Subsea 7 S.A.

Quarter 1 2016 Results Transcript

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Speakers:
Jean Cahuzac - Chief Executive Officer
Ricardo Rosa - Chief Financial Officer
John Evans - Chief Operating Officer

Isabel Green - Investor Relations Director

Good afternoon, everyone. With me on the call today are Jean Cahuzac, our Chief Executive Officer; Ricardo Rosa, our Chief Financial Officer; and John Evans, our Chief Operating Officer. The results press release is available to download on our website, along with the presentation slides that we'll be referring to on today's call.

Please take note of our forward-looking statements disclosure, on slide 2. Similar wording is also included in our press release.

I'll now turn the call over to Jean.

Jean Cahuzac – Chief Executive Officer

Thank you. Good afternoon, and welcome to our first-quarter results conference call. I will begin with a summary of our performance during the quarter, before handing over to Ricardo, who will cover our financial results in more detail. I will conclude with our view on the market, and the outlook for our business in the year ahead, before inviting your questions.

Turning first to the highlights on slide 4, revenue was $746 million in the quarter, down 37%, reflecting lower levels of activity with fewer SURF projects being executed offshore compared to last year.

Adjusted EBITDA, at $284 million, resulted in a margin of 38%. We have continued to benefit from projects in the final stages of its completion, where good execution and lower costs have resulted in higher profit recognition. Our performance also reflects the successful implementation of our 2015 cost reduction and resizing program.

We have maintained a strong financial and liquidity position, as reflected in the increase in our net cash position, which is now at $633 million.

Our robust balance sheet is valued by our clients, as it gives them confidence that we will deliver our commitments to them.

We achieved 71% active vessel utilization in the first three months of the year, slightly better than the total vessel utilization reported for the first quarter last year. Seven vessels were stacked as at the end of March. If we include these, total vessel utilization was 55%.

The measures we have taken to reduce costs and improve efficiency have kept us competitive in a very challenging environment. We booked $1.1 billion of order intake, increasing our backlog at the end of March to $6.5 billion. Awards included the West Nile Delta Phase 2 project, which consolidated our growing presence in Egypt; and also, two Life-of-Field contracts in the UK.

The challenging industry conditions have not changed since we spoke to you in March. The timing of new awards to market is still uncertain as clients continue to limit investments in major new self-developments, due to the oil price environment.

In these difficult times, we are focused on winning work, reducing cost, and also maintaining an acceptable risk profile. Externally, we are working with our clients to identify solutions which allow us to lower the cost of their field development projects and make more projects viable. Internally, we are addressing our own cost base, resizing our capacity to enable us to offer more competitive pricing at this point.

I turn now to slide 5, to look at our operational performance in more detail.

Starting with the Northern Hemisphere and Life of Field business unit, we made significant progress on several projects in the US Gulf of Mexico. The Dalmatian project was substantially completed, and offshore work is ongoing on the Holstein Deep and Coulomb Phase II projects.

In the North Sea, offshore activity levels and vessel utilization were low, reflecting the decline in activity resulting from the low oil price, as well as seasonal weather conditions. We are addressing this by forming new ways of working and collaborating with our clients and partners to lower the overall cost of field development.

Onshore, our bundle fabrication facility in Wick remained busy; and we progressed with engineering and project management on SURF projects, ahead of offshore operations planned for the second and third quarters.

In the southern hemisphere and global projects business unit, good execution resulted in cost reduction and de-risking of several projects, including Ofon 2 offshore Nigeria, which was substantially completed in the first quarter.

We have made significant progress on various projects, including the TEN project offshore Ghana, and the Persephone project offshore Australia. Our projects offshore Egypt are going well, with project management, engineering, and fabrication progressing on West Nile Delta Phase 1; and completion of pipelay operation by *Seven Borealis* on East Nile Delta.

Offshore Brazil, we completed the BC-10 project; and our newest PLSV, *Seven Rio,* started her long-term day-rate contract, as planned. We achieved high levels of vessel utilization for all our PLSVs working offshore Brazil.

We are not yet in a positon to provide an update on the broking risk to some of our older vessels by Brazilian flags unit. What I can say is that we are having constructive discussions with Petrobras, but it will take some time before negotiations are completed.

Moving on to side 6, to look at our backlog. We ended the first quarter with order backlog of $6.5 billion, an increase on the year-end position, with negligible impact from foreign exchange movements in the quarter.

Order intake of $1.1 billion gave a book to bill of 1.4 times. This is mostly due to the award of the West Nile Delta Phase 2 project offshore Egypt, which had a value of over $750 million. Also included was the extension to an existing Life of Field contract offshore UK.

I will talk more about the market and outlook later on, but first I will hand over to Ricardo to review our financial performance in more detail.

Ricardo Rosa - Chief Financial Officer

Thank you, Jean. And good afternoon, everyone. Let's first look at the income statement highlights, on slide 8. First-quarter revenue of $746 million was down 37% from the prior-year period, reflecting lower offshore activity levels in both business units with fewer projects in progress due to the industry downturn.

Adjusted EBITDA of $284 million and margin of 38% shows the benefits of our cost reduction program, as well as good execution and risk mitigation, and successful completion of large projects.

Net operating income of $194 million was 10% higher than the first quarter of 2015, both as a result of increased EBITDA and the lower depreciation charge, reflecting the impact of vessel and equipment impairments in the prior year.

Our seaway heavy lifting joint venture was the main contributor to the $16 million earned from joint ventures and associates in the period.

Income before taxes of $211 million was in line with the prior year, and included a net foreign exchange gain of $14 million from functional currency movement, which we reported within other gains and losses.

Our tax charge was $64 million, equivalent to an effective tax rate of 30.5%; and net income was $147 million, which gave rise to diluted earnings per share of $0.42.

Slide 9 shows the revenue and net operating income by business unit. In the northern hemisphere and Life-of-Field business unit, first-quarter revenue of $331 million was down 41% on the same quarter in the prior year, mostly due to significantly lower levels of activity in the North Sea.

Net operating income of $37 million was 23% lower year on year, but showed significant improvement on the $49 million operating loss incurred in the fourth quarter of 2015. The improvement resulted from higher revenue, a reduced cost base, and risk mitigation measures on certain projects.

In the Southern Hemisphere and Global Projects business unit, first-quarter revenue was $413 million, down 33% on the prior year, with fewer projects in their offshore phase compared to 2015. This revenue trend is expected to persist as we complete projects and our workload diminishes.

Net operating income in the southern hemisphere was $149 million, up 26% year on year, despite the lower revenue. Strong margin for the quarter was due to good execution across our portfolio and the relatively high mix of projects in the final stages of execution. These factors enabled us to save costs, mitigate risk, and successfully close out projects.

We do not expect to sustain the Hemisphere's margin at this level, because the mix of early stage to near-completed projects will change over time. Also, our pricing today is already factoring in our new lower cost base with the associated savings being shared with our clients, to help make projects viable in the low oil price environment.

Slide 10 summarizes our cash flows in the period. Net cash of $633 million at the end of March represented an improvement of $210 million on the position at the end of December 2015.

$281 million in net cash was generated from operating activities, in part due to a $29 million increase in net operating liabilities.Our improved working capital balance this quarter is contrary to our expectation for a part reversal of our working capital position and consequent cash outflow during the course of the full year.

Net cash used in investing activities, totalling $74 million, included capital expenditures of $82 million, mostly on our vessel new build program, which I will address in a moment.

We spent $72 million repurchasing $78 million face value of our 2017 convertible bonds in the quarter, leaving a balance outstanding of $470 million at par value.

Our financial and liquidity positions remain strong with $1.1 billion of cash and cash equivalents at the end of March, and a further $1.1 billion of undrawn facilities. In this regard, we have recently extended our revolving credit facility by $250 million to an aggregate $750 million, all on attractive terms.

We believe it is important to maintain a prudent strategy for capital management in view of our outstanding bond, maturing in late 2017, our capex commitments for the new-build program, and our forecasted working capital outflow as our project portfolio contracts.

Our strong balance sheet also allows us to take a long-term view of the business, and address appropriate strategic investment opportunities that may arise.

As shown on slide 11, our new-build program is in its final stages, with the remaining $275 million investment expected to be completed this year, following delivery of the four remaining vessels. Three of these vessels are due for delivery before the end of June, and the last vessel is targeted for the fourth quarter.

Slide 12 sets out our guidance. We continue to expect revenue in 2016 to be significantly below the level reported last year. However, following our strong first-quarter performance, we have raised our guidance for adjusted EBITDA percentage margin from significantly lower to lower than last year.

We have updated our effective tax rate guidance to between 30% and 32% for 2016, and have indicated that we expect our working capital outflow to range between $250 million and $350 million for the full year.

All other guidance remains unchanged.

Jean Cahuzac - Subsea 7 SA - CEO

Thank you, Ricardo. Let's turn now to slide 14.

We are delivering solutions for our clients, but are lowering the cost of development and enabling projects to progress at the lower oil price.

There is no silver bullet to lowering the cost of field development as each field is different, but there are many ways we can approach the challenge and successful solutions can often be applied across several projects.

Engaging early helps us to reduce project costs by proposing the right solution first time. When we are present from the start, together with our alliance partners, KBR and Granherne, we can identify the optimal field design. This early stage is also the best moment to consider how our technology portfolio can be applied, and whether an integrated solution could be more cost effective for the players.

But it's not just the large complex projects we can help with. In many cases, significant project management and engineering hours can be eliminated by agreeing to lighter levels of oversight, re-using prequalified solutions, and lowering the overall administrative burden.

Moving to slide 15, I would like to share with you some details on three projects that illustrate the changes we are driving to reduce costs.

Firstly, West Nile Delta Phase 1, a fast-track domestic gas project offshore Egypt. Our longstanding relationship with the client supported better ways to work together; it eliminated unnecessary administration and reduced man hours. In addition, numerous innovative engineering ideas were implemented. One example: one cost saving we identified was a change to the PLET protection cover design to reduce its weight and enable hourly access. I could list a number of other examples.

The second example is on a smaller project: Coelacanth in the US Gulf of Mexico. As one of our competitors was unable to deliver, this project was offered to us with a short execution window. It lasted only 10 weeks from award to completion. The key to the success of this project was our ability to optimize available resources at short notice and re-use solutions that were already qualified. We worked closely with our client, whose pragmatic approach helped the project to progress very quickly.

Thirdly, the Maria project offshore Norway. By engaging early, we were able to reduce over specification and apply appropriate operating standards. We took a more flexible and collaborative approach to working together with our client; and this enabled us to significantly reduce project management and engineering costs.

Turning to slide 16, we are actively adapting our business to the challenging industry conditions.

In 2015, we launched a cost reduction program and resizing program to reduce the capacity and cost of our fleet and workforce. This program was successfully completed in the first quarter of 2016, and, as I mentioned earlier, we are already seeing the financial benefits in our reported results.

The market outlook has not changed, with many projects pushed to the right, despite the progress we are making to lower the cost of the projects. As a result, we will be implementing additional cost reduction measures in 2016.

We remain focused on our long-term strategic objective, and our cost reduction measures reflect this.

We remain committed to our investment in technology and innovation. We have concentrated our attention on certain strategic technology programs where we see the greatest impact to future developments. We will continue to operate a modern, versatile, and high specification fleet, announced by the addition of our new build vessels.

We have continued with our reorganization by combining our Life of Field and i-Tech capabilities in to a single business, branded i-Tech Services. This strategic change will enable us to expand and strengthen services we provide to our clients over the full lifecycle of the field.

Slide 17 summarizes our view of the near-term outlook. Overall, the industry conditions remain challenging, and the timing of new awards to market is still uncertain.

In the Northern Hemisphere and Life of Field business units, the market-wide cost challenge in the North Sea remains. Improving weather conditions are expected to result in better utilization and activity levels over the second and third quarter.

There is potential opportunity for Life of Field services outside the North Sea as we look to increase our presence worldwide under our i-Tech Services brand.

In the southern hemisphere and global projects business units, there are still several project tenders being discussed with clients. This includes the Fortuna and Platina projects offshore West Africa; the Greater Enfield project offshore Australia; the Golfinho project offshore Mozambique; the Mad Dog 2 project in the US Gulf of Mexico; and the Atoll project offshore Egypt.

Our joint venture, SHL, remains well positioned to capture additional work in the renewables sector.

Finally, our alliance with OneSubsea continues to do well, and we are seeing an accelerated interest from clients. We currently have three FEED studies in hand, and are working on over 10 clear prospects where our alliance can participate. We believe it's only a matter of time before the first combined SPS and SURF package come to the market.

And now, John, Ricardo, and I will be pleased to answer your questions.

Q & A

Fiona Maclean - BofA Merrill Lynch - Analyst

I'd like to, first of all, get some clarification on the wording around the margin guidance for 2016. Is this purely as a result of what's happened in the first quarter, or do you have a different view on how margins are going to be evolving for the following three quarters?

And then, I'll come back to my second question, once I've received the answer to that one. Thank you.

Jean Cahuzac - Subsea 7 SA - CEO

The good results margin in first quarter, obviously, has an impact on the overall yearly results. We did see a lot of pressure from the markets with a very high competition on all the projects. Our costs have gone down, as I said before, which contribute to improving the results somewhat. But one should not underestimate that competition is tough, and there are fewer projects in front of us.

Fiona Maclean - BofA Merrill Lynch - Analyst

Okay, very clear. And then, secondly, when you look at the shape of your business today, and you mentioned you have this new segment that's going to be a little bit more specialist in its services, are you looking at all to utilize your balance sheet to do any M&A activity at this point in the cycle? Or is there still a valuation mismatch on some things you may be interested in?

Jean Cahuzac - Subsea 7 SA - CEO

First, a general comment on the Life of Field. We see a lot of interest from our customers for higher involvement at Subsea 7 on the operating side, the maintenance side of their field, so we see a potential to grow this activity on a worldwide basis.

Regarding potential acquisition, or M&A, we have a strong balance sheet. We will look at opportunity on a case-by-case basis and take at the time the right decision for the shareholders. But it's premature to say what will happen, or will not happen.

Mukhtar Garadaghi - Citi - Analyst

In terms of your pipeline, please, Jean, could you comment on the sizes of some of these opportunities, without being too specific? And, for example, Mad Dog, is SURF scope in its traditional sense, and Greater Enfield as well?

My second question is on SHL. Could you just quantify the opportunity there as well in terms of these offshore renewables projects? Basically, any colour on the outlook for that business.

And finally, in terms of your engagement with your clients, you're talking about high involvement in to Life of Field services. What's happening on the ground? Are we seeing elimination of some of these duplicated efforts on engineering, and such? And what are you seeing on your client side? Are these companies outsourcing more, or are we talking about in-housing some of the engineering services?

Jean Cahuzac - Subsea 7 SA - CEO

Thank you, Mukhtar. I am going to answer your question regarding SHL, and then I will pass you on to John for the two other questions.

Regarding SHL; SHL is a joint venture that we have with some financial partners. We've been quite successful over the last couple of years, both in renewables, but also oil and gas activities. We see some activity, middle size or larger projects, as a possible opportunity for SHL, so we will continue to pursue these opportunities and support SHL, as required.

John Evans - Subsea 7 SA - COO

With the workload we identify on slide 17, Mukhtar, there's a range of different projects here. Atoll, Platina, and Fortuna are what we call medium-sized SURF projects. Golfinho is a larger project in Mozambique; and Mad Dog 2 has gone through a lot of re-scoping and resizing by our clients, and is probably somewhere in between the two in terms of what that will be when it finally lands.

So there is a train of different tenders in the market at the moment with a different portfolio.

Coming back to your question about are the clients responding, I think the slide that we have in the pack, which Jean talked about, the three examples, I think each of those examples are about our clients adapting the way they would normally work, and working with us in a different way. We couldn't achieve what we have achieved on those particular projects if we didn't have those changes.

As Jean says, there is no silver bullet. Each client addresses this differently. On West Nile, we've done it one way; on Maria, we've done it a different way; and same with the Gulf of Mexico project which we did it a different way. But I think it's fair to say that we are seeing good responses to the questions and the opportunities being raised by working differently.

Andrew Dobbing - SEB Equities - Analyst

First question on revenues, which were maybe a little bit disappointing in Q1. I guess North Sea was pretty weak, and I'm just trying to get a sense of seasonality in that market as it might be a little bit different from normal. It looks like there was very little progress on North Sea projects, and I guess that's going to pick up a lot in Q2 and Q3.

Related to the revenue outlook, can you touch on progress in Egypt. Has offshore operations actually started on East Nile Delta? And relating to that, has there been any meaningful revenue contribution from the Egyptian projects in Q1 related to procurement, or anything like that?

Jean Cahuzac - Subsea 7 SA - CEO

I will let John answer on Egypt, and then I will take the questions on revenue and the North Sea.

John Evans - Subsea 7 SA - COO

In Egypt, as we mention in Jean's talk, we executed the pipelay on East Nile Delta in quarter 1, so *Seven Borealis* did that. We have further construction work going on in quarter 2.

On the West Nile Delta Phase 1, we're a shade under 20% complete, and we've done engineering procurement and we have a lot of heavy duty fabrication ongoing in the country at the moment; and the main offshore will kick off in quarter 3 and quarter 4 for that project.

Jean Cahuzac - Subsea 7 SA - CEO

Regarding your question on North Sea and, speaking of revenue, what we are seeing in the North Sea, the seasonal effect that we see every year due to weather on activity. But there is also an impact from a lower level of activity, due to the oil price. So one cannot say it's only the seasonal effect. We see more activity in Q2, Q3, but there is still impact from the lower market condition.

Regarding the revenue for 2016, you have the numbers in front of you regarding the backlog to be executed in 2016, which is a high percentage of what I see as a consensus for 2016. It's premature for 2017.

Andrew Dobbing - SEB Equities - Analyst

If I could have one more question on procurement, trying to understand the moving parts a little bit. It's been falling dramatically, I think it was about $2.8 billion in 2014; it fell to $1.6 billion in 2015. Even as a percentage of sales, it's been falling dramatically, I think from 45% of sales in 2013 to 34% of sales in 2015.

You have guided I think in the last conference call that procurement would fall again in 2016. Can you just talk a little bit about how we should be thinking about the moving parts? Is it just deflation that's driving that, or are there other important things we should be thinking about?

John Evans - Subsea 7 SA - COO

I think it's just a change in the portfolio of the work we've got. We have a strong PLSV business in Brazil, which is a steady-state business there with some additional tonnage coming in this year.

A lot of our Life of Field work is day-rate type work, where there's very little procurement in it. And as you can see on the major projects listing, the big projects are coming off the boil, although we have some new projects there in Egypt which will contribute the standard-type procurement model. So what you've said is what we expect to see.

Andrew Dobbing - SEB Equities - Analyst

Is the phasing very important to try and think about, John, in terms of being very exposed to the early part of many projects, we should see a big increase in procurement? Or is that not something we should be particularly concerned about?

John Evans - Subsea 7 SA - COO

Well, I certainly think with the relationship between procurement and our project total value on EPIC hasn't changed. The relevant cost components of each have, but the relative split between them is about the same.

In Subsea 7 world today, we have less large EPIC projects going through than we did a year or two ago, but that's how the procurement number comes down.

Jean Cahuzac - Subsea 7 SA - CEO

Maybe one point to add is that in our negotiation with our customer today we are, I think, able to negotiate good terms and conditions from a cash flow profile of the project on these large projects. But there are not a lot of large projects, so we're not going to see a lot of procurement on the oncoming projects.

Mick Pickup - Barclays - Analyst

A couple of questions, if I may. Firstly, your peers this morning were putting a great deal of emphasis on the strength of the balance sheet and how they think on some of the projects that's going to be a mitigating factor in their favour. I'm assuming you're in the same position, though. I'm just wondering if you're seeing your balance sheet gaining you an advantage on some of the contracts.

Jean Cahuzac - Subsea 7 SA - CEO

I think it's fair to say that what we hear from our clients when they look at who to select they look at the balance sheet. And we have some example of where they decided to go to Tier 1-type operators or contractors because of the balance sheet. It's obviously a risk that they don't want to take, so it's an advantage in a number of cases.

Do you want to comment on the balance sheet, Ricardo?

Ricardo Rosa - Subsea 7 SA - CFO

No, Jean, I think you've touched on it very well. I'll leave as is as I indicated in my initial comments, we firmly believe that maintaining a strong balance sheet through this relatively uncertain period in the cycle is important, both because of the flexibility it provides us in terms of sources of easier financing, but also because it sends a strong message to our clients that we are there for the duration and that we are capable of executing on our commitment. I think that's positive for us.

Mick Pickup - Barclays - Analyst

Okay, thank you, Ricardo. And a follow up, I think, Ricardo, you said going forward you're going to have new projects where our new cost structure is already factored in to the projects. Could you tell me how much you've saved?

Ricardo Rosa - Subsea 7 SA - CFO

Mick, we've touched on that a fair amount in previous calls. I think we've talked about the target savings that we were hoping to get as a result of our recycling exercise in 2015.

And if you look at some of the results that we've shared with investors, our headcount is down 3,600 in the course of 2015 versus the target 2,500; and we certainly did what we intended to do in terms of reducing the vessel fleet.

So I would say that we have achieved and potentially exceeded our targets in terms of our internal cost base. But, this being said, activity still continues to be precarious and we are certainly not resting on our laurels. We're targeting everything we can to continue achieving further reductions.

Frederik Lunde - Carnegie Investment Bank AB - Analyst

Very good numbers; I think you surprised us big time this morning.

I'm just curious, you said at Q4 you were quite happy with the consensus for 2016 and is that still your view today? What do you see in terms of revisions based on the good start of the year?

Jean Cahuzac - Subsea 7 SA - CEO

No, if we had a problem with the consensus number that we see we would mention it, and we have not said anything. But, Ricardo, do you have something to comment?

Ricardo Rosa - Subsea 7 SA - CFO

I think it's a good start to the year. This being said, as Jean has mentioned consensus, we would have made some comment if we felt uncomfortable with consensus. I would remind you, we raised guidance as we indicated in our earnings presentation, and so we're expecting a somewhat higher EBITDA percentage margin than we'd initially seen. But apart from that, I think that there's little else to comment.

Frederik Lunde - Carnegie Investment Bank AB - Analyst

You mentioned that you're looking at strategic acquisitions. I'm just curious, how you do you evaluate those versus your own equity? It's got to be difficult to find anything more attractive than Subsea 7 equity these days.

Ricardo Rosa - Subsea 7 SA - CFO

Our view is that we intend to maintain a strong balance sheet throughout the cycle and associated with that is ready access to liquidity both on and off the balance sheet.

And in the event that we perceive that there is excess cash which cannot be earmarked for our continuing capex commitments and management of working capital, and is not earmarked for potential opportunities in the M&A space, we will consider returning it to shareholders. And that is why we have maintained our share repurchase program in place.

Jean Cahuzac - Subsea 7 SA - CEO

To come back on how we look at opportunities also, one should not think about the necessarily large M&A, or whatever. They are one of our focuses and key differentiator is technology, and we will continue to evaluate opportunities to strengthen our position on some key technologies. We’re not talking about, let's say, large investments; they are things that we can do very well within our own balance sheet.

Frederik Lunde - Carnegie Investment Bank AB - Analyst

But your equity or your shares are showing at half a book value and between 4 times EBITDA, so I guess valuation is not really going to be the catalyst for share repurchases. Is this more at getting visibility on the market, or is it completing the capex program and basically going in to 2017 with outlook for more free cash flow? What is going to be the catalyst for concluding this discussion?

Jean Cahuzac - Subsea 7 SA - CEO

Well, we aim to complete the new-build own vessel investment, and that's going on pretty well. And then, we will review if there are opportunities outside of vessels which would make sense, and evaluate each of them on their own merit.

Christopher Mollerlokken - SpareBank 1 Markets - Analyst

As in Q4, Q1 was influenced by, of course, significant positive gains on the close-out of projects. Going forward, can you provide any color regarding how the projects could potentially develop in second quarter, third quarter? Or where fourth quarter and first quarter were exceptional in terms of amount of successful close-outs?

Jean Cahuzac - Subsea 7 SA - CEO

You have in the back the costs and where we are on the execution of the project, so there will be fewer projects which will come to closure in the coming quarters.

The way I look at the results, it reflects, I would say, a very good operational performance from our teams. And we have been doing that for quite a while, and no reason why it will change. But there will be fewer projects which will come to closure.

Daniel Butcher - JPMorgan - Analyst

I was wondering, on the cost savings side, you've alluded to additional measures that you otherwise wouldn't have taken that you're going to look at taking now. Can you elaborate a bit more about how many more vessels you would look at stacking, and how many more staff you would look at cutting, and any other efficiency measures you might be taking?

Jean Cahuzac - Subsea 7 SA - CEO

Yes, I'm not going to be able to give you all the details of the plans. But I think we have proven in 2015 that we were very proactive in terms of taking the measure when needed, when we had more information about the market trend. So we're going to remain very proactive and then we will reduce a capacity, as required.

What is important for us is to continue to do what we did in 2015, which is also to maintain capability, not only to execute the project well during the downturn, but to be able to rebound when the market improves.

So, same approach as for 2015. It's been successful in 2015, and I expect it to be successful in 2016.

Daniel Butcher - JPMorgan - Analyst

And if I could perhaps have one more go at asking about the margins. 29%, 30%, and now 38% in the last three quarters on an EBITDA basis, do you think you'll be above 30% in second quarter, and then dropping off? Or will that persist through the third quarter as well.

Jean Cahuzac - Subsea 7 SA - CEO

I'm not going to give you a number, but, as Ricardo said, you cannot expect the margin to remain at this level during the coming quarters as fewer projects will be at the final stage of execution. As the portfolio project has change, as there is still question on margin because of competition, you should expect slower margins in the future, there's no doubt there.

Kevin Roger - Kepler Cheuvreux - Analyst

Two questions from my side please, where in the margin, once again; sorry to come back on this. But just once again surprised the market with a strong beat in terms of EBITDA margin you revised of the guidance for this year. Last year, you have done the same thing. I was wondering, would you say take a very conservative approach in your guidance for the full year in that we could have some positive surprise over the next quarters?

And the second one, please, regarding the potential award that you identified, the SURF, which one is the most likely to be sanctioned over the coming months, in your view, please?

Jean Cahuzac - Subsea 7 SA - CEO

I think on the second part of your question, the uncertainty about which project, when, and how remains. And I think I wouldn't speculate on which one will be the first and when it will happen. I honestly don't know. But they are still on the table, and there are more projects which will be put on the table. But uncertainty will remain.

Regarding the conservative question, we are not conservative in our approach. We are actually applying very strictly accounting rules in the way we manage the project. And we are prudent when we evaluate the risk, and we are releasing contingency when it makes sense. So we will not change this approach.

Regarding the margin, my comment is the same as before: there is not a lot we can do.

And I think another point that I should have mentioned is that we are prudent on revenue recognition. What you have in the numbers is something that has been accepted by the clients, so we have a very high degree of percentages that we will get. We are not speculating on future commercial negotiation.

Kevin Roger - Kepler Cheuvreux - Analyst

Maybe just one other question, please. Can we have an update from your *Seven Waves* vessel, please, with the fire that we had in Brazil? Can we have an update from this?

John Evans - Subsea 7 SA - COO

Yes, so the Waves is in Europe being repaired, as we advised last time. The tower has been removed off the vessel and will then be repaired, in line with what we discussed previously.

We're in a discussion with Petrobras regarding the position, as we talk about in an event that occurred with some client products. That discussion continues. And we maintain our position, as we are under contract at the moment.

Haakon Amundsen - ABG Sundal Collier - Analyst

Two questions from me, please. You mentioned that the market outlook hasn't changed. I just wondered if you can put some colour on how you think about the brownfield and the subsea tie-back part of the market, given the current oil price environment; if that is likely to have a positive impact on that part of the market.

And then secondly, with respect to your working capital guidance for this year, I just wondered if you could say that does this reflect a normalized level as we go in to 2017, when you look at the working capital relative to your sales?

Jean Cahuzac - Subsea 7 SA - CEO

Yes, I will answer the first part of the question, and Ricardo will pick up the second part.

What we are seeing today is a few tie-backs around the world. The way I see the market recovering when it recovers will start with more tie-back to maintain production, fight against deflation, and large projects coming a bit later on. So we are seeing some activity there, not to the levels that we used to see when the market was better.

One of the important things about the tie-backs in to the environment is the differentiator of Subsea 7, and I would just name two. The differentiator is to be able to propose lower cost solution, and John elaborated on that.

The other one is technology. You have seen the recent announcement of the bundle that we announced. We continue to be quite successful with our bundle technology in the UK because it's a very cost-effective solution for the tie-backs in this part of the world, and maybe in other part of the world, too.

Today there is some work there, but not a lot. And there is competition, but we are able to differentiate ourselves for these types of jobs.

And the last point on tie-back, when we talk about priority on technology we see future the market going to have longer tie-back, long distance tie-back, and that's why we are focusing on technology which relates to this type of challenges. An example, just one example is the electrically trace heated pipe, which is the key technology project for us which will allow us to make the differentiation later on.

Ricardo Rosa - Subsea 7 SA - CFO

I think with regard to the guidance we have provided on net working capital movement, we've given it on the basis of our best estimate that we have come up with using a bottom-up approach. But I think you have to bear in mind that there is a lot of variability on timing of cash flows, revenue recognition, and payment of supplier, particularly related to the lump sum projects. So we will be updating our guidance as the year progresses, and where we think it is appropriate to do so.

You should not make any assumptions about 2017 working capital movements, and particularly since we haven't provided any guidance yet with regard to activity levels and associated revenue and cost lines. I think I would suggest that we remain focused on 2016 and, therefore, not make any premature assumptions of how working capital will move next year.

Michael Rae - Redburn Partners - Analyst

I was actually going to ask about *Seven Waves* as well and just whether the downtime of that vessel is covered by any insurance, or how the contract actually works, given that the equipment problems were related to another party. And I suppose my question is, are you still receiving payment for that contract even though the vessel is not working?

Jean Cahuzac - Subsea 7 SA - CEO

Well, as far as we are concerned the vessel is under contract and we expect payment. Regarding the insurance, we are covered for equipment replacement and repair. So the revenue side will come from Petrobras, and the repair of equipment is insured with some deductible, as you can imagine.

Michael Rae - Redburn Partners - Analyst

In terms of what's going through the P&L at the moment, is there revenue with no cost?

Ricardo Rosa - Subsea 7 SA - CFO

We are continuing to monitor the situation on *Seven Waves*, and we'll be providing an update, as appropriate, as the contractual discussions with Petrobras progress.

Jean Cahuzac - Subsea 7 SA - CEO

The cost of the Waves are in the numbers. We actually take the costs as they occur. We have people costs, operating costs, etc.

Michael Rae - Redburn Partners - Analyst

Since the vessel is not operating, I assume they are minimal at the moment?

Jean Cahuzac - Subsea 7 SA - CEO

We are optimizing the cost as part of the contract commitment with Petrobras, where we have to mitigate the costs for Petrobras to allow them to minimize their cost. Providing it doesn't impact us, is fine.

David Farrell - Macquarie Research - Analyst

Sorry, one quick question from me. Just in terms of the margin, to what degree is there a bit of a structural shift within Subsea 7 in to a higher margin business, given the increasing proportion of the PLSV contract in the overall revenue mix?

Jean Cahuzac - Subsea 7 SA - CEO

The PLSVs have a positive impact on margin in our results, and today are playing a key role in the overall results of the Company, it's true. But there are also projects -- the projects which came to an end or under completion, particularly in Africa, generated high margin as they pick contracts. So I wouldn't say that it's only PLSVs who explain the Q1 margin level; it's the overall portfolio of projects.

Mark Wilson - Jefferies - Analyst

Yes, sorry to ask again on the *Seven Waves* situation, but I think the good margin performance this quarter wasn't so much of a surprise if you looked at your cost of sales trend. And so I would just like to ask a follow on from Michael's question regarding the *Seven Waves* repair, whether that is included in your cost of sales for this quarter and the second quarter, or whether it's in capex, or what?

Ricardo Rosa - Subsea 7 SA - CFO

As far as *Seven Waves* is concerned, I think you have to bear in mind too that this is one of about seven vessels, or eight vessels operating in Brazil. And we have also had a significant amount of revenue and associated margin relating to lump sum contracts which have nothing to do with the PLSV, so I don't think you should over play any impact related to *Seven Waves*.

Now, in specific response to your question, the cost of repairing the equipment that was damaged on *Seven Waves* is largely covered by insurance. There are some potential additional costs that we have evaluated, and we evaluated them in the course of 2015, shortly after the incident. So if there are any additional costs that arose they were recognized at the time that the -- to the extent that they had been committed at the time that they were incurred.

As Jean has already mentioned, *Seven Waves* has been de-manned and the costs associated with it reduced as much as possible, so I don't think you should overplay the impact that the vessel has on the profitability of the first quarter.

Morten Nystrom - Nordea Markets - Analyst

Thank you, gentlemen, for taking my questions. First, on the negotiation you mentioned with Petrobras, just to understand this, is it -- are these conversations now largely completed and you are, more or less, just waiting for the final signature? Or is it still an ongoing discussion with Petrobras regarding contractual terms?

Jean Cahuzac - Subsea 7 SA - CEO

I think it's ongoing. As I mentioned in my comments, it's in a constructive way on both sides. But it's ongoing. It's a complex situation that Petrobras is in, so it may take some time.

Morten Nystrom - Nordea Markets - Analyst

Okay. Second question is, I guess you have several -- said several quarters now that we should expect now slower margins in the future, and that will happen, obviously. But I would also expect that the strong Q1 also surprised you, given that you have lifted your EBITDA assumptions for the full year. Could you give some color on what could surprise your forecast for EBITDA margins for the remainder of 2016?

Ricardo Rosa - Subsea 7 SA - CFO

I think surprise is a strong word. We have emphasized the importance of good execution in terms of preserving or enhancing margins; and good execution means that we are able to mitigate risks and, therefore, incur potentially lower costs than could have been incurred had those risks crystallised. And furthermore, Jean has also referred to the discussions that we had with clients as we close out projects.

So I think all these elements -- and added to that we have the reduction in the cost base that we have achieved as a result of our efforts in 2015. So when you add it altogether there is some potential for variability on the upside.

But looking forward, and it's an inherent feature of our business, there is also downside risk. And I think some of the downside risk has already been highlighted in your questions with regard to, for instance, the PLSVs; and clearly, that could potentially have an impact going forward.

But there are other variables as well. There have been risks associated with the execution of lump sum projects that we are foreseeing in the course of this year.

Jean Cahuzac - Subsea 7 SA - CEO

As you know, it's always difficult to look at results on one-quarter basis, and that's why we made the comments on the whole year of 2016. Things go up and down, and it's part of our business.

Morten Nystrom - Nordea Markets - Analyst

And a final question from me, if I may. Let's assume that the oil moves to $50, will this be a level where oil companies eventually will start sanctioning projects? Or do we need to see a higher oil price? I know there's a lot of different things playing in, cash flows, etc., but what kind of, when you talk to clients, breakeven levels do you see on deepwater SURF projects in the different regions?

Jean Cahuzac - Subsea 7 SA - CEO

I'm very encouraged with the discussions we have with our clients on what we can achieve together to reduce the costs to make projects viable. But one of the drivers you mentioned is the cash flow management of the oil operators, and I would let them answer on when they will be ready to actually change their approach; it relates to dividend, it relates to a lot of things. I can't really answer your questions, it's very difficult now.

Things are going in the right direction with projects are viable at the lower oil price. What is the strategy of the oil company in terms of the timing of release of their cash and dividend versus investments is, I would say, up to them to answer.

I would like to thank you, everybody, for the questions.

To conclude, the fundamental long-term outlook for deepwater and oil and gas remain intact. We are, meanwhile, adapting to industry conditions. At the same time, we are staying focused on our strategic priorities.

Our industry has functioned well at low oil price in the past, and we can do so again in the future, I have no doubt about that. And our ability to deliver projects at lower costs is the key differentiator for Subsea 7, and I think will be an even higher key differentiator with the progress we are making in working and technology.

So, with that, we'd like to thank everybody for participating to the call, and looking forward to meeting you in the near future. Thank you.