 5.7. And the big picture here is we continue to do a really good job growing efficiencies and we're sort of eating into and in fact, year to date, more than eating into any inflationary pressures we're seeing.

Patrick O'Rourke — Analyst, ATB Capital Markets

Okay, great. And then, Ian, you're always very thoughtful on your approach to the commodities, so I'd like to hear your view on this. You're using a bandwidth of $50 to $55 right now for your kind of

five-year plan and just wondering what you would have to see in the market out there to shift that to something a little bit higher and incorporate that in your business planning and the way you're allocating capital.

Ian Dundas — President & Chief Executive Officer, Enerplus Corporation

Yeah, I don't get called thoughtful very often, so thanks. It's a good way to start the day. I think there are a few things here. Absolutely inherent in all of this is thinking our way through sustainability and thinking about volatility. So we're just not that smart and there are a lot of things that are up there that can move those prices around a little bit, so we're using what we think are mid-cycle prices to guide our business. And as we think about higher price environments, we will take advantage of some of that through hedging strategies and the like.

So, if we had a strong, strong view of a higher market, would that influence activity behaviours? I don't know that it would, honestly. Some of the things we do, you know, we might have a very strong view on the market and if the (inaudible) market is not there to be able to mitigate some of that, then that would mute any activities we have. As you think about things like as we realize, like right now we're realizing higher prices, meaningfully higher prices than that, but a forecast is not money in the bank and so we are very cognizant of actual results versus forecast.

So I don't think there's anything sort of fundamentally out there that we would do dramatically different and, in fact, in the strong price, like you can easily create a stronger price forecast than $50 to $55. I think it's very plausible. I think it's actually potentially likely. With that probably comes higher inflationary assumptions than we're baking in now. So we'll be balanced on this. Our goal is to be able to

make money in all cycles and that means conservative balance sheet management, focusing on returns, using risk management tools to take price risk out of the equation as we're spending dollars, and so that's what sort of guided us for years and is going to continue to guide us in the future. But I think the oil setup feels pretty good right now and if you told me we were averaging about $55, I wouldn't bet against that over the next couple of years. I guess we'll see.

Patrick O'Rourke — Analyst, ATB Capital Markets

Okay. Thank you.

Ian Dundas — President & Chief Executive Officer, Enerplus Corporation

Thanks, Pat.

Operator

Your next question comes from Cody Kwong from Stifel. Cody, please go ahead.

Cody Kwong — Analyst, Stifel

Hi, guys. Thanks for taking my call. I've got a question probably for Ian. When you guys were talking about your free cash flow priority being 90% debt/10% return of capital until you get to your debt threshold that you want, how does that change once you meet that target? If you can maybe expand upon that, whether it's through just kind of in theory or if you had some actual numbers that you had in your mind.

Ian Dundas — President & Chief Executive Officer, Enerplus Corporation

Good morning, Cody. Thanks for that question. I think we'll stay away from numbers here. The concepts that we've laid out, 90% to debt, once we're through that level, which could be within a year possibly, the signal that we've sent is we see higher returns to shareholders. We haven't put a pin in what exactly that looks like, in part because I think you want to look at the environment you're in at the moment and how competing priorities exist, but we do think we've got a really attractive plan that grows the Company and puts us in a great position to de-lever and to continue to provide capital to shareholders.

The tools that we've highlighted, things that we think are important, a growing rock-solid sustainable base dividend we think is something that will be really attractive to shareholders, which means it needs to sustain price volatility as well. So we're on the path to continuing to move that forward. We also think share buyback plays a role and we think it particularly plays a role when you look at the valuations of our Company. We see significant intrinsic value that we plan on unlocking and the share buyback, I think, plays a nice role in that. It also helps support the sustainability of the base dividend and keeps your capital structure strong.

So I guess those are the principles that are guiding us. There are others out there who have a variable dividends and specials and those things and, yeah, we'll remain attuned to the market and those such things, but right now think sustainable growing base dividend, I think share buybacks, particularly when we see the valuation that we're seeing right now, and then think, once we've hit our

debt targets, more coming for shareholders. And then we'll work to provide more visibility as we get closer to that as to what more looks like.

Cody Kwong — Analyst, Stifel

Okay. Thank you very much.

Ian Dundas — President & Chief Executive Officer, Enerplus Corporation

Thank you.

Operator

Ladies and gentlemen, as a reminder, should you have a question, please press star one.

Okay, there are no further questions at this time. I'll turn it back to Ian for closing remarks.

Ian Dundas — President & Chief Executive Officer, Enerplus Corporation

Well, thank you, everybody. Appreciate you dialling in today. Enjoy the last little bit of summer. For those Canadians who are watching the gold medal soccer match with Sweden, I won't say anything about it. Anyway, enjoy the rest of your day. 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.