Philly Shipyard ASA (OSE: PHLY)
Q4 2017 and Full Year 2017 Results

15 February 2018

Highlights

- ✓ Philly Shipyard delivered the final vessel (Hull 028) of a series of four product tankers to Kinder Morgan, as assignee of Philly Tankers, 10 days ahead of its contract delivery date
- ✓ As of 31 December 2017, the four-product tanker order for Kinder Morgan is 100% complete and the two-containership order for Matson is approximately 54% complete
- ✓ Fourth quarter and full year 2017 net income of USD 31.5 million and USD 68.0 million, respectively, compared to USD 19.3 million and 38.7 million in the same periods in 2016
- ✓ Total cash and cash equivalents of USD 110.1 million at 31 December 2017, excluding USD 13.2 million of restricted cash securing a loan
- ✓ Order backlog of USD 187.7 million on 31 December 2017

Subsequent Events

- ✓ Philly Shipyard placed the TOTE containership project on hold and is considering alternative projects

Operations and Shipping Investments

Vessel Construction

On 20 November 2017, Philly Shipyard delivered Hull 028, the final product tanker in the four-ship order for Philly Tankers, a Jones Act shipping company that is majority-owned (but not controlled) by Philly Shipyard. This vessel was delivered to Kinder Morgan, as assignee of Philly Tankers, ten days before its contract delivery date.

At the end of the fourth quarter of 2017, Philly Shipyard was building two containerships under contract with Matson (Hulls 029-030). During Q4 2017, the main engine was installed on Hull 029 and production activities continued on Hull 030.

In addition, during Q4 2017, Philly Shipyard continued design, planning and procurement activities related to the construction of up to four additional state-of-the-art, cost-effective and environment-friendly vessels for the Hawai'i containership trade. By year-end, Philly Shipyard had ordered all major long-lead items for the first pair of these vessels (Hulls 031-032). During Q1 2018, this project was placed on hold and the Letter of Intent (LOI) between Philly Shipyard and TOTE for the construction and sale of these vessels expired in accordance with its terms. For more details regarding this project, please see the Outlook discussion below.

While Philly Shipyard continues to actively seek the new orders and capital necessary to build Hulls 031 and 032, the delay it has experienced thus far has caused it, and will continue to cause it, to experience a slow-down of various departments. Due to this interruption of Philly Shipyard's building program, it is necessary to temporarily cease certain operations and place some employees in a layoff status. Accordingly, Philly Shipyard has reduced and will continue to adjust its workforce in line with its backlog.

Shipping Investments

In 2015, Philly Shipyard entered into definitive agreements to sell its future interests in the four-ship Philly Shipyard-Crowley joint venture (Hulls 021-024) to a subsidiary of Marathon Petroleum Corporation (Marathon). The closing of the sale of Philly Shipyard's interest with respect to each of Hulls 021-024 occurred at its delivery. As of the delivery of Hull 024 in Q3 2016, Philly Shipyard had sold all of these joint venture interests to Marathon and recognized all of the income from these sales.

Additionally, in 2015, Philly Tankers entered into definitive agreements to sell its four shipbuilding contracts with Philly Shipyard (Hulls 025-028) and related assets to Kinder Morgan. The closing of the sale of Philly Tankers' shipping assets with respect to each of Hulls 025-028 occurred at its delivery. With the delivery of Hull 028 in

Q4 2017, Philly Tankers has successfully divested all of its shipping assets and intends to initiate a liquidation process promptly.

To date, the dividends paid by Philly Tankers to its shareholders total USD 76.7 million (including USD 2.6 million in Q4 2017), and Philly Shipyard's share of those dividends totals USD 41.2 million, of which USD 39.9 million was received by end of 2017 and USD 1.3 million was received in the beginning of January 2018. On 19 October 2017, Philly Tankers announced that it will not make any further dividend payments before liquidation other than any dividends necessary to cover U.S. tax withholding payments on behalf of its non-U.S. shareholders due at an earlier time. In this announcement, Philly Tankers stated its belief that this is the most cost-efficient and tax-efficient manner to distribute its capital to its shareholders

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 2017 was 0.98 compared to 1.10 at the end of Q4 2016. 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 2017 was 4.43 compared to 3.31 at the end of Q4 2016. Philly Shipyard continues to work proactively to further improve safety and reduce the number of incidents at the shipyard.

Financial Information

Fourth Quarter and Full Year 2017 Results

Operating revenues and other income for the fourth quarter of 2017 were USD 199.9 million compared to operating revenues and other income of USD 145.6 million for the fourth quarter of 2016. Q4 2017 operating revenues and other income were driven by the delivery by Philly Shipyard of Hull 028 to Kinder Morgan, the related sale by Philly Tankers of its Hull 028 shipping assets to Kinder Morgan (profit and deferred gain from equity-accounted investees) and continued progress on the Matson vessels (Hulls 029-030). In contrast, Q4 2016 operating revenues and other income were primarily driven by the delivery by Philly Shipyard of Hull 025 to Kinder Morgan, the related sale by Philly Tankers of its Hull 025 shipping assets to Kinder Morgan (profit and deferred gain from equity-accounted investees) and continued progress on the Matson vessels (Hulls 029-030). There was substantially more progress on the Matson project in Q4 2017 than Q4 2016; this difference contributed to the significant increase in operating revenues and other income in Q4 2017 compared to Q4 2016.

Net income for Q4 2017 was USD 31.5 million compared to net income of USD 19.3 million for Q4 2016.

As previously disclosed, under International Financial Reporting Standards (IFRS), (1) with respect to each of Hulls 021-024, 49.9% of the profit on such vessel was deferred, and the total estimated deferred margin for all four vessels was recognized pro-rata (25% per ship) at delivery, and (2) with respect to each of Hulls 025-028, 100% of the revenue, cost and profit on such vessel was deferred, and the deferred amounts for each vessel were recognized at delivery. This accounting treatment is required for Hulls 021-024 because, at the time the Philly Shipyard-Crowley joint venture was formed, it was contemplated that Philly Shipyard would maintain 49.9% of the economic benefits once the vessels were delivered. This accounting treatment is required for Hulls 025-028 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 an economic interest in the Philly Shipyard-Crowley joint venture vessels or investment in Philly Tankers, and more closely represents earnings from shipbuilding activities.

EBITDA for the fourth quarter of 2017 was USD 40.4 million compared to EBITDA of USD 34.0 million in the fourth quarter of 2016. The increase in EBITDA was mainly driven by a reduction in the estimate for post-delivery costs for the Philly Tankers vessels delivered earlier in 2017. In addition, the allocated depreciation expense relating to the construction of Hulls 026-028 during 2017 was reclassified to the cost-of-vessels expense line

[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 investees minus recognized deferred gain in equity-accounted investees.

and recognized in Q4 2017. Adjusted EBITDA for the fourth quarter of 2017 was USD 10.0 million compared to Adjusted EBITDA of USD 23.2 million in the fourth quarter of 2016. The decrease in Adjusted EBITDA was driven primarily by the significantly lower margin on the Matson project than the Philly Tankers project.

Net financial items in Q4 2017 was a loss of USD 0.4 million compared to a loss of USD 2.5 million in Q4 2016. The loss on account of net financial items in Q4 2017 was mainly due to USD 0.6 million of net interest expense items whereas the loss on account of net financial items in Q4 2016 was mainly due to a USD 2.0 million loss on foreign exchange forward contracts.

Operating revenues and other income in 2017 ended at USD 615.8 million compared to operating revenues and other income of USD 233.6 million in 2016. 2017 full year operating revenues and other income were primarily driven by the delivery by Philly Shipyard of Hull 026, Hull 027 and Hull 028 to Kinder Morgan, 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 investees) and continued progress on the Matson vessels (Hulls 029-030). In contrast, 2016 full year operating revenues and other income were primarily driven by the delivery by Philly Shipyard of Hull 025 to Kinder Morgan, the related sale by Philly Tankers of its Hull 025 assets to Kinder Morgan, the remaining progress on the Philly Shipyard-Crowley joint venture vessels (Hulls 021-024) along with the sale of the shipping assets pertaining to Hulls 023 and 024 to Marathon and continued progress on the Matson vessels (Hulls 029-030). The main driver for the significant increase in operating revenues and other income in 2017 versus 2016 is that Philly Shipyard recognized 100% of the revenue and other income on three product tankers (i.e., Hulls 026, 027 and 028) in 2017, compared to only one product tanker (i.e., Hull 025) in 2016. Additionally, there was substantially more progress on the Matson project in 2017 than 2016.

Net income for full year 2017 was USD 68.0 million compared to net income of USD 38.7 million for full year 2016.

EBITDA for full year 2017 was USD 106.2 million compared to EBITDA of USD 70.4 million for full year 2016. The allocated depreciation expense relating to the construction of Hulls 026-028 during 2017 was reclassified to the cost-of-vessels expense line and recognized in Q4 2017. Adjusted EBITDA in 2017 totaled USD 41.4 million compared to Adjusted EBITDA of USD 87.1 million in the same period of 2016. The decrease in Adjusted EBITDA was driven primarily by the significantly lower margin on the Matson project than the Philly Tankers project.

Balance Sheet

Total assets were USD 255.8 million at 31 December 2017 compared to USD 408.8 million at 31 December 2016. The decrease in total assets was primarily driven by decreases in work-in-process and vessels-under-construction receivable, which decreased from a combined USD 180.3 million to a combined USD 20.7 million due to delivery of the Philly Tankers vessels.

Total debt was USD 59.6 million at 31 December 2017 compared to total debt of USD 157.5 million at 31 December 2016. The net decrease was mainly due to the repayment in full of the outstanding Caterpillar loans for Hulls 026 and 027. The Caterpillar loan facility is described under Financing below.

Cash and cash equivalents (excluding restricted cash) were USD 110.1 million at 31 December 2017, compared to USD 69.1 million at 31 December 2016. The increase of USD 41.0 million was due primarily to the delivery of Hulls 026, 027 and 028 to Kinder Morgan along with dividends paid by Philly Tankers to Philly Shipyard as well as additional customer payments made by Matson on Hulls 029 and 030. As of 31 December 2017, restricted cash consisted of USD 13.2 million related to the Welcome Fund loan, which is expected to be released in 2020 when the loan matures.

Total equity increased to USD 156.4 million at 31 December 2017 from USD 91.4 million at 31 December 2016 due to the net income of USD 68.0 million slightly reduced by the dividend paid of USD 3.0 million in Q1 2017.

Financing

The Company had a secured USD 150.0 million loan facility with Caterpillar Financial Services Corporation (Cat Financial), subject to a maximum borrowing amount of USD 75.0 million per vessel, for construction financing on Hulls 025-028. This facility was repaid in full and terminated upon the delivery of Hull 028 on 20 November 2017.

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 2017.

The Company also has an unsecured three-year revolving credit facility for up to USD 10.0 million from TD Bank, N.A, which automatically reduced from a maximum of USD 20.0 million on 1 May 2017. The facility terminates in April 2019. USD 1.2 million of this facility was utilized as of 31 December 2017 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

The contract with Matson (Hulls 029-030) provides for shipbuilding activity with delivery dates through Q1 2019. As of 31 December 2017, Philly Shipyard had an order backlog of USD 187.7 million.

Philly Shipyard achieved record high revenues and profits in 2017. The main drivers of the record high revenues were the deliveries of three product tankers (Hulls 026-028) to Kinder Morgan, as well as continued progress on two containerships (Hulls 029-030) for Matson. While there was no profit on the Matson project in 2017, Philly Shipyard recognized 100% of the profit (including profit and deferred gain from equity-accounted investees) on Hulls 026-028 in 2017.

In contrast, Philly Shipyard expects it will recognize revenues in 2018 only for the continued progress on the Matson project (Hulls 029-030) and potentially some initial progress on contracts for new vessel construction projects, if and when secured, provided that revenue recognition over time is allowed for such other contracts under the new IFRS 15 standard. The revenues in 2018 will in any case be significantly lower than in 2017. Philly Shipyard expects that the margin contribution from the Matson project and any other vessel construction projects to be recognized in 2018 will not be significant and will be lower than S,G&A and other overhead costs not allocated to projects for 2018.

The key focus area for Philly Shipyard's operations is continued progress on the containerships under construction for Matson. In addition, the main focus areas for Philly Shipyard's business are securing new contracts to expand its order backlog beyond Hull 030 and seeking capital to finance the construction of new vessels. As noted in the Vessel Construction discussion above, the delay Philly Shipyard has already experienced in securing this new business and financing has interrupted its building program, causing Philly Shipyard to temporarily halt certain operations and lay-off some employees.

In July 2017, Philly Shipyard and TOTE entered into a Letter of Intent (LOI) for the construction and sale of up to four new, cost-efficient and eco-friendly containerships for the Hawai'i trade, with planned deliveries for the first pair (Hulls 031-032) in 2020 and the second pair (Hulls 033-034) in 2021. In order to support this timetable, and minimize the gap in its shipbuilding activities, Philly Shipyard initiated design, planning and procurement activities for these vessels.

However, in January 2018, TOTE announced that its plans to enter the U.S. mainland to Hawai'i containership service are on hold as a result of its Phase 1 technical review of Piers 1 and 2 in Honolulu Harbor. These two piers, along with 40+ acres of adjacent land, had been assigned to TOTE by the Hawai'i Department of Transportation (HDOT) for TOTE's access and use commencing in 2020, to coincide with the planned start of TOTE's new operations in Hawai'i. According to TOTE's release, its preliminary study of the site's infrastructure indicated that this terminal space will require upgrades and improvements to accommodate TOTE's new Hawai'i service.

Due to the scope and timing of these upgrades and improvements, the LOI was allowed to expire in accordance with its terms on 31 January 2018. TOTE, however, noted in its release that it continues to be open to working with HDOT to update plans and a timeline for access to a deep-water terminal in Honolulu Harbor that would allow TOTE to launch its new Hawai'i service.

Based on these developments, Philly Shipyard's project to build Hulls 031-034 as containerships was put on hold. Philly Shipyard has suspended substantially all construction-related activities on these vessels. As previously disclosed, Philly Shipyard has placed orders for all major long-lead items for the first pair, enabling a rapid start-up if conditions permit. If these orders were to be cancelled, then the cancellation costs would be substantially lower than the value of the orders placed.

Philly Shipyard intends to resume this project when there is more clarity regarding the new order situation and related capital requirements. Accordingly, Philly Shipyard is exploring alternatives in order to secure contracts and financing for these vessels. In addition, Philly Shipyard is continuing to pursue potential new construction projects for other types of Jones Act vessels.

Among other endeavors, Philly Shipyard has teamed with Fincantieri Marine Group and Vard Marine to compete for the detail design and construction of the U.S. Coast Guard’s next generation heavy polar icebreaker. In support of this effort, the team is participating in a government funded industry study to develop a baseline icebreaker design, cost estimate, and project schedule and refine key vessel features and performance requirements.

Shipping

As Philly Shipyard and Philly Tankers completed definitive documentation in 2016 to divest their shipping assets related to Hulls 021-028, they will no longer have exposure to these vessels in service. These transactions streamlined the business and marked a successful conclusion to an innovative plan to invest in eight Jones Act product tankers with an approximate contract value of USD 1.0 billion through the Philly Shipyard-Crowley joint venture (Hulls 021-024) and Philly Tankers (Hulls 025-028). 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

The delay Philly Shipyard has experienced in securing new contracts and financing for work after the last vessel in the current backlog (Hull 030) has interrupted its building program, causing Philly Shipyard to temporarily halt certain operations and lay-off some employees. If this delay continues, then it will further interrupt Philly Shipyard’s building program and increase the risks faced by Philly Shipyard, including challenges related to attracting and retaining skilled workers at current forecasted rates. In addition, because multiple vessels are in production at any one time, lack of a continued firm backlog may cause operational inefficiencies for completion of the remaining vessels in the current backlog.

Philly Shipyard faces additional risks if it is unable to secure new orders and/or financing for vessels after Hull 030. There can be no assurance that Philly Shipyard will obtain new orders or financing for these vessels. If the shipyard fails to obtain new orders or financing for these vessels before the Matson project is substantially complete, then it is expected that the Company would incur significant expenses (including cancellation costs for long-lead items) and it would be challenging for Philly Shipyard to continue operations after delivery of Hull 030, which is scheduled in Q1 2019.

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.

During 2018, Philly Shipyard will continue to transition from building a series of tankers to building prototype container vessels. Management views the container vessels as a higher risk since Philly Shipyard’s main activity during the last ten years has been building tankers and the last container vessel built by Philly Shipyard was delivered 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 increases the current construction cost estimation uncertainty. In addition, due to the break-even projected margin on Hulls 029 and 030, there is a risk of a loss-making project.

For a further analysis of risks, please refer to the Company’s 2016 annual report.

Oslo, Norway
15 February 2018
Board of Directors and Chief Executive Officer
Philly Shipyard ASA

CONDENSED CONSOLIDATED INCOME STATEMENT

Amounts in USD millions (except number of shares and earnings per share)	Q4 Unaudited 2017	Q4 2016	Full Year Ended 31 Dec. Unaudited 2017	Full Year Ended 31 Dec. 2016
Operating revenues and other income	199.9	145.6	615.8	233.6
Operating expenses	(159.5)	(111.6)	(509.6)	(163.2)
Operating income before depreciation - EBITDA	**40.4**	**34.0**	**106.2**	**70.4**
Depreciation	2.5	(2.7)	(5.8)	(3.6)
Operating income - EBIT	**42.9**	**31.3**	**100.4**	**66.8**
Net financial items	(0.4)	(2.5)	0.6	1.5
Income before tax	**42.5**	**28.8**	**101.0**	**68.3**
Tax expense	(11.0)	(9.5)	(33.0)	(29.6)
Income after tax **	**31.5**	**19.3**	**68.0**	**38.7**
Weighted average number of shares	**12,107,901**	**12,107,901**	**12,107,901**	**12,107,901**
Basic and diluted earnings per share (USD)	**2.61**	**1.59**	**5.62**	**3.19**

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Amounts in USD millions	Q4 Unaudited 2017	Q4 2016	Full Year Ended 31 Dec. Unaudited 2017	Full Year Ended 31 Dec. 2016
Income after tax	31.5	19.3	68.0	38.7
Other comprehensive income, net of income tax	-	-	-	-
Total comprehensive income for the period **	**31.5**	**19.3**	**68.0**	**38.7**

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

Amounts in USD millions	Unaudited 31 Dec. 2017	31 Dec. 2016 *
Assets		
Non-current assets		
Property, plant and equipment	50.1	50.6
Restricted cash	13.2	13.1
Deferred tax asset long-term	-	16.6
Equity-accounted investees	48.4	64.3
Other non-current assets	0.4	0.3
Total non-current assets	**112.1**	**144.9**
Current assets		
Vessels-under-construction receivable	7.3	-
Work-in-process	13.4	180.3
Restricted cash	-	7.0
Prepayments and other receivables	4.5	5.7
Deferred tax asset short-term	2.5	-
Income tax receivable	5.9	1.8
Cash and cash equivalents	110.1	69.1
Total current assets	**143.7**	**263.9**
Total assets	**255.8**	**408.8**
Equity and liabilities		
Total equity	**156.4**	**91.4**
Non-current liabilities		
Interest-bearing long-term debt	59.4	59.3
Deferred tax liability long-term	2.7	1.0
Total non-current liabilities	**62.1**	**60.3**
Current liabilities		
Trade payables, accrued liabilities and provisions	36.1	58.9
Income tax payable	1.0	2.1
Interest-bearing short-term debt	0.2	0.2
Construction loans	-	98.0
Customer advances, net	-	97.9
Total current liabilities	**37.3**	**257.1**
Total liabilities	**99.4**	**317.4**
Total equity and liabilities	**255.8**	**408.8**

* Annual 2016 financial information is derived from audited financial statements.

** All attributed to the equity holders of PHLY.

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Full Year Ended 31 Dec.	
	Unaudited	
Amounts in USD millions	**2017**	**2016**
As of beginning of period	91.4	143.4
Dividend paid	(3.0)	(90.7)
Total comprehensive income for the period *	68.0	38.7
As of end of period	**156.4**	**91.4**

CONDENSED CONSOLIDATED CASH FLOW STATEMENT

	Full Year Ended 31 Dec.	
	Unaudited	
Amounts in USD millions	**2017**	**2016**
Net cash from operating activities	109.9	28.2
Investment in property, plant and equipment	(8.1)	(8.5)
Dividend received from equity-accounted investees	39.9	-
Investment in equity-accounted investees	-	(7.7)
Sale of shipping assets, net of transaction costs	-	22.7
Net cash from investing activities	31.8	6.5
Proceeds from interest-bearing debt	0.3	0.2
Repayment of interest-bearing debt	-	(14.0)
Proceeds from construction loans	127.0	260.0
Repayment of construction loans	(225.0)	(191.0)
Dividend paid	(3.0)	(90.7)
Net cash used in financing activities	(100.7)	(35.5)
Net change in cash and cash equivalents	**41.0**	**(0.8)**
Cash and cash equivalents at beginning of period	69.1	69.9
Cash and cash equivalents at end of period	**110.1**	**69.1**

* All attributed to the equity holders of PHLY.

Notes to the condensed interim consolidated financial statements for the fourth quarter and full year for 2017

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 and full year periods ended 31 December 2017 and 31 December 2016 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 2016, 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 and full year periods are not necessarily indicative of the results that may be expected for any subsequent quarter or year.

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 2016.

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 2016.

   There have not been any new IFRS standards or interpretations which were effective 1 January 2017 that have had a significant impact on Q4 2017 or full year 2017. PHLY has analyzed how the new IFRS 15 standard - Revenue from Contracts with Customers (effective 1 January 2018) - potentially will impact its current contract with Matson. The conclusion is that the new IFRS 15 standard will not change the way revenues have been recognized for the Matson contract.

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 2016 unless described elsewhere in this report.

6. **Tax estimates**
   Income tax expense is recognized in each interim period based on the best estimate of the expected annual income tax rates.

7. **Share capital and equity**
   At 31 December 2017 and 31 December 2016, 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 fourth quarters or for the full years ended 31 December 2017 or 31 December 2016. Accordingly, 12,107,901 ordinary shares were used in the calculation of earnings per share for the fourth quarters and for the full years ended 31 December 2017 and 31 December 2016.

8. **Interest-bearing debt**
   The following shows material changes in interest-bearing debt during 2017:

Amounts in USD millions	Non-current debt	Current debt	Total interest-bearing debt
Balance 31 December 2016	**59.3**	**98.2**	**157.5**
Proceeds from borrowings	-	127.0	127.0
Repayment of debt	-	(225.0)	(225.0)
Reclass of debt	0.1	-	0.1
Balance 31 December 2017	**59.4**	**0.2**	**59.6**

The Company had a loan agreement with Caterpillar Financial Services Corporation (Cat Financial) for a USD 150.0 million loan facility, subject to a maximum borrowing amount of USD 75.0 million per vessel, for construction financing on Hulls 025-028. The loan was secured by a first lien on Hulls 025-028. The loan accrued interest at three-month LIBOR plus 3.0% per annum as defined in the loan agreement. This facility was repaid in full and terminated upon the delivery of Hull 028 on 20 November 2017.

PSI has a secured term loan of up to USD 60.0 million (USD 59.4 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 or 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 13.1 million of cash collateral; (2) PSI's shares in its wholly-owned subsidiary, APSI Tanker Holdings II LLC (ATH II); and (3) ATH II's shares in Philly Tankers AS. The loan also contains a covenant restricting dividends and other distributions by ATH II until an additional USD 39.3 million of cash collateral has been deposited to secure the loan. USD 60.0 million is drawn under this term loan at 31 December 2017.

The Company has an unsecured three-year revolving credit facility for up to USD 10.0 million from TD Bank, N.A., which automatically reduced from a maximum of USD 20.0 million on 1 May 2017. 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 1.2 million of this facility was utilized as of 31 December 2017 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 2017.

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 2017 were USD 30 thousand (USD 30 thousand for the same period in 2016) and for the full year ending 31 December 2017 were USD 120 thousand (USD 120 thousand for the same period in 2016).

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 2017 were USD 30 thousand (USD 30 thousand for the same period in 2016) and for the full year ending 31 December 2017 were USD 120 thousand (USD 120 thousand for the same period in 2016).

10. Capitalized interest

	Q4		Full Year Ended 31 Dec.	
Amounts in USD millions	**2017**	**2016**	**2017**	**2016**
Interest expense	(0.9)	(1.7)	(4.9)	(4.5)
Interest capitalized on construction contracts	0.5	1.2	3.4	3.5
Net interest expense	**(0.4)**	**(0.5)**	**(1.5)**	**(1.0)**

11. Construction contracts

The order backlog is USD 187.7 million at 31 December 2017 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. 2017	Order intake 12 months to 31 Dec. 2017	Order backlog 31 Dec. 2016
	187.7	**(4.0)**	**784.4**

The profit recognized on long-term contracts in process (Hulls 029-030) as of 31 December 2017 is as follows:

Amounts in USD millions	31 Dec. 2017
Contract revenue recognized to date	221.7
Less: contract expenses recognized to date	(221.7)
Profit recognized to date (Hulls 029-030)	**-**
Contract costs incurred to date (Hulls 029-030)	**260.1**

Contract revenue and profit recognized to date includes revenue and profit for Hulls 029-030 since the contract for these vessels is accounted for as a long-term construction contract. 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.

As of 31 December 2017, the Company has one contract in progress that is accounted for using the percentage of completion method. The Company is building two containerships to be delivered to Matson in 2018 and 2019 (Hulls 029-030). These vessels are an all-new design and the Company last delivered a containership in 2006. Accordingly, there is a higher project execution risk compared to the recent construction of multiple product tankers, which increases the current estimation uncertainty. In addition, due to the break-even projected margin on Hulls 029 and 030, there is a risk of a loss-making project. Philly Shipyard recognizes revenues and expenses for the two-containership order from Matson as one project. As of 31 December 2017, the Matson project is approximately 54% complete.

Customer milestone payments (excluding repayment of the USD 58.0 million Philly Tankers note) as of 31 December 2017 and 31 December 2016 totaled USD 253.8 million and USD 178.1 million, respectively. Customer milestone payments pertaining to repayment of the USD 58.0 million Philly Tankers note as of 31 December 2017 and 31 December 2016 totaled USD 0 and USD 29.0 million (Hull 026), respectively.

Customer advances, net as of 31 December 2017 and 31 December 2016 totaled USD 0 and USD 97.9 million, respectively.

Vessels-under-construction receivable as of 31 December 2017 and 31 December 2016 totaled USD 7.3 million and USD 0, respectively. As of 31 December 2017, 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 2017 and 31 December 2016 totaled USD 13.4 million and USD 180.3 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. Work-in-process at year-end 2017 represents the costs incurred by Philly Shipyard on the CV3700 project (Hulls 031-032).

As of 31 December 2017, PSI has non-cancellable purchase commitments for materials and equipment of approximately USD 28.4 million for the construction of Hulls 029-030.

12. Operating revenues and other income

	Q4		Full Year Ended 31 Dec.	
Amounts in USD millions	**2017**	**2016**	**2017**	**2016**
Operating revenues	191.6	137.7	591.8	205.2
Profit in equity-accounted investees (Hulls 025-028)	6.8	6.4	19.6	6.2
Recognized deferred gain in equity-accounted investees (Hulls 025-028)	1.5	1.5	4.4	1.5
Gain-on-sale of shipping assets (Hulls 021-024)	-	-	-	20.7
Operating revenues and other income	**199.9**	**145.6**	**615.8**	**233.6**

Profit in equity-accounted investees (Hulls 025-028) represents the Company's 53.7% share of the net profit of Philly Tankers, which at full years ending 31 December 2017 and 31 December 2016 amounted to USD 19.6 million and USD 6.2 million, respectively.

Recognized deferred gain in equity-accounted investees (Hulls 025-028) represents the Company's USD 5.9 million 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 at full years ending 31 December 2017 and 31 December 2016 amounted to USD 4.4 million and USD 1.5 million, respectively. USD 5.9 million was evenly recognized at delivery of each of Hulls 025-028.

13. Financial instruments

As of 31 December 2017, the Company accounts for its forward exchange contracts with a notional value of USD 4.3 million at fair value (fair value of a USD 162 thousand asset at 31 December 2017, an improvement of USD 1.76 million from year-end 2016). These contracts are the only assets and liabilities accounted for at fair value. As disclosed in the Company’s 2016 annual report, the fair value of forward exchange contracts are determined by market observable inputs. Other than as noted above, there are no significant deviations between carrying amounts of financial assets and liabilities and their fair values due to short-term maturities.

14. Commitments and contingencies

As part of the transactions contemplated by the Authorization Agreement executed by PSI and Philadelphia Shipyard Development Corporation (PSDC) in 2011, PSI agreed to a new termination event under its shipyard lease, pursuant to which PSDC has the right to recapture the shipyard if PSI fails to maintain an average of at least 200 full-time employees at the shipyard for 90 consecutive days, 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 PSI will have at least 200 full-time employees on staff as long as there is ongoing shipbuilding activity at the shipyard.

15. Use and reconciliation of non-GAAP financial measures

	Q4		Full Year Ended 31 Dec.	
	Unaudited		**Unaudited**	
Amounts in USD millions	**2017**	**2016**	**2017**	**2016**
EBITDA	40.4	34.0	106.2	70.4
plus: capitalized Welcome Fund interest expense	-	0.3	0.2	1.2
plus: deferred shipbuilding profits (Hulls 025-028)	1.4	16.4	30.9	51.8
less: recognized shipbuilding profits (Hulls 025-028)	(23.5)	(19.6)	(71.9)	(19.6)
less: profit in equity-accounted investees (Hulls 025-028)	(6.8)	(6.4)	(19.6)	(6.2)
less: recognized deferred gain in equity-accounted investees (Hulls 025-028)	(1.5)	(1.5)	(4.4)	(1.5)
plus: deferred shipbuilding profits (Hulls 021-024)	-	-	-	5.4
less: recognized shipbuilding profits (Hulls 021-024)	-	-	-	(14.4)
Adjusted EBITDA	**10.0**	**23.2**	**41.4**	**87.1**

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 investees minus recognized deferred gain in equity-accounted investees.

The Company has made adjustments to EBITDA to reflect shipbuilding activities (1) as if Philly Shipyard had no economic interest in Hulls 021-024 or investment in Hulls 025-028, (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 an economic interest in the Philly Shipyard-Crowley joint venture vessels or investment in Philly Tankers, and more closely represents earnings from shipbuilding activities.

16. Events after 31 December 2017

On 26 January 2018, Philly Shipyard announced that it had placed the TOTE containership project on hold and is considering alternative projects. On 31 January 2018, the Letter of Intent between Philly Shipyard and TOTE expired in accordance with its terms. For more details, please see the Outlook discussion above.

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