Philly Shipyard ASA (OSE: PHLY)
Q4 2018 and Full Year 2018 Results

6 February 2019

Key Events

- ✓ As of 31 December 2018, the two-containership order for Matson is approximately 95% complete
- ✓ On 31 October 2018, Philly Shipyard delivered the first vessel (Hull 029) in the two-containership order for Matson
- ✓ Philly Shipyard continued to idle certain operations and impose layoffs due to the lack of new orders after the Matson project
- ✓ Fourth quarter and full year 2018 operating revenues and other income of USD 19.4 million and USD 129.2 million, respectively, compared to USD 198.7 million and USD 614.6 million in the same periods in 2017
- ✓ Fourth quarter and full year 2018 EBITDA of negative USD 3.4 million and negative USD 33.4 million, respectively, compared to USD 39.3 million and USD 105.1 million in the same periods in 2017
- ✓ Fourth quarter and full year 2018 net loss of USD 9.0 million and USD 45.4 million, respectively, compared to net income of USD 30.7 million and USD 67.2 million in the same periods in 2017
- ✓ Total cash and cash equivalents of USD 49.6 million at 31 December 2018, excluding USD 44.6 million of restricted cash for securing a loan and a guarantee holdback
- ✓ Order backlog of USD 17.4 million on 31 December 2018

Operations and Shipping Investments

Vessel Construction

At the end of the fourth quarter of 2018, Philly Shipyard was building the second of two containerships for Matson (Hulls 029-030). Hull 029 (named *Daniel K. Inouye)* was delivered to Matson on 31 October 2018. This vessel is the largest containership ever built in the United States. Hull 030 was launched on 13 November 2018. The planned delivery date for Hull 030 remains Q1 2019.

While Philly Shipyard continues to actively seek new orders and the capital necessary to build vessels after Hull 030, it continues to adjust its operations and workforce in line with its current order backlog. These adjustments include idling additional parts of its facilities and laying off more of its employees. Currently, the only shipbuilding activity is in one of the two graving docks at the shipyard; all other production facilities are idle. Today, Philly Shipyard's workforce (including direct employees and subcontracted personnel) totals slightly more than 400 people, down from approximately 1,200 people at the beginning of 2018.

Shipping Investments

Philly Tankers, a Jones Act shipping company that is majority-owned by Philly Shipyard, is proceeding with an orderly liquidation process for the purpose of distributing its available cash balances to its shareholders. Philly Shipyard expects these liquidating distributions will total approximately USD 83.1 million (including Philly Shipyard's share of USD 44.6 million) and will be made in Q1 2019. To date, the dividends paid by Philly Tankers to its shareholders total USD 78.1 million (including Philly Shipyard's share of USD 41.9 million).

Health, Safety, Security and Environment (HSSE)

Philly Shipyard's 12-month trailing average for its Lost Time Incident Frequency Rate (LTIFR), as defined by the Occupational Safety and Health Administration (OSHA), at the end of Q4 2018 was 0.23 compared to 0.98 at the end of Q4 2017. Philly Shipyard's 12-month trailing average for its other Recordable Incident Frequency Rate, based on recordable incidents (other than lost time incidents) per 200,000 hours, at the end of Q4 2018 was 3.63 compared to 4.43 at the end of Q4 2017. Philly Shipyard continues to work proactively to further improve safety and reduce the number of incidents at the shipyard.

Financial Information

Fourth Quarter 2018 Results

Operating revenues and other income for the fourth quarter of 2018 were USD 19.4 million compared to operating revenues and other income of USD 198.7 million for the fourth quarter of 2017. Q4 2018 operating revenues and other income were driven by the continued progress on the Matson vessels (Hulls 029-030), whereas Q4 2017 operating revenues and other income were driven mainly by the delivery by Philly Shipyard of Hull 028 to Kinder Morgan and the related sale by Philly Tankers of its Hull 028 shipping assets to Kinder Morgan (profit and deferred gain from equity-accounted investments), as well as continued progress on the Matson vessels (Hulls 029-030).

Net loss for Q4 2018 was USD 9.0 million compared to net income of USD 30.7 million for Q4 2017. The net loss for Q4 2018 was driven by USD 5.3 million of under-recovered overhead costs (i.e., overhead costs incurred and not allocated to projects), as well as an impairment of USD 3.5 million of deferred tax asset since Philly Shipyard did not have an order backlog after delivery of Hull 030 at year-end 2018.

As previously disclosed, under International Financial Reporting Standards (IFRS), 100% of the revenue, cost and profit on each of the Philly Tankers vessels (i.e., Hulls 025-028) was deferred, and the deferred amounts for each of these vessels were recognized at delivery, as if Philly Shipyard was originally building these vessels for its own account. This accounting treatment was required for the Philly Tankers vessels because there were no external customers at the time these contracts were signed and shipbuilding activities commenced.

In addition to the IFRS financial measures reported above, EBITDA[1] and Adjusted EBITDA[2] are considered other relevant earnings indicators for Philly Shipyard as they measure the operational performance of the shipyard. In particular, Philly Shipyard believes presenting Adjusted EBITDA is useful to investors as it provides another measure of Philly Shipyard's profitability from its operations, as if Philly Shipyard never had any shipping investments, and more closely represents earnings from shipbuilding activities.

EBITDA for the fourth quarter of 2018 was negative USD 3.4 million compared to EBITDA of USD 39.3 million in the fourth quarter of 2017. The decrease in EBITDA was mainly driven by the significant under-recovered overhead costs (i.e., overhead costs incurred and not allocated to projects) and impairment charge described above, as well as a breakeven margin recognized in Q4 2018 on the Matson project compared to the significantly higher margin recognized in Q4 2017 on the Philly Tankers project. In addition, in Q4 2017, Philly Shipyard delivered Hull 028 to Kinder Morgan and, as a result, recognized 100% of the profit from the sale by Philly Shipyard of Hull 028 along with 53.7% of the profit and deferred gain from the related sale by Philly Tankers of its Hull 028 shipping assets. Adjusted EBITDA for the fourth quarter of 2018 was negative USD 3.6 million compared to Adjusted EBITDA of USD 10.1 million in the fourth quarter of 2017. The decrease in Adjusted EBITDA was driven primarily by the significant under-recovered overhead costs (i.e., overhead costs incurred and not allocated to projects) and impairment charge described above, as well as the lower project margin described above.

Net financial items in Q4 2018 was USD 0 compared to expense of USD 0.4 million in Q4 2017.

Full Year 2018 Results

Operating revenues and other income in 2018 ended at USD 129.2 million compared to operating revenues and other income of USD 614.6 million in 2017. Operating revenues and other income in 2018 were primarily driven by the continued progress on the Matson vessels (Hulls 029-030), whereas operating revenues and other income in 2017 were primarily driven by the delivery by Philly Shipyard of Hull 026, Hull 027 and Hull 028 to Kinder Morgan and the related sale by Philly Tankers of its Hull 026, Hull 027 and Hull 028 shipping assets to Kinder Morgan (profit and deferred gain from equity-accounted investments), as well as continued progress on the Matson vessels (Hulls 029-030).

The operating revenues in 2018 were impacted by the implementation of the new IFRS 15 standard (IFRS 15). This had an impact on the timing of revenue recognition by increasing accumulated revenues recognized at 31 December 2017 from Hulls 029 and 030 by USD 38.4 million, with a corresponding decrease in future revenue to be recorded from 1 January 2018. As such, there is a USD 38.4 million difference between accumulated

[1] EBITDA is defined as earnings before interest, taxes, depreciation and amortization.

[2] Adjusted EBITDA is defined as EBITDA plus capitalized Welcome Fund interest expense plus or minus net deferred shipbuilding profits plus or minus loss or profit, respectively, in equity-accounted investments minus recognized deferred gain in equity-accounted investments.

revenue from the 1 January 2018 effective date of IFRS 15 and 31 December 2017 as presented in the annual report for 2017. See notes 4 and 11 for further details.

Net loss in 2018 was USD 45.4 million, compared to net income of 67.2 million in 2017. The net loss in 2018 was driven by a loss of USD 11.1 million recognized in 2018 on the Matson project (compared to a forecasted breakeven project margin in 2017), under-recovered overhead costs (i.e., overhead costs incurred and not allocated to projects) of USD 9.4 million (USD 0 in 2017), an impairment charge of USD 17.6 million due to the write-off of the full amount of the work-in-process assets pertaining to two containerships (Hulls 031-032) in connection with cancellation of the CV3700 project, as well as an impairment of USD 3.5 million of deferred tax asset since Philly Shipyard did not have an order backlog after delivery of Hull 030 at year-end 2018.

EBITDA for 2018 was negative USD 33.4 million compared to EBITDA of USD 105.1 million in 2017. Adjusted EBITDA in 2018 totaled negative USD 32.9 million compared to Adjusted EBITDA of USD 41.5 million in 2017.

Statement of Financial Position

Total assets were USD 190.0 million at 31 December 2018 compared to USD 253.0 million at 31 December 2017.

Total interest-bearing debt was USD 59.6 million at 31 December 2018 compared to USD 59.6 million at 31 December 2017.

Cash and cash equivalents (excluding restricted cash) were USD 49.6 million at 31 December 2018 compared to USD 110.1 million at 31 December 2017. The decrease of USD 60.5 million was primarily due to operating activities and USD 26.5 million of additional restricted cash deposited into an escrow account to secure the Welcome Fund loan. This deposit was funded out of the dividends previously paid by Philly Tankers to Philly Shipyard described above in the Shipping Investments section and was required by the Welcome Fund lender in connection with the liquidation of Philly Tankers. As of 31 December 2018, restricted cash consisted of USD 44.6 million, of which USD 39.7 million is related to the Welcome Fund loan, which is expected to be used for repayment of the Welcome Fund loan at its maturity in 2020, and USD 4.9 million is related to a guarantee holdback for Hull 029. For further details on the Welcome Fund loan, see note 8.

Work-in-process was USD 0 at 31 December 2018 compared to USD 13.4 million at 31 December 2017. As previously disclosed in the Company's Q3 2018 report, the project to build up to four containerships (CV3700 vessels) for delivery to TOTE Maritime was cancelled and, in connection therewith, the full amount of the work-in-process assets pertaining to the first two CV3700 vessels (Hulls 031-032), totaling USD 17.6 million, was written off. USD 17.3 million of this impairment charge was taken in Q3 2018 and the remaining USD 0.3 million of this impairment charge was taken in Q4 2018.

Total equity decreased to USD 110.2 million at 31 December 2018 from USD 155.6 million at 31 December 2017 due to the net loss of USD 45.4 million.

Financing

The Company has a secured five-year term loan for up to USD 60.0 million from PIDC Regional Center, LP XXXI through the Welcome Fund loan program. The loan matures in March 2020. The entire USD 60.0 million amount was drawn under this facility as of 31 December 2018.

The Company also has an unsecured three-year revolving credit facility for up to USD 10.0 million from TD Bank, N.A. The facility terminates in April 2019. USD 0.7 million of this facility was utilized as of 31 December 2018 for the issuance of letters of credit.

Shareholder Distributions

Due to the current main focus on securing new orders beyond Hull 030, the PHLY Board has decided not to pay any further ordinary or extraordinary dividends at this time. The PHLY Board will revisit the Company's dividend policy and dividend plan when it has more clarity about the Company's new order situation and related capital requirements.

Outlook

Shipbuilding

As of 31 December 2018, Philly Shipyard had an order backlog of USD 17.4 million. This backlog represents a contractual obligation to deliver the second of two container vessels for Matson (Hull 030). Philly Shipyard is scheduled to deliver Hull 030 to Matson during the first quarter of 2019. The key focus area for Philly Shipyard's operations continues to be the completion and delivery of Hull 030.

As of today, Hull 030 is the last vessel in PSI's order book. Securing contracts for new vessels is the key to unlocking Philly Shipyard's potential for sustained operations and profitability. Due to the under-recovery of overhead costs (i.e., overhead costs incurred and not allocated to projects), Philly Shipyard expects it will suffer significant losses in 2019, even if the shipyard receives orders for new vessels.

In the near term, Philly Shipyard's main focus is the pursuit of the opportunity to build National Security Multi-Mission Vessels (NSMV). The NSMV program seeks to replace up to five of the U.S. state maritime academy training ships. The U.S. Maritime Administration (MARAD) released a request for proposal (RFP) for a vessel construction manager (VCM) for the NSMV program. The VCM contract is expected to be awarded early this year. The VCM will then enter into a contract with a U.S. shipyard to build the vessels. The shipyard contract is expected to be awarded within Q2 2019. MARAD has received USD 300 million in federal funding for the first vessel. Delivery of the first vessel is targeted for the end of Q4 2021.

In addition, Philly Shipyard is in discussions related to several other potential new construction projects for U.S.-built vessels. Philly Shipyard is expanding its search for new opportunities throughout the marine industry. Philly Shipyard is also exploring potential partnerships that can create a stronger entity to secure new work into the shipyard and create value for the Company and its shareholders.

Additionally, Philly Shipyard is aggressively pursuing several possibilities for short-term work to have some activity in the shipyard in 2019 before a production start of a new shipbuilding project. In particular, Philly Shipyard is pursuing opportunities for steel work and repair jobs to utilize idle capacity in its fabrication shops and dry-docks.

Since it began operations, Philly Shipyard has focused exclusively on construction of merchant vessels for the domestic Jones Act market. In the past 15 years, PSI has delivered five containerships, two aframax crude tankers and 22 product tankers. Until now, these projects have consumed PSI's capacity. The Jones Act fleet of dry cargo and petroleum tankers has been recapitalized over the last decade and there are few, if any, immediate opportunities for PSI to build these same types of vessels. In the next 5-10 years, Philly Shipyard believes there are many prospects within specialty and high-end segments of the Jones Act market and replacement needs remain for segments of the aging Jones Act fleet. However, it is anticipated the market opportunities for large Jones Act ocean-going vessels in this time frame will be cyclical and will not produce a steady and predictable stream of work.

In contrast, the outlook for the next 5-10 years in the government sector is very promising. Given these market conditions, following PSI's last commercial product tanker order in 2015, the Company began to plan combining government and commercial work in order to best achieve continuous shipbuilding activities. In order to successfully execute this plan, Philly Shipyard has already taken substantial steps to build-up its government contracting resources and systems and ensure it is prepared to handle government work. Among other endeavors, Philly Shipyard has gained valuable experience with the significant investment made over the past several years in connection with the government-funded industry study and bid preparation for the U.S. Coast Guard's next generation Heavy Polar Icebreaker (now known as Polar Security Cutter) program.

Although the Company faces many challenges and risks, due to its strong cash position, Philly Shipyard believes it is well-positioned to capitalize on any newbuild opportunities in the commercial and government segments that create value for its shareholders. Philly Shipyard remains committed to building the most cost-efficient and environmentally friendly vessels in the Jones Act market and believes that it will be the supplier of choice when these vessels are ordered. Additionally, Philly Shipyard intends to offer the government a new high quality, cost-effective solution to meet their ship program needs.

Shipping

As part of the process of liquidating Philly Tankers described above, Philly Shipyard expects to receive its liquidating distribution from Philly Tankers in Q1 2019. Going forward, in line with its business strategy, Philly Shipyard will continue to evaluate opportunities to participate in the post-delivery economics of the ships that it constructs.

Risks

Philly Shipyard faces significant risks if it is unable to secure new orders and/or financing for vessels after the last vessel in the current order backlog (Hull 030), which is scheduled for delivery in Q1 2019. There can be no assurance that Philly Shipyard will obtain new orders or financing for vessels after Hull 030.

Furthermore, even if Philly Shipyard obtains new orders or financing for vessels after Hull 030, none of the possible projects it is presently pursuing alone will fully cover the estimated under-recovered overhead costs (i.e., overhead costs incurred and not allocated to projects) in its 2019 forecast.

The delay Philly Shipyard has experienced in securing new orders and financing for work after Hull 030 has interrupted its building program, resulting in the idling of all production activities in its facility except in one of two graving docks and a decrease of more than 65% of its workforce (including direct employees and subcontracted personnel) since the beginning of 2018. If this delay continues, then it will further interrupt Philly Shipyard's building program and increase the costs and risks faced by Philly Shipyard, including challenges related to attracting and retaining skilled workers; increases in under-recovered overhead costs (i.e., overhead costs incurred and not allocated to projects); and operational inefficiencies for completion of the remaining vessel in the current order backlog.

The longer the delay in securing new orders beyond Hull 030 continues, the more expensive and challenging it becomes for Philly Shipyard to resume shipbuilding operations. In particular, the extended gap in production activities increases the risk that the Company is unable to mobilize the shipyard's workforce and retain sufficient capital to support future shipbuilding projects. Moreover, under these circumstances, there is a risk that the going concern assumption will no longer apply for Philly Shipyard and, as such, Philly Shipyard will need to do an impairment charge against its fixed assets.

Philly Shipyard depends on unionized labor for construction of vessels. Work stoppages or other labor disturbances could have a material adverse effect on the Company's business, results of operations and financial condition. In order to mitigate this risk, the shipyard signed a four-year collective bargaining agreement with the Unions which was effective through January 2019 (the "2015 CBA"). The 2015 CBA includes a no-strike clause. PSI and the Unions are in the process of negotiating a multi-year extension of the 2015 CBA (the "2019 CBA"). In connection with these negotiations, the 2015 CBA has been temporarily extended until 15 February 2019. There can be no assurance the 2019 CBA will be agreed and ratified.

Philly Shipyard further depends upon a 99-year lease agreement for the shipyard facility. Failure to maintain certain employment levels may result in early termination of this lease. For more details regarding this lease, see "Note 14: Commitments and contingencies" below.

Given Hulls 029-030 are prototype container vessels and the last container vessel built by Philly Shipyard was delivered in 2006, there is a higher technical design risk and a higher project execution risk compared to the recent construction of multiple product tankers, which were based on a proven design. This prototype risk increases the current construction cost estimation uncertainty and the likelihood of occurrence of contract contingencies. In particular, failure to meet Philly Shipyard's performance obligations to deliver vessels on time and within the contract specifications (e.g., speed, container capacity and fuel consumption) can potentially lead to penalties and ultimately contract termination. The loss incurred on the Matson project is attributable in part to this prototype risk. With the delivery of Hull 029 in Q4 2018, the degree of this prototype risk is reduced going forward, as the technical design risk is largely mitigated and the main risk remaining is project execution risk.

Operational risk is the ability to deliver vessels under existing contracts at the agreed time, quality, functionality and cost. Delivering projects in accordance with the contract terms and the anticipated cost framework represents a substantial risk element. Results also depend on costs of goods and services, both Philly Shipyard's own and those charged by suppliers, and on interest expense, exchange rates and customers' ability to pay.

Philly Shipyard is dependent on commitments for debt financing and has exposure in the financial markets, including currency, interest rate, counterparty and liquidity risks. Philly Shipyard has established guidelines and systems to manage this exposure.

Philly Shipyard faces risks related to the contracts for its vessels, including the risk that those contracts are cancelled and the underlying vessels are ultimately sold to third parties for less favorable terms. If this risk were to materialize, then it could have a negative effect on Philly Shipyard's financial performance.

For a further analysis of risks, please refer to the Company's 2017 annual report.

CONDENSED CONSOLIDATED INCOME STATEMENT

Amounts in USD millions (except number of shares and earnings per share)	Q4 Unaudited 2018	Q4 2017	Twelve Months Ended 31 Dec. Unaudited 2018	Twelve Months Ended 31 Dec. 2017
Operating revenues and other income	19.4	198.7	129.2	614.6
Operating expenses	(22.8)	(159.4)	(162.6)	(509.5)
Operating (loss)/income before depreciation - EBITDA	**(3.4)**	**39.3**	**(33.4)**	**105.1**
Depreciation	(1.9)	2.5	(7.8)	(5.8)
Operating (loss)/income - EBIT	**(5.3)**	**41.8**	**(41.2)**	**99.3**
Net financial items	-	(0.4)	(0.6)	0.6
(Loss)/income before tax	**(5.3)**	**41.4**	**(41.8)**	**99.9**
Tax expense	(3.7)	(10.7)	(3.6)	(32.7)
(Loss)/income after tax **	**(9.0)**	**30.7**	**(45.4)**	**67.2**
Weighted average number of shares	**12,107,901**	**12,107,901**	**12,107,901**	**12,107,901**
Basic and diluted (loss)/earnings per share (USD)	**(0.74)**	**2.54**	**(3.75)**	**5.55**

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Amounts in USD millions	Q4 Unaudited 2018	Q4 2017	Twelve Months Ended 31 Dec. Unaudited 2018	Twelve Months Ended 31 Dec. 2017
(Loss)/income after tax	(9.0)	30.7	(45.4)	67.2
Other comprehensive income, net of income tax	-	-	-	-
Total comprehensive (loss)/income for the period **	**(9.0)**	**30.7**	**(45.4)**	**67.2**

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

Amounts in USD millions	Unaudited 31 Dec. 2018	31 Dec. 2017 *
Assets		
Non-current assets		
Property, plant and equipment	44.1	50.1
Equity-accounted investments	44.6	47.3
Restricted cash	44.6	13.2
Deferred tax asset	-	0.9
Other non-current assets	0.3	0.2
Total non-current assets	**133.6**	**111.7**
Current assets		
Cash and cash equivalents	49.6	110.1
Vessels-under-construction receivable	-	7.3
Work-in-process	-	13.4
Income tax receivable	3.3	5.9
Other current assets	3.5	4.6
Total current assets	**56.4**	**141.3**
Total assets	**190.0**	**253.0**
Total equity	**110.2**	**155.6**
Non-current liabilities		
Interest-bearing long-term debt	59.6	59.4
Deferred tax liability	3.0	0.7
Total non-current liabilities	**62.6**	**60.1**
Current liabilities		
Trade payables, accrued liabilities and provisions	16.0	36.1
Income tax payable	-	1.0
Interest-bearing short-term debt	-	0.2
Customer advances, net	1.2	-
Total current liabilities	**17.2**	**37.3**
Total liabilities	**79.8**	**97.4**
Total equity and liabilities	**190.0**	**253.0**

* Annual 2017 financial information is derived from audited financial statements.

** All attributed to the equity holders of PHLY.

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Amounts in USD millions	Twelve Months Ended 31 Dec. Unaudited 2018	2017
As of beginning of period	155.6	91.4
Total comprehensive (loss)/income for the period *	(45.4)	67.2
Dividend paid	-	(3.0)
As of end of period	**110.2**	**155.6**

CONDENSED CONSOLIDATED CASH FLOW STATEMENT

Amounts in USD millions	Twelve Months Ended 31 Dec. Unaudited 2018	2017
Net cash (used in)/from operating activities	(34.2)	109.6
Investment in property, plant and equipment	(1.8)	(7.2)
Dividend received from equity-accounted investments	2.2	39.9
Net cash from investing activities	0.4	32.7
Portion of interest-bearing debt held in escrow	(26.5)	(0.1)
Repayment of capital lease	(0.2)	(0.2)
Proceeds from construction loans	-	127.0
Repayment of construction loans	-	(225.0)
Dividend paid	-	(3.0)
Net cash used in financing activities	(26.7)	(101.3)
Net change in cash and cash equivalents	**(60.5)**	**41.0**
Cash and cash equivalents at beginning of period	110.1	69.1
Cash and cash equivalents at end of period	**49.6**	**110.1**

* All attributed to the equity holders of PHLY.

Notes to the condensed interim consolidated financial statements for the 4th quarter and full year 2018

1. **Introduction – Philly Shipyard ASA**
   Philly Shipyard ASA (PHLY) is a company domiciled in Norway. The condensed interim consolidated financial statements for the three-month period and full year ended 31 December 2018 and 31 December 2017 are comprised of PHLY and its direct and indirect wholly-owned subsidiaries, including Philly Shipyard, Inc. (PSI).

   This interim report has not been subject to audit or review by independent auditors.

   The audited consolidated financial statements of PHLY as of and for the year ended 31 December 2017, which include a detailed description of accounting policies and significant estimates, are available at www.phillyshipyard.com.

2. **Basis of preparation**
   These condensed interim consolidated financial statements reflect all adjustments, in the opinion of PHLY's management, that are necessary for a fair presentation of the results of operations for the period presented. Operating results for the three-month period and full year are not necessarily indicative of the results that may be expected for any subsequent quarter or year.

   The interim consolidated financial statements for the fourth quarter of 2018 have been prepared on the basis of a going concern assumption. This assumption is based on liquidity forecasts prepared by the Company which demonstrate that the Company's current financial situation, including its cash position, will make it possible to continue operations for a period of at least twelve months from the date of this report. However, there is inherent uncertainty in cash flow forecasts and the ability of the Company to secure a customer order beyond Q1 2019.

   As outlined above, the Company has initiated several cost saving initiatives including idling certain operations and imposing layoffs. These actions allow the Company to actively work on securing new orders beyond the delivery of the last vessel in the current order book (i.e., Hull 030) in Q1 2019.

3. **Statement of compliance**
   These condensed interim consolidated financial statements have been prepared in accordance with IFRS as adopted by the European Union IAS 34 Interim Financial Reporting. They do not include all of the information required for full annual financial statements, and should be read in conjunction with the audited consolidated financial statements of PHLY as of and for the year ended 31 December 2017.

4. **Significant accounting principles**
   The accounting policies applied by PHLY in these condensed interim consolidated financial statements are substantially the same as those applied by PHLY in its audited consolidated financial statements as of and for the year ended 31 December 2017.

   When implementing the new IFRS 15 standard (IFRS 15), the Company has concluded that the Company can continue with revenue recognition over time. In addition, the Company has assessed the effect implementing IFRS 15 has on the costs related to the Matson contract. In 2017, the cost incurred has exceeded the cost recognized as expense according to IAS 11, and presented as an asset (work-in-process). According to IFRS 15 these expenses cannot be presented as an asset. For 2017, applying IFRS 15 for this contract, these incurred expenses that are not charged as cost shall be recognized as cost with a similar increase in revenue based on IFRS 15, with no margin. The Matson contract was as of 31 December 2017 estimated to be a USD 0 margin contract and there was no effect on equity in the opening balance related to IFRS 15. As of 31 December 2018, the Matson contract is estimated to be a loss-making contract. The estimated loss is provided for as of Q4 2018.

   Although IFRS 15 had no impact on the Matson vessels in 2017, it has had an impact on those vessels in 2018. The impact is related to how percentage-of-completion (POC) is measured under IFRS 15. Until the end of 2017, POC was measured using production hours, whereas from the beginning of 2018, POC is measured based on costs, by calculating the proportion of contract costs incurred for work performed compared to the estimated total costs for each contract. This is considered a better measure of the progress and completion of a project, as it also captures the progress for design, planning and procurement activities before start of production. Measuring POC by using costs incurred is also commonly used in earned value management systems.

Through Q4 2018, measuring progress and revenue recognition is based on the restated revenue and cost numbers as if IFRS 15 was applied in 2017 without restatement of 2017 comparative amounts, with the cumulative effect of applying the new standard as an adjustment to equity as at 1 January 2018.

Further details of the changes can be seen in note 11.

5. Use of estimates

The preparation of condensed interim consolidated financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expense. Actual results may differ from these estimates.

The most significant judgments made by management in preparing these condensed interim consolidated financial statements in applying PHLY's accounting policies, and the key sources of estimation uncertainty, are the same as those that are applied to the audited consolidated financial statements as of and for the year ended 31 December 2017 unless described elsewhere in this report.

Due to the limited backlog to Q1 2019, an impairment trigger has been identified for the carrying amount of property, plant and equipment. The Company has estimated the recoverable amount using the value-in-use method determined by discounted future cash flows. No impairment of property, plant and equipment balances has been recorded in 2018. The key assumption applied in this assessment is dependent on the ability of the Company to successfully obtain shipbuilding contracts (at historically consistent margins) beyond the delivery of Hull 030 in Q1 2019. Whilst the Company is actively working on securing new orders there can be no assurance that Philly Shipyard will successfully obtain new orders.

6. Tax estimates

Income tax expense is recognized in each interim period based on the best estimate of the expected annual income tax rates. Due to the limited backlog to Q1 2019, deferred tax assets of USD 3.5 million was impaired in Q4 2018.

7. Share capital and equity

At 31 December 2018 and 31 December 2017, PHLY had 12,107,901 ordinary shares (excluding 466,865 own shares) at a par value of NOK 10 per share. There were no share issuances or repurchases for the quarters or for the years ended 31 December 2018 or 31 December 2017. Accordingly, 12,107,901 ordinary shares was used in the calculation of earnings per share for the quarters and for the years ended 31 December 2018 and 31 December 2017.

8. Interest-bearing debt

The following shows material changes in interest-bearing debt during 2018:

Amounts in USD millions	Non-current debt	Current debt	Total interest-bearing debt
Balance 31 December 2017	**59.4**	**0.2**	**59.6**
Repayment of debt	-	(0.2)	(0.2)
Reclass of debt	0.2	-	0.2
Balance 31 December 2018	**59.6**	-	**59.6**

PSI has a secured term loan of up to USD 60.0 million (USD 59.6 million on the statement of financial position which is the loan amount net of unamortized loan fees) with PIDC Regional Center, LP XXXI, a partnership between CanAm Enterprises and the Philadelphia Industrial Development Corporation (PIDC). The loan has a fixed interest rate of 2.625% per annum through maturity. The loan matures in March 2020. This loan was made through the Welcome Fund loan program, a source of low-cost capital generally available to commercial, retail, industrial and non-profit firms that create significant job growth and are located in or planning to locate to the City of Philadelphia. The loan has a five-year term and is secured by a first lien on: (1) USD 39.7 million of cash collateral; (2) PSI's shares in its wholly-owned subsidiary, APSI Tanker Holdings II LLC (ATH II), representing 100% of the total outstanding shares of ATH II as of 31 December 2018; and (3) ATH II's shares in Philly Tankers AS (PTAS), representing 53.7% of the total outstanding shares of PTAS as of 31 December 2018. The loan also contains a covenant restricting dividends and other distributions by ATH II until an additional USD 13.1 million of cash collateral has been deposited to secure the loan. It is expected that the additional USD 13.1 million of cash collateral will be deposited to secure the loan in Q1 2019 in connection with the liquidation of PTAS. USD 60.0 million is drawn under this term loan at 31 December 2018.

PSI has an unsecured three-year revolving credit facility for up to USD 10.0 million from TD Bank, N.A. The facility terminates in April 2019. The loan accrues interest at 30-day LIBOR plus 2.50% per annum as defined in the credit agreement. USD 0.7 million of this facility was utilized as of 31 December 2018 for the issuance of letters of credit.

9. Related party transactions

Aker Capital AS, a wholly-owned subsidiary of Aker ASA, is the majority shareholder of PHLY, owning 57.6% of its total outstanding shares as of 31 December 2018. In addition, Kristian Røkke, the Deputy Chairman of the Board of Directors of PHLY, is a Board member of TRG Holding AS, which owns 66.7% of the total outstanding shares of Aker ASA as of 31 December 2018.

Philly Shipyard has service agreements with Aker ASA and certain of its affiliates which provide specified consulting, tax, financial and administrative services. All payables under these agreements are paid within the normal course of business. Philly Shipyard believes that related party transactions are made on terms equivalent to those that prevail in arm's length transactions.

Related administrative costs and financial statement amounts for the three-month period ending 31 December 2018 were USD 30 thousand (USD 30 thousand for the same period in 2017) and for the year ending 31 December 2018 were USD 120 thousand (USD 120 thousand for the same period in 2017).

PSI entered into an administrative services agreement with Philly Tankers LLC (PTLLC) whereby PSI will supply certain administrative services to PTLLC. Related revenues for the three-month period ending 31 December 2018 were USD 30 thousand (USD 30 thousand for the same period in 2017) and for the year ending 31 December 2018 were USD 120 thousand (USD 120 thousand for the same period in 2017). As part of the liquidation of Philly Tankers, this administrative services agreement was assigned by PTLLC to Philly Tankers AS (PTAS) on 31 May 2018.

10. Capitalized interest

	Q4		Twelve Months Ended 31 Dec.	
Amounts in USD millions	**2018**	**2017**	**2018**	**2017**
Interest expense	(0.5)	(1.1)	(1.9)	(5.3)
Interest capitalized on construction contracts	-	0.5	-	3.4
Net interest expense	**(0.5)**	**(0.6)**	**(1.9)**	**(1.9)**

11. Construction contracts

The order backlog is USD 17.4 million at 31 December 2018 and represents a contractual obligation to deliver vessels that have not yet been produced for the Company's customer (Matson). Order backlog consists of future contract revenues and is subject to adjustment based on change orders as defined in the construction contracts.

Amounts in USD millions	**Order backlog 31 Dec. 2018**	**Order intake 12 months to 31 Dec. 2018**	**Order backlog 31 Dec. 2017**
	17.4	**(0.9)**	**187.7**

The loss recognized on long-term contracts in process (Hulls 029-030) as of 31 December 2018 is as follows:

Amounts in USD millions	**Actual 31 Dec. 2018**	**Restated IFRS 15 31 Dec. 2017**	**Adjustment Q1 2018**
Contract revenue recognized to date	389.8	260.1	(38.4)
Less: contract expenses recognized to date	(400.9)	(260.1)	38.4
Loss recognized to date (Hulls 029-030)	**(11.1)**	**-**	**-**

Total incurred contract expenses as of 31 December 2017 can be specified as follows:

Contract expenses charged to profit and loss according to IAS 11	221.7
Incurred contract expenses included in the balance	38.4
Total incurred contract expenses thru 31 December 2017	**260.1**
Contract costs incurred thru 31 December 2018 (Hulls 029-030)	**404.6**

Contract revenue and loss recognized to date includes revenue and loss for Hulls 029-030 since the contract for these vessels is accounted for using the principle-over-time revenue recognition method according to IFRS 15.

The progress and the revenue recognition thru 31 December 2018 is the difference between the accumulated revenue per 31 December 2018 and the restated accumulated revenue per 31 December 2017.

The adjustment in Q1 2018 is due to cost incurred in 2017 that was included in the statement of financial position as work-in-process according to IAS 11, but according to IFRS 15 will be expensed with a corresponding increase in revenue. The adjusted revenue and cost for 2017 include the costs presented in the statement of financial position as work-in-process as of 31 December 2017.

The total revenues to be recognized for this contract starting 1 January 2018 through delivery of Hull 030 will be USD 38.4 million lower due to this change in IFRS 15. There is no change in the contractual amount to be received from the Company's customer (Matson).

100% of the revenue, cost and profit for each of Hulls 025-028 was recognized at its delivery in Q4 2016, Q1 2017, Q3 2017 and Q4 2017, respectively. This accounting treatment was required for Hulls 025-028 because there were no external customers at the time these contracts were signed and shipbuilding activities commenced, and these vessels were considered as built for its own account.

As of 31 December 2018, the Company has one contract in progress that is accounted for using the POC method. During 2018, the Company was building two containerships for Matson: Hull 029 delivered in Q4 2018 and Hull 030 scheduled to be delivered in Q1 2019. These vessels are based on a prototype design and the Company last delivered a containership in 2006. Accordingly, there is a higher technical design risk and a higher project execution risk compared to the recent construction of multiple product tankers, which were based on a proven design. This prototype risk increases the current construction cost estimation uncertainty and the likelihood of occurrence of contract contingencies. Philly Shipyard recognizes contract revenues and expenses for the two-containership order from Matson as one project. As of 31 December 2018, the Matson project is approximately 95% complete. The estimated contract loss is provided for as of Q4 2018.

Customer milestone payments as of 31 December 2018 and 31 December 2017 totaled USD 391.8 million and USD 253.8 million, respectively.

Customer advances, net as of 31 December 2018 and 31 December 2017 totaled USD 1.2 million and USD 0, respectively.

Vessels-under-construction receivable as of 31 December 2018 and 31 December 2017 totaled USD 0 and USD 7.3 million, respectively. As of 31 December 2018, vessels-under-construction receivable represents the difference between costs incurred for the Matson vessels (Hulls 029-030) and customer advances received from Matson for those vessels.

Work-in-process as of 31 December 2018 and 31 December 2017 totaled USD 0 and USD 13.4 million, respectively. Work-in-process related to non percentage-of-completion accounting projects is presented gross (where costs incurred are presented as a work-in-process asset, and payments from customers received are presented as customer advances, net liability). Percentage-of-completion accounted projects are presented net.

In 2018, the project to build up to four containerships (CV3700 vessels) for delivery to TOTE Maritime was cancelled and, in connection therewith, the full amount of the work-in-process assets pertaining to the first two CV3700 vessels (Hulls 031-032), totaling USD 17.6 million, was written off. USD 17.3 million of this impairment charge was taken in Q3 2018 and the remaining USD 0.3 million of this impairment charge was taken in Q4 2018.

As of 31 December 2018, PSI has non-cancellable purchase commitments for materials and equipment of approximately USD 4.6 million for the construction of Hulls 029-030.

12. Operating revenues and other income

	Q4		Twelve Months Ended 31 Dec.	
Amounts in USD millions	**2018**	**2017**	**2018**	**2017**
Operating revenues	19.2	191.6	129.7	591.8
Profit/(loss) in equity-accounted investments (Hulls 025-028)	0.2	6.8	(0.5)	19.6
Recognized deferred net gain in equity-accounted investments (Hulls 025-028)	-	0.3	-	3.2
Operating revenues and other income	**19.4**	**198.7**	**129.2**	**614.6**

Profit/(loss) in equity-accounted investments (Hulls 025-028) represents the Company's 53.7% share of the total comprehensive profit/(loss) of Philly Tankers, which for the years ending 31 December 2018 and 31 December 2017 amounted to a loss of USD 0.5 million and a profit of USD 19.6 million, respectively.

Recognized deferred net gain in equity-accounted investments (Hulls 025-028) represents the Company's USD 4.7 million net gain that was deferred on the issuance of Philly Tankers shares in July 2014 to external parties at a price exceeding the Company's cost basis, which for the full years ending 31 December 2018 and 31 December 2017 amounted to USD 0 and USD 3.2 million, respectively. USD 1.4 million was fully recognized at delivery of Hull 026 in Q1 2017, USD 1.5 million was fully recognized at delivery of Hull 027 in Q3 2017 and USD 1.5 million was fully recognized at delivery of Hull 028 in Q4 2017, reduced with recognition of a USD 1.2 million deferred transaction cost in Q4 2017.

13. Financial instruments

As of 31 December 2018, the Company had no forward exchange contracts or other financial instruments.

14. Commitments and contingencies

Pursuant to the shipyard lease between PSI and Philadelphia Shipyard Development Corporation (PSDC), if PSI fails to maintain an average of at least 200 full-time employees at the shipyard for 90 consecutive days, then the lease term (i.e., a 99-year lease with 80 years remaining including options) is automatically converted to month-to-month and PSDC has the right to terminate the lease, subject to the right of PSI to complete work-in-process projects and a one-time, limited cure right which allows PSI to restore the lease to a five-year term under certain circumstances. Philly Shipyard expects that this minimum employment condition will not be triggered as long as there is continuous shipbuilding activity at the shipyard. Due to the gap in shipbuilding activity following the delivery of the last vessel in its order backlog (Hull 030), which is scheduled in Q1 2019, Philly Shipyard has obtained a temporary waiver of this minimum employment condition until 31 December 2019.

15. Use and reconciliation of non-GAAP financial measures

	Q4		Twelve Months Ended 31 Dec.	
	Unaudited		Unaudited	
Amounts in USD millions	**2018**	**2017**	**2018**	**2017**
EBITDA	(3.4)	39.3	(33.4)	105.1
(less)/plus: (profit)/loss in equity-accounted investments (Hulls 025-028)	(0.2)	(6.8)	0.5	(19.6)
plus: deferred shipbuilding profits (Hulls 025-028)	-	1.4	-	30.9
plus: capitalized Welcome Fund interest expense	-	-	-	0.2
less: recognized shipbuilding profits previously deferred (Hulls 025-028)	-	(23.5)	-	(71.9)
less: recognized deferred net gain in equity-accounted investments (Hulls 025-028)	-	(0.3)	-	(3.2)
Adjusted EBITDA	**(3.6)**	**10.1**	**(32.9)**	**41.5**

Non-GAAP financial measures are defined as numerical measures that either exclude or include amounts that are not excluded or included in the comparable measures calculated and presented in accordance with GAAP (i.e. IFRS).

The following financial measure may be considered a non-GAAP financial measure:

Adjusted EBITDA, which is defined as EBITDA (i.e., earnings before interest, taxes, depreciation and amortization) plus capitalized Welcome Fund interest expense plus or minus net deferred shipbuilding profits plus or minus loss or profit, respectively, in equity-accounted investments minus recognition of deferred net gain on equity-accounted investments.

The Company has made adjustments to EBITDA to reflect shipbuilding activities (1) as if Philly Shipyard had no shipping investments, (2) as if profit was recognized on Hulls 025-028 using the percentage of completion method of accounting and (3) to adjust for capitalized interest expense on long-term debt. The Company believes presenting Adjusted EBITDA is useful to investors as it provides another measure of Philly Shipyard's profitability from its operations, as if Philly Shipyard never had any shipping investments, and more closely represents earnings from shipbuilding activities.

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