CORPORATE PARTICIPANTS

Don Caron
Chief Executive Officer

Jason Theiss
Chief Financial Officer

Trent Abraham
President, Fluids Division

PRESENTATION

Operator

Good day, ladies and gentlemen. Welcome to the Bri-Chem Corp.'s 2017 Third Quarter Financial Results.

At this time, all participants are in listen-only mode. Following the presentation, we will conduct a question and answer session. At that time, participants are asked to press star, one to register for a question. For assistance during the call, please press star, zero on your telephone touch-tone phone.

As a reminder, this conference call is being recorded today, November 9, 2017.

Representing Bri-Chem today, we have Don Caron, President and Chief Executive Officer; Jason Theiss, Chief Financial Officer; and Trent Abraham, President of Operations.

Please be advised that statements made on this call other than statements of historical fact may contain forward-looking information. I refer you to the forward-looking information statements disclaimer included in Bri-Chem's Q3 press release, Annual Report, and Annual Information Form. Bri-Chem also cautions you that this disclaimer also applies to and expressly qualifies any forward-looking information disclosed in today's call.

It is my pleasure to introduce Don Caron, President and Chief Executive Officer. Please go ahead.

Don Caron, Chief Executive Officer

Thank you, Operator. I'd like to welcome everyone to Bri-Chem's 2017 Third Quarter Results Conference Call. I will start today with a general overview of our 2017 Q3 consolidated operations; and Jason Theiss, our CFO, will provide a detailed financial results overview; and following that I will discuss the outlook for Q4 and into 2018; and we will end with a question and answer session.

The summer drilling program in Western Canada rebounded from their lows of the past two years which resulted in stronger sales in Canada during the third quarter, while drilling activity remained consistent in the U.S.A. which drove increased year-over-year revenue growth for the Company in the third quarter.

Canada experienced 190 average active rigs during the third quarter of 2017, which is an increase of 71 percent over the prior-year quarter, while the active U.S.A. rig count increased 97 percent over the same period with 947 average active rigs operating in Q3 2017. Activity levels throughout Canada and the U.S.A. have stabilized as commodity prices have rebounded from their lows and appear to be also on the rise. With better technology in the field, companies are able to lower their cost of production which has driven increased drilling activity throughout 2017.

Key Q3 and year-to-date 2017 highlights include the following. Bri-Chem generated consolidated revenues of $30.5 million, an increase of 80 percent from the third quarter in 2016, resulting primarily from higher business activity levels throughout North America.

Third quarter revenue increased by 100 percent in the Canadian Fluids Distribution division and the U.S.A. Fluids Distribution and Blending and Packaging divisions were up 90 percent and 94 percent, respectively, over the third quarter of 2016.

Operating income was $1.9 million and $4.2 million for the three and nine months ended September 30, 2017 compared to negative $0.5 million and negative $3.1 million in the same comparable periods, representing a 532 percent and a 237 percent increase, respectively.

EBITDA was $2.3 million and $5.2 million, respectively, for the three and nine months ended September 30, 2017 versus $0.1 million and negative $2.2 million in the comparable periods in 2016. The increases of over 2000 percent and 330 percent are as a result, again, of significantly improved drilling activity throughout our business segments in the third quarter and the year-to-date operations in North America.

Bri-Chem reported net earnings of $0.9 million or $0.04 diluted earnings per share compared to a net loss of $0.7 million or $0.03 diluted loss per share in 2016, while year-to-date date, the Company reported net earnings of $1.4 million or $0.06 earnings per share compared to a net loss of $4.2 million or $0.09 loss per share for the same period in 2016.

Working capital as at September 30, 2017, was $15.3 million compared to $13.8 million at December 31, 2016. The Company's current ratio (defined as current assets divided by current liabilities) was 1.33 to 1 compared to 1.37 to 1 at December 31, 2016.

Also, the Company has announced on November 7, 2017 that it reached an agreement with the Canadian Imperial Bank of Commerce to increase its Asset-Based Lending Facility from $25 million to $35 million and extend the term of the ABL facility for a period of three years up to November 2020. In addition, the Company has also refinanced its current subordinate debt loan that was outstanding with a new five-year term loan with GreyPoint Capital Inc. Details of this will come further with Jason's discussion.

I will now turn the call over to Jason, our CFO, and he'll provide a detailed financial results overview.

Jason Theiss, Chief Financial Office

Thanks, Don. I'd like to welcome everybody to the call today. Bri-Chem reported EBITDA per share of $0.10 and $0.22 for the three and nine months ended September 30, 2017. The rebound in drilling activity throughout 2017 contributed to positive revenue and earnings growth when compared to the same periods in 2016. Stronger global demand and improved summer drilling program in Western Canada has driven demand increases in drilling fluid products during the third quarter of this year.

Bri-Chem's North American Oil and Gas Fluids Distribution and Blending divisions recorded sales of $30.5 million and $88.3 million for the three and nine months ended this year, representing increases of 80 percent and 121 percent, respectively. The Canadian Drilling Fluids Distribution division generated sales of $12 million and $35 million for the three and nine months of 2017 compared to sales of $6 million and $12.8 million for the same comparable periods of 2016.

The summer drilling program in Western Canada returned to a more reasonable drilling activity levels in the third quarter of 2017. There were 190 average active rigs operating during Q3 2017 compared to 111 average active rigs operating during the third quarter of 2016. The industry experienced a return to more traditional summer drilling programs, which saw rig increases throughout the quarter in the major resource plays that we service. This led to overall stronger drilling activity. In addition, the industry experienced a 75 percent increase in the number of wells drilled in Q3 2017 compared to Q3 of 2016. The average number of operating rigs operating for the nine months of 2017 was 185 rigs, an increase of 80 percent over the same period of 2016.

The U.S. Drilling Fluids Distribution division reported sales of $13.7 million and $38.7 million for the three and nine months ended September 30 of 2017 compared to sales of $7.2 million and $16.1 million for the same comparable periods of 2016. This represented an increase of 90 percent quarter-over-quarter and 140 percent year-over-year.

The average number of rigs running in the U.S. during the third quarter of 2017 increased by 467 rigs to a total of 947 rigs on average, while the U.S. averaged 859 operating rigs for the year-to-date. That's compared to 486 average rigs running for the nine months of 2016. U.S. rig activity continues to experience an increase over the past several months with independent drilling fluid companies gaining rigs as activity levels continue to increase. This has led to an increase in demand for fluid products. Major resource plays in the Rockies, the Mid-Continent, and the Permian in Texas continue to experience higher increased drilling activity levels.

The Canadian Fluids Blending and Packaging division recorded sales of $3.4 million for the three months ended September 30, 2017, an increase of 13 percent compared to the same quarter of 2016, while the division had sales of $11.3 million for the nine months of 2017 compared to sales of $7.7 million for the same period of 2016. Again, with the increased activity levels, total blending and packaging demands have increased for the quarter and for the year-to-date of 2017.

Our U.S. Fluids Blending and Packaging division generated sales of $1.4 million and $3.2 million for the three and nine months ended September 30, 2017.

Our consolidated gross margins were 20 percent for the third quarter of 2017 compared to 16 percent for the third quarter of 2016. With a return to more stabilized selling prices throughout 2017, we have experienced improved margins. With stronger drilling activity in the third quarter, the U.S. Distribution division experienced margin improvement in the third quarter which drove overall improvements in consolidated gross margins.

In addition, last year the Company sold down excess inventories of certain products that were being sold at near or below cost which had a negative impact on margins in the prior year.

Margins in our Canadian Fluids business saw a return to more traditional levels during the third quarter, as the division improved margins by purchasing certain commodities more cost-effectively. Gross margins were 15 percent for the third quarter of 2017 compared to 12 percent for the same Q3 period in 2016. We should experience similar margins in the fourth quarter and beyond to those that we experienced in the third quarter.

Margins in the U.S. Fluids Distribution division grew to 21 percent for the third quarter of 2017 and 19 percent for the nine months of this year, compared to margins of 14 percent and 15 percent, respectively, for the same comparable periods in 2016. During the third quarter, the division saw improved gross margins as selling prices improved in all the major resource plays. Higher margin regions in the U.S., such as the Rockies, experienced an increase in the number of wells drilled, which assisted in margin improvements during the quarter. In addition, the division is purchasing certain products in a more cost-effective manner which has resulted in improved margins. Similar to Canada, with increased drilling activity, the margins are expected to remain strong for the remainder of '17 and into 2018.

The Canadian Blending division recorded gross margins of 23.6 percent and 20.4 percent for the three and nine months ended September 30, 2017. These margins are consistent to the same comparable periods in 2016, and our margins in the U.S. Blending division were 37.6 percent for the quarter and that was also consistent from the third quarter of 2016.

We continue to monitor the Canadian dollar in relation to foreign currencies and adjust our selling prices accordingly. However, we are uncertain as to the potential impact on gross margins in relation to foreign purchases of product.

With the anticipated winter drilling season approaching in Canada, the Canadian Distribution division has increased its inventory during the third quarter. The division purchased products from international vendors which has resulted in longer lead times, and as a result, we've purchased product in advance of the winter drilling season to ensure that we had sufficient inventory levels when drilling activity levels increases as a result of the winter drilling program. The remainder of the divisions do have sufficient inventory levels to meet the current and future short-term demands out there in the market.

A reminder that since our products are commodity in nature, sometimes our margins do have the ability to fluctuate, depending on our product mix.

Currently, the Company employs 73 staff today compared to 70 employees at the end of 2016. Wages and benefits during the quarter did increase as a result of additional personnel along with higher commissions paid to sales personnel due to increased product sales during the quarter. We continue to remain focused on our infrastructure and we may increase personnel marginally if activity levels continue to rise. Currently Bri-Chem is sufficiently staffed to date given the current drilling activity levels and demand for our product.

We experienced an increase in selling and administrative expenses for the third quarter and year-to-date of approximately $97,000 and $122,000, respectively. Selling costs increased in correlation to the increase in drilling activity and sales. Professional fees increased as the Company has adjusted its monthly accruals in 2017 for legal expenses. Occupancy costs were consistent during Q3 2017 compared to Q3 of 2016, while costs increased for the year-to-date in 2017 compared to 2016, as the Company incurred a $250,000 break fee to exit a long-term lease in a facility in Canada. General and administrative expenses increased during the quarter as the Company increased its provision for doubtful accounts.

As activity levels continue to improve, we anticipate selling and administrative costs to increase slightly but not at the same proportion as to the increase in sales. Management constantly and continually evaluates its operating overheads and adjusts spending based on activity levels. We will continue to prudently manage our overhead as activity levels continue to improve. Our infrastructure allows us to be a highly-scalable operation, and we do not anticipate any major significant changes to our overheads in the short term.

The Company maintains a stable working capital position throughout 2017. At the end of the quarter, working capital was $15.3 million with a current ratio of 1.33 to 1 compared to 1.37 at December 31, 2016.

Today, I'm happy to announce that Bri-Chem has extended its senior asset-based lending facility with CIBC Bank. The amended and restated ABL facility is a three-year committed facility that comes with reduced interest rates and an increase to the overall facility from previously $25 million up to $35 million (how boring). The increase will ensure Bri-Chem is adequately funded for its operational needs given the current market environment.

In conjunction with the extension of the senior credit facility, Bri-Chem also agreed on terms to a five-year term debt facility with GreyPoint Capital, a mid market lender out of Toronto, Ontario. The proceeds of the loan were used to refinance previously subordinated debt which was coming due in November. The GreyPoint loan is committed to five years, bears interest at a 30-day banker's acceptance average, plus 8 percent and has monthly principal payments of $67,000 per month. These two facilities will strengthen Bri-Chem's balance sheet and will reduce interest costs immediately. Based on the new ABL facility, Bri-Chem has approximately $13.7 million available under a senior facility and we're in compliance of all of our financial covenants at the quarter end.

That concludes my overall financial summary. I'll turn the call back over to Don.

Don Caron, Chief Executive Officer

Thank you Jason. North American oil and gas drilling activity levels throughout 2017 have increased and recovered from their lows in 2016, and we expect activity levels to remain at or near current levels for fiscal 2018. We are cautiously optimistic, however, about activity levels in the fourth quarter of 2017 as many drilling companies are nearing completion of their capital spend for fiscal 2017, which could trigger a marginal reduction in drilling activity during the fourth quarter of 2017.

PSAC has forecasted 2,153 wells to be drilled in Western Canada for the fourth quarter of 2017, representing a 45 percent increase over the fourth quarter of 2016. Furthermore, PSAC is forecasting 7,889 wells to be drilled in Western Canada for 2018, which is an increase of 4 percent over 2017. The modest increase is expected to have a positive impact on the demand for drilling fluids and is anticipated to drive more demand for our drilling fluid products in 2018.

While the U.S.A. drilling market is showing signs of a small reduction in active rigs operating in the fourth quarter of 2017, we feel that drilling activity levels will remain consistent to that of 2017 or marginally improved throughout 2018. We also intend to look at expanding deeper into certain active resource plays in the U.S.A. drilling market so we can continue to expand our growing client base and secure more overall market share.

As a result of the closing of our recently announced agreement to renew and increase our senior operating facility and refinance our current subordinated debt with our new committed five-year term debt, our overall financial position has now been solidified and we can focus on growing our business. As activity levels continue to improve over the medium term, we will seek new growth opportunities while remaining committed to providing superior customer service, while having sufficient inventory levels to meet the demand of our customers throughout our unmatched North American warehouse distribution network.

I would like now to open up the call to a question and answer session. Operator, please provide instructions to the listeners.

QUESTION AND ANSWER SESSION

Operator

Thank you. If you have a question at this time, please press star, one on your telephone keypad. There will be a brief pause while participants register. Thank you for your patience.

Once again, please press star, one at this time if you have a question.

The first question is from Darren McCammon from Proactive Financial. Please go ahead.

Darren McCammon, Proactive Financial

Hi guys. Great quarter.

Don Caron, Chief Executive Officer

Thank you.

Darren McCammon, Proactive Financial

Congratulations on the Fulcrum debt refinance. That's a big deal too.

Don Caron, Chief Executive Officer

Yes, absolutely. We're happy that we got that done.

Darren McCammon, Proactive Financial

Now that you've got that done and are having strong quarters, can you talk a little bit about how you plan to get the word out?

Don Caron, Chief Executive Officer

Well I think that like I've discussed in the past that we needed to string together, have some consistency with respect to our operations and our numbers and obviously have the momentum on our side not only with good numbers but also with the fact that the oil and gas industry is starting to have some stability towards it. So now that'll open a few more doors up for us to be able to go and visit similar to what we did in the past where we were on quite a mission, while we had $90 to $100 oil we had quite a schedule where a lot of people wanted to see us and clearly over the last two years now there hasn't been a big audience for a small cap company like ours. So we certainly do intend on getting back out there and revisiting a lot of the firms and new firms that aren't aware of our Company and obviously doing a lot more presentations and getting that word out.

Darren McCammon, Proactive Financial

Good. Do you have any road shows or conferences or anything currently on your schedule?

Don Caron, Chief Executive Officer

The last few—I'm going to say last three to four weeks has been nothing short of flat out busy with not only operations but with our financings that took place here. The focus has been on that. We have made several calls out to the marketplace of groups that we were in touch with prior to securing a financing with the individual groups that we came with and so we indicated to them that once we got this quarter completed that we would be following up with them and hopefully booking some road shows with them.

Darren McCammon, Proactive Financial

Okay, great. That's understandable. Also, your presentation on the website is from 2015. Maybe you guys could get—I know you're busy, but maybe you could get to providing an update.

Don Caron, Chief Executive Officer

Yes, I mean the website has been something that has not been a priority to us and we do have that on our agenda as well but given the fact that we will be out there again a little bit more than we certainly have in the past, that that is something that's going to have to go to the top of the priority list.

Darren McCammon, Proactive Financial

Okay, thanks. I just new pictures and stuff for my article.

Don Caron, Chief Executive Officer

Ah, not a problem.

Darren McCammon, Proactive Financial

So thanks for covering the margins in such detail. I had a question on that, but you already covered it so I don't need to go back into it. On the Fulcrum refinance the way I calculate it is it dropped about $0.01 per quarter to earnings. Do I have that about right, just the lower interest rate?

Don Caron, Chief Executive Officer

Yes, I think that if we ran the numbers just on the extra 8.5 percentage points I think you're very close.

Darren McCammon, Proactive Financial

Okay, thanks. On your capex, how should I think about—how much of it is maintenance versus how much of it is growth?

Jason Theiss, Chief Financial Officer

Sure. We typically don't run an extraordinary amount of maintenance capex there. If you were to look at a capex budget in the past, this Company was very capex light and that was more or less maintenance capex. So that historically had been anywhere between $200,000 to $300,000 annually, which I would say is a very safe number from a maintenance capex perspective. Any increases that we've seen in capex over the last couple of years and into 2017 and 2018 is going to be growth capex. So that would include things like our laboratory facility in Bakersfield, California. It'll include our rental—we were renting storage tanks for some of our product, like bulk barite, like our liquid inverts, that we now purchase those tanks themselves. We got into an expansion where we got into some more liquid blending in the Texas marketplace.

So that's where the capex has come from in '17. In '18 we're going to continue on, as Don mentioned, along that same process of getting deeper into the bigger resource plays and we'll be spending a majority of that capex will be on growth capex and not on maintenance.

Darren McCammon, Proactive Financial

Okay. So $200,000 to $300,000 on maintenance and the rest is growth. Got it. Do you guys own a lot of your own trucks that bring the liquid stuff out or does the customer (inaudible)?

Don Caron, Chief Executive Officer

Trent, do you want to answer that question?

Trent Abraham, President, Fluids Division

Yes. So the only place that we have our own trucks is in the Sun Coast materials out of Bakersfield, California and that is for field and for customer delivery to their locations. Everywhere else it is all third party truckers and transportation groups that are arranged by the customer. We have some priority ones that we like to promote and utilize in the areas because of the service that they provide and we suggest them to our customers first.

Darren McCammon, Proactive Financial

Okay, good, thanks. On the ABL, so you used about $15 million of it this quarter. Why did you need to raise it from $25 million to $35 million?

Jason Theiss, Chief Financial Officer

Well part of the reason for the increase there is driven by market demand as activity levels continue to increase, and we've got some seasonality of our business in Western Canada. The winter drilling season, for example, you typically will see an increase in rig count and I believe the number of wells increases is an indication of that but we'll run about 330 rigs this winter. That means that we've got to use our line to purchase inventory and carry our AR until we start seeing a collection of that AR.

I mentioned also that due to some of the international purchasing that we're doing, there's longer lead times for a lot of those products. It's usually anywhere from 8 to 10 to 12 weeks in some cases they get that product brought in from overseas and a lot of those vendors require payment, partial payments or full payments upfront before we get that product. So that puts us utilizing more of our revolver and then that revolver comes down over a period of time. So during the winter months is typically when we ramp up and we are buying a lot more inventory and then come this spring breakup period is when we come and typically pound down the line because we're collecting a lot of the receivables.

Darren McCammon, Proactive Financial

Okay. I thought you did—you peaked at about $17.8 million on the ABL last year. So you're expecting—I'm just reiterating it and correct me if I'm wrong—you're expecting that number to be a bit higher this year due to increased business and then also longer lead times on some of your sourcing.

Jason Theiss, Chief Financial Officer

Correct.

Darren McCammon, Proactive Financial

Okay. So you also indicate further expansion into the U.S. You talked about the GreyPoint Capital did 9.5 percent and it's, correct me if I'm wrong, but it doesn't have prepayment penalties and there is always the possibility of paying a dividend. So given those different choices for free cash flow, can you talk a little bit about your capital allocation strategy and what you intend to do with free cash flow? Give me a little more colour?

Don Caron, Chief Executive Officer

Well I think first of all just to clarify, we do have some flexibility in the repayment of the GreyPoint loan but it's not a full out no penalty if we do redeem that loan earlier. We were able to get some flexibility where we could pay back a portion of it without any penalties but if we do decide that we could get cheaper money elsewhere and want to pay this loan back it's not that it doesn't come with some prepayment penalties. Now we don't feel that it's an onerous prepay penalty but there certainly is one.

Now with respect to free cash flow, again, as a result of the fact that we are garnering more market share and that our customer base is growing alongside with us in new regions as a result of us enabling them to be able to go to new regions, a lot of our free cash flow gets tied up, as Jason just mentioned, into increasing our inventory levels to be able to service more business. There isn't a lot of free cash flow for us to utilize right now to say go out and do any particular large acquisition and so we've got to be very careful again that we're monitoring activity levels and right now we feel that they're going to be stable. But of course the commodity price still has some volatility out there that we still have to be cautious of not putting too much out there and then putting our cash flow in jeopardy.

Darren McCammon, Proactive Financial

Okay. So that last warehouse that you bought, do we know what the ROI is on that?

Don Caron, Chief Executive Officer

Now which warehouse are you referring to?

Darren McCammon, Proactive Financial

Well the last expansion that you did. I think it was in the Permian.

Don Caron, Chief Executive Officer

Yes, I think...

Jason Theiss, Chief Financial Officer

Probably Kermit.

Don Caron, Chief Executive Officer

Yes, that wasn't something that we purchased. That was again a third party startup on an invert facility that is actively now really started to take off for us. It does take us some time and we're really excited about where it's going. We've had to deal with some of the trucking issues as Trent mentioned to ensure that we do have reliability there. But as far as an ROI, it's just too soon to provide that right now but we certainly believe that that is going to be a very profitable centre for us.

Jason Theiss, Chief Financial Officer

We typically, Darren, rent that. Something like that we would rent the facility, we'd rent the equipment and really all we're providing is the material, the product that we sell would go into that warehouse and then we service the customers within that region. So it's not a true acquisition of a warehouse.

Darren McCammon, Proactive Financial

Yes, I understand. So an ROI really isn't—well, you didn't put much cash into it in the first place, so. I guess what I'm trying to get to is kind of an idea of what kind of ROIs you're seeing from growth versus paying down debt versus paying down the dividend and really what it comes down to. Maybe you could get back to me with some more about that.

Don Caron, Chief Executive Officer

Yes, that's something that clearly now that we are starting to generate the type of EBITDA that we have this quarter, and hopefully going forward it's going to be similar if not better, then that's something that we could start to explore and provide more insight to.

Darren McCammon, Proactive Financial

Okay, thanks. That's all the questions I have at this time.

Jason Theiss, Chief Financial Officer

Thanks Darren.

Operator

Thank you. There are no further questions at this time. I'd like to turn the meeting back over to Mr. Caron.

Don Caron, Chief Executive Officer

Okay, well, again, everyone, thank you for attending our Q3 2017 conference call, and we certainly look forward to rejoining with everybody for our year-end Q4 which will be likely around the third week of March 2018. So again, thank you very much for attending.

Operator

Thank you. The conference has now ended. Please disconnect your lines at this time and thank you for your participation.
