Philly Shipyard ASA (OSE: PHLY)
Q2 2019 and Half-Year 2019 Results

15 July 2019

Key Events

- ✓ Philly Shipyard continues to pursue a mix of newbuild and repair opportunities in the commercial and government markets
- ✓ Philly Shipyard was awarded a prime contract to conduct industry studies for the Common Hull Auxiliary Multi-Mission Platform (CHAMP) program for the U.S. Navy
- ✓ Second quarter and first half 2019 operating revenues and other income of USD 0 and USD 18.9 million, respectively, compared to USD 40.4 million and USD 83.4 million in the same periods in 2018
- ✓ Second quarter and first half 2019 EBITDA of negative USD 3.3 million and negative USD 4.8 million, respectively, compared to USD 0.2 million and negative USD 1.1 million in the same periods in 2018
- ✓ Second quarter and first half 2019 net losses of USD 2.8 million and USD 6.2 million, respectively, compared to net losses of USD 2.0 million and USD 5.6 million in the same periods in 2018
- ✓ Total cash and cash equivalents of USD 58.8 million at 30 June 2019, excluding USD 69.0 million of restricted cash
- ✓ On 5 April 2019, the PHLY Annual General Meeting was held; all proposals were approved and no changes were made to the Board of Directors

Subsequent Events

- ✓ On 2 July 2019, Philly Shipyard was awarded a contract to perform modernization, repair and maintenance work on the *SS Antares*, a U.S. Maritime Administration cargo ship
- ✓ Effective 15 July 2019, Brian Leathers, assumed the position of Chief Financial Officer (CFO); Mr. Leathers brings deep government contracts experience to Philly Shipyard and replaces Jan Ivar Nielsen, who is resigning as the company's CFO to pursue another executive role within the Aker group

Operations

Currently, there is no shipbuilding or repair activity at the shipyard and all production facilities are idle and both graving docks are empty. Today, Philly Shipyard employs approximately 80 people. Philly Shipyard plans to keep a core group of employees to focus on efforts to secure new orders and transition the shipyard into a mix of commercial and government work. Philly Shipyard has also begun to recall some of its laid-off workers to staff a short-term repair contract awarded to it on 2 July 2019 for the *SS Antares*, a U.S. Maritime Administration (MARAD) cargo ship.

The Company has initiated various cost saving initiatives to preserve its cash. Until pre-production activities related to a potential new shipbuilding project start, Philly Shipyard expects to maintain a cash burn rate of approximately USD 1.5-1.7 million per month on average (excluding any impact from new work and extraordinary items). A majority of this cash covers the cost of the core group of employees to be retained to secure new work and transition the shipyard into a compliant government contractor. This cash also covers SG&A related to these efforts and fixed costs such as real estate taxes, utilities and insurance.

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 Q2 2019 was 0.23 compared to 0.65 at the end of Q2 2018. 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 Q2 2019 was 2.93 compared to 3.82 at the end of Q2 2018.

With a vastly reduced workforce in Q2 2019, comprised primarily of management and staff, Philly Shipyard continues to proactively approach safety no differently than before delivery of Hull 030 in an ongoing effort to improve safety and reduce the number of incidents at the shipyard. Together with management, the HSE department has worked to improve several key safety processes in anticipation of workers returning to the shipyard, which includes an overhaul to our training programs and policies intended to improve overall worker safety.

Financial Information

Second Quarter 2019 Results

Operating revenues and other income for the second quarter of 2019 were USD 0 compared to operating revenues and other income of USD 40.4 million for the second quarter of 2018. In Q2 2019, there was no shipbuilding or other activities whereas in Q2 2018 operating revenues and other income were driven mainly by the continued progress on the two Matson vessels (Hulls 029-030). Based on the successful recovery and receipt of certain amounts from its suppliers for the CV3700 project, approximately USD 2.2 million of previously incurred cancellation costs that were written-off and charged as impairment costs in 2018 were reversed in Q2 2019.

Net loss for Q2 2019 was USD 2.8 million compared to net loss of USD 2.0 million for Q2 2018. The net loss for Q2 2019 was driven primarily by significantly higher under-recovered overhead costs (i.e., overhead costs incurred and not allocated to projects) of USD 5.5 million compared to USD 0.5 million of under-recovered overhead costs incurred in Q2 2018 slightly offset by the partial reversal of impairment of assets of USD 2.2 million pertaining to the cancellation of the CV3700 project.

EBITDA, defined as earnings before interest, taxes, depreciation and amortization, is considered a relevant earnings indicator for Philly Shipyard as it measures the operational performance of the shipyard.

EBITDA for the second quarter of 2019 was negative USD 3.3 million compared to EBITDA of USD 0.2 million in the second quarter of 2018. The decrease in EBITDA was mainly driven by the lack of any shipbuilding or other activity in Q2 2019. Net financial items in Q2 2019 was income of USD 0.1 million compared to expense of USD 0.1 million in Q2 2018.

Year-to-Date 2019 Results

Operating revenues and other income in the first six months of 2019 ended at USD 18.9 million compared to operating revenues and other income of USD 83.4 million in the first six months of 2018. June 2019 year-to-date operating revenues and other income were primarily driven by the remaining progress on the second Matson vessels (Hull 030) whereas June 2018 year-to-date operating revenues and other income were primarily driven by the continued progress on the two Matson vessels (Hulls 029-030). Operating revenues and other income in the first six months of 2018 were also partially impacted by the implementation of the new International Financial Reporting Standards (IFRS) 15 standard (IFRS 15) leading to a reduction in both accumulated revenue and cost of USD 38.4 million in Q1 2018 and recognition of these amounts as an opening equity adjustment at IFRS 15 implementation date of 1 January 2018.

Net loss for the first six months of 2019 was USD 6.2 million compared to net loss of USD 5.6 million in the same period of 2018.

EBITDA for the first six months of 2019 was negative USD 4.8 million compared to EBITDA of negative USD 1.1 million in the same period of 2018.

Statement of Financial Position

Total assets were USD 172.0 million at 30 June 2019 compared to USD 190.0 million at 31 December 2018.

Total interest-bearing debt was USD 59.8 million at 30 June 2019 compared to USD 59.6 million at 31 December 2018. The Welcome Fund loan, which matures in March 2020, was reclassified from long-term debt to short-term debt in Q1 2019.

Cash and cash equivalents (excluding restricted cash) were USD 58.8 million at 30 June 2019 compared to USD 49.6 million at 31 December 2018. The increase of USD 9.2 million was primarily due to the liquidation of the equity-accounted investments in Philly Tankers of USD 44.6 million offset slightly by (1) a reduction in trade payables, accrued liabilities and provisions of USD 10.7 million, and (2) a net increase of USD 24.4 million of restricted cash consisting of (a) USD 20.2 million deposited into a collateral account to secure the Welcome Fund loan, (b) USD 4.4 million deposited into escrow accounts established as holdbacks for guarantees, deficiencies and disputed items for Hull 030, (c) USD 0.4 million of interest income earned on the restricted cash and (d) USD 0.6 million released from escrow accounts established as holdbacks for guarantees, deficiencies and disputed items for Hulls 029 and 030. USD 13.1 million of the Welcome Fund restricted cash deposit was required by the Welcome Fund lender in connection with the liquidation of Philly Tankers. The remaining USD 7.1 million of the Welcome Fund restricted cash deposit was made by Philly Shipyard to defease and fully cash collateralize the loan in exchange for the release of substantially all loan covenants, including all financial covenants. The Matson restricted cash deposits were required by Matson as holdbacks in connection with the deliveries of Hulls 029 and 030.

Restricted cash as of 30 June 2019 amounted to USD 69.0 million, of which USD 60.3 million is related to the collateral account securing the Welcome Fund loan, USD 4.3 million is related to holdbacks for guarantees, deficiencies and disputed items for Hull 029 and USD 4.4 million is related to similar holdbacks for Hull 030. The restricted cash amount for the Welcome Fund loan is expected to be used for repayment of the Welcome Fund loan at its maturity in March 2020. The restricted cash amounts for the holdbacks are expected to be released within the next 12 months. Accordingly, the entire restricted cash amount was reclassified from a long-term asset to a short-term asset in Q1 2019. For further details on the Welcome Fund loan, see note 8.

Right-of-use assets in the amount of USD 13.8 million at 30 June 2019 represents the net book value of the assets that PSDC purchased from Philly Shipyard in 2011. These assets were reclassified from property, plant and equipment to right-of-use assets per the new IFRS 16 lease standard (IFRS 16), which took effect 1 January 2019. For further details on IFRS 16, see note 4.

Total equity decreased to USD 105.3 million at 30 June 2019 from USD 111.5 million at 31 December 2018 due to the net loss of USD 6.2 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 30 June 2019. As of 30 June 2019, the loan was defeased and fully cash collateralized. Substantially all loan covenants, including all financial covenants, have been released.

The Company also had an unsecured three-year revolving credit facility for up to USD 10.0 million from TD Bank, N.A. The facility terminated in Q2 2019.

Shareholder Distributions

The PHLY Board has decided to continue to suspend payment of dividends. 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 and Repair, Maintenance, Modernization and Conversion Work

As of 30 June 2019, Philly Shipyard had no order backlog. Philly Shipyard continues to pursue a mix of newbuild and repair opportunities in the commercial and government markets. Securing contracts to build 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 continue to incur losses in 2019, even if the shipyard receives orders to build new vessels. Barring any impact from new work or extraordinary items, it is expected these losses (at an EBITDA level) should be in line with the cash burn rate.

In the near term, Philly Shipyard's main focus continues to be the pursuit of the opportunity to build National Security Multi-Mission Vessels (NSMV) for the U.S. Maritime Administration (MARAD). The NSMV program seeks to replace as many as five of the aging vessels that serve as training ships for the state maritime academies in the United States. The contract for the vessel construction manager (VCM) for the NSMV program was awarded to TOTE Services, LLC (TOTE Services) on 22 May 2019, National Maritime Day. Award of the construction contract is anticipated within Q4 2019. The U.S. Congress has appropriated USD 600 million in funding for the first two vessels (i.e., NSMV 1 and NSMV 2). MARAD's current objective is to receive the lead vessel within Q4 2022.

In addition, Philly Shipyard is engaged in discussions related to several other potential new construction projects for U.S.-built vessels, including some contracts which could be awarded in 2019, but mainly work for the medium-term and long-term horizons. Among other endeavors, Philly Shipyard is actively pursuing opportunities to build a variety of specialty vessels in the commercial and government sectors. Philly Shipyard is also exploring potential partnerships that can enhance its prospects 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 potential new shipbuilding project. In particular, Philly Shipyard is pursuing opportunities for steel work and repair, maintenance, modernization and conversion jobs to utilize idle capacity in its fabrication shops and dry-docks. In support of this, Philly Shipyard has submitted to the U.S. Navy a Master Ship Repair Agreement and is in the process of having its two drydocks certified to Naval Sea Systems Command (NAVSEA) requirements.

On 2 July 2019, Philly Shipyard was awarded its first repair and maintenance contract for the *SS Antares*, a large MARAD vessel that is managed by TOTE Services. It is planned that the vessel will arrive at the end of July with the repair and maintenance effort expected to last approximately two months. Philly Shipyard's objective is to win similar repair and maintenance contracts going forward in order to continuously utilize its drydocks as part of its plan to reconstitute its workforce.

Philly Shipyard's strategy and outlook for combining government and commercial work remains unchanged since the 2018 annual report.

On 29 May 2019, Philly Shipyard was one of four shipyards selected to conduct industry studies for the Common Hull Auxiliary Multi-Mission Platform (CHAMP) program. Philly Shipyard is teaming with Vard Marine to conduct these studies for the U.S. Navy. The CHAMP program is a multi-phase effort that involves design studies, preliminary design, and detail design and construction (DD&C) to ultimately recapitalize the Military Sealift Command (MSC) fleet of aging ships. The demand for the CHAMP program could approach 60+ vessels. The CHAMP vessels are not combatants, and are more commercially oriented, which fits the structure of Philly Shipyard's facility. It is anticipated the shipyards will ultimately compete for the DD&C contract, with award in 2023 and acquisition occurring over the next decade.

Shipping

Since the liquidation of Philly Tankers was completed in Q1 2019, Philly Shipyard has no shipping assets. Going forward, in line with its business strategy, Philly Shipyard will continue to evaluate opportunities to participate in the post-delivery economics of the commercial ships that it constructs.

Risks

Philly Shipyard's revenue is derived primarily from contracts awarded on a project-by-project basis. It is difficult to predict whether or when Philly Shipyard will be awarded a new contract due to, among other things, the complex bidding and selection processes, potential for contract award protests and challenges, changes in existing or forecast market conditions, governmental regulations and uncertainty regarding the timing of budget appropriations. Because Philly Shipyard's revenue is derived from contract awards, the Company's revenues, results of operations and cash flows can fluctuate materially from period to period.

At this time, Philly Shipyard has no order backlog for shipbuilding programs. Philly Shipyard faces significant risks if it is unable to secure new orders and/or financing for major commercial or government shipbuilding programs such as the NSMV program. There can be no assurance that Philly Shipyard will obtain new orders or financing for vessels. Furthermore, even if Philly Shipyard obtains new orders or financing for vessels, 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 has interrupted its building program, resulting in the idling of all production activities in its facility and a decrease of more than 90% 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 and increases in under-recovered overhead costs (i.e., overhead costs incurred and not allocated to projects).

The longer the delay in securing new orders continues, the more expensive and challenging it becomes for Philly Shipyard to win new orders and 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 and raise 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 would need to do an impairment charge against its fixed assets. A going concern qualification would make it very challenging to secure new orders and/or financing.

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, Philly Shipyard has signed a four-year collective bargaining agreement with the Unions which is effective through January 2023. The collective bargaining agreement includes a no-strike clause.

Philly Shipyard's success also depends to a great degree on the abilities of its key management personnel, particularly its executives and other key employees who have significant experience within Philly Shipyard's industry. The loss of the services of one or more of these individuals could adversely affect Philly Shipyard.

Philly Shipyard further depends upon a 99-year lease agreement for the shipyard facility and the future operations of the yard will accordingly be dependent upon Philly Shipyard fulfilling its obligations under this lease agreement. Failure to maintain certain employment levels may result in early termination of this lease. For more details regarding this lease, see note 14.

The Shipyard is dependent upon having access to construction financing facilities and other loans and debt facilities to the extent its own cash flow from operations and milestone payments from customers are insufficient to fund its operations and capital expenditures. In turn, the Shipyard must secure and maintain sufficient equity capital to support debt facilities. Additionally, the Shipyard may be required to obtain bonding capacity in case there is need for payment or performance bonds, or to furnish letters of credit, refund guarantees or other forms of security, to support major commercial or government shipbuilding programs such as the NSMV program. Philly Shipyard may not be able to obtain sufficient debt facilities or bonding capacity or furnish sufficient security if and when needed with favorable terms, if at all.

In 2019, there has been increased activity to obtain waivers under the Jones Act and legislation to repeal the Jones Act has been proposed. The Company is closely monitoring the situation.

Philly Shipyard's operations historically focused primarily on construction of new vessels for the U.S. Jones Act market. Philly Shipyard is continuing to develop and implement the policies and procedures required to be a fully compliant U.S. Government contractor. Philly Shipyard is aggressively pursuing U.S. Government opportunities for future ship design and construction programs, as well as vessel maintenance, modernization, conversion and repair projects. Entry into, or further development of, lines of business in which the Company has not historically operated may expose Philly Shipyard to business and operational risks that are different from those it has experienced historically. Philly Shipyard's management may not be able to effectively manage these additional risks or implement successful business strategies in new lines of business.

For a further analysis of risks, please refer to the Company's 2018 annual report.

Responsibility Statement
The unaudited condensed interim consolidated financial statements and interim financial report as of and for the six months ended 30 June 2019 were approved by the Board of Directors and the President and CEO on 15 July 2019.

The condensed interim consolidated financial statements have been prepared in accordance with IAS 34 Interim Financial Reporting as endorsed by the European Union and the Norwegian additional requirements in the Securities Trading Act.

To the best of our knowledge, the condensed interim consolidated financial statements give a true and fair view of the assets, liabilities, financial position and profit of PHLY, and the interim management report of PHLY includes a fair review of the development and performance of the business and the position of PHLY, together with a description of the principle opportunities and risks associated with the expected development of PHLY for the remaining months of the financial year.

Oslo, Norway
15 July 2019
Board of Directors and President and CEO
Philly Shipyard ASA

James H. Miller
Board Chairman

Kristian Røkke
Deputy Board Chairman

Amy Humphreys
Board Member

Elin Karfjell
Board Member

Steinar Nerbøvik
President and CEO

CONDENSED CONSOLIDATED INCOME STATEMENT

Amounts in USD millions (except number of shares and earnings per share)	Q2 Unaudited 2019	Q2 2018	6 Months Ended 30 June Unaudited 2019	6 Months Ended 30 June 2018	Full Year 2018 *
Operating revenues and other income	-	40.4	18.9	83.4	129.2
Operating expenses	(3.3)	(40.2)	(23.7)	(84.5)	(145.0)
Operating (loss)/income before depreciation - EBITDA	**(3.3)**	**0.2**	**(4.8)**	**(1.1)**	**(15.8)**
Depreciation	(1.8)	(2.0)	(3.6)	(3.9)	(7.8)
Reversal of impairment of assets/(impairment of assets)	2.2	-	2.2	-	(17.6)
Operating loss - EBIT	**(2.9)**	**(1.8)**	**(6.2)**	**(5.0)**	**(41.2)**
Net financial items	0.1	(0.1)	-	(0.5)	(0.6)
Loss before tax	**(2.8)**	**(1.9)**	**(6.2)**	**(5.5)**	**(41.8)**
Tax expense	-	(0.1)	-	(0.1)	(2.3)
Loss after tax **	**(2.8)**	**(2.0)**	**(6.2)**	**(5.6)**	**(44.1)**
Weighted average number of shares	**12,107,901**	**12,107,901**	**12,107,901**	**12,107,901**	**12,107,901**
Basic and diluted loss per share (USD)	**(0.23)**	**(0.17)**	**(0.52)**	**(0.46)**	**(3.64)**

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Amounts in USD millions	Q2 Unaudited 2019	Q2 2018	6 Months Ended 30 June Unaudited 2019	6 Months Ended 30 June 2018	Full Year 2018 *
Loss after tax	(2.8)	(2.0)	(6.2)	(5.6)	(44.1)
Other comprehensive income, net of income tax	-	-	-	-	-
Total comprehensive loss for the period **	**(2.8)**	**(2.0)**	**(6.2)**	**(5.6)**	**(44.1)**

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

Amounts in USD millions	Unaudited 30 June 2019	31 Dec. 2018 *
Assets		
Non-current assets		
Property, plant and equipment	26.8	44.1
Right-of-use assets	13.8	-
Restricted cash	-	44.6
Equity-accounted investments	-	44.6
Other non-current assets	0.3	0.3
Total non-current assets	**40.9**	**133.6**
Current assets		
Cash and cash equivalents	58.8	49.6
Restricted cash	69.0	-
Income tax receivable	-	3.3
Other current assets	3.3	3.5
Total current assets	**131.1**	**56.4**
Total assets	**172.0**	**190.0**
Equity and liabilities		
Total equity	**105.3**	**111.5**
Non-current liabilities		
Deferred tax liability	1.5	1.5
Interest-bearing long-term debt	-	59.6
Total non-current liabilities	**1.5**	**61.1**
Current liabilities		
Interest-bearing short-term debt	59.8	-
Trade payables, accrued liabilities and provisions	5.3	16.0
Income tax payable	0.1	0.2
Customer advances, net	-	1.2
Total current liabilities	**65.2**	**17.4**
Total liabilities	**66.7**	**78.5**
Total equity and liabilities	**172.0**	**190.0**

* Annual 2018 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	6 Months Ended 30 June Unaudited 2019	2018
As of beginning of period	111.5	155.6
Total comprehensive loss for the period *	(6.2)	(5.6)
As of end of period	**105.3**	**150.0**

CONDENSED CONSOLIDATED CASH FLOW STATEMENT

Amounts in USD millions	6 Months Ended 30 June Unaudited 2019	2018
Net cash used in operating activities	(15.1)	(17.4)
Investment in property, plant and equipment	(0.1)	(1.8)
Dividend received from equity-accounted investments	44.6	2.0
Net cash from investing activities	44.5	0.2
Portion of interest-bearing debt held in escrow	(20.2)	-
Repayment of capital lease	-	(0.1)
Net cash used in financing activities	(20.2)	(0.1)
Net change in cash and cash equivalents	**9.2**	**(17.3)**
Cash and cash equivalents at beginning of period	49.6	110.1
Cash and cash equivalents at end of period	**58.8**	**92.8**

* All attributed to the equity holders of PHLY.

Notes to the condensed interim consolidated financial statements for the 2nd quarter and year-to-date 2019

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 six-month periods ended 30 June 2019 and 30 June 2018 are comprised of PHLY and its direct and indirect wholly-owned subsidiaries (collectively referred to herein as the Group), 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 2018, 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 year-to-date periods are not necessarily indicative of the results that may be expected for any subsequent quarter or year.

The going concern assumption

The interim consolidated financial statements have been prepared on a going concern basis which contemplates continuity of normal business activities and realization of assets and settlement of liabilities in the normal course of business. The ability of the entity to continue as a going concern is dependent upon continuing shipbuilding operations and securing a customer order. While the Group is actively working on securing new orders, there is inherent uncertainty and no assurance that the Group will successfully secure a customer order.

The following conditions indicate a material uncertainty that may cast a significant doubt on the Group's ability to continue as a going concern:

- The Group does not have contracted customer order backlog. The delay Philly Shipyard has experienced in securing new orders and financing has interrupted its building program, resulting in the idling of all production activities in its facility and a decrease of more than 90% 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 and increases in under-recovered overhead costs (i.e., overhead costs incurred and not allocated to projects).

- The longer the delay in securing new orders 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 to retain and raise sufficient financing to support future shipbuilding projects.

- 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 79 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. Due to a forecasted breach of this condition caused by the gap in shipbuilding activity following the delivery of Hull 030, which would have occurred in Q1 2019, Philly Shipyard obtained a temporary conditional waiver of this minimum employment condition until 31 December 2019. If PSI obtains a new order during this waiver period, the waiver of the minimum employment condition will continue until PSI reaches the 200 full-time employee requirement.

The Group acknowledges the material uncertainty in being able to continue ordinary shipbuilding operations and secure new contracted customer backlog in order to comply with the shipyard lease minimum employment condition without obtaining additional waivers to continue operations beyond 31 December 2019. However, the Directors are confident that this is achievable through a combination of the following:

- 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 as many as five of the U.S. state maritime academy training ships. The award of this shipyard contract is anticipated to be announced within Q4 2019 with a delivery of the first vessel targeted within Q4 2022. If PSI is successful in its bid for this NSMV program, the Group is dependent upon having access to construction financing facilities and other loans and debt facilities to the extent its own cash flow from operations and milestone payments from customers are insufficient to fund its operations and required capital expenditures. Additionally, the Shipyard may be required to obtain bonding capacity in case there is need for payment or performance bonds, or to furnish letters of credit, refund guarantees or other forms of security, to support this project. PSI may not be able to obtain sufficient debt facilities or bonding capacity or furnish sufficient security if and when needed with favorable terms, if at all.

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

• In the event that Philly Shipyard is in breach of the shipyard lease condition to maintain an average of at least 200 full-time employees at the shipyard for 90 consecutive days, the Group has the intention to request an additional waiver beyond 31 December 2019; however, the success of obtaining this waiver from PSDC is uncertain.

Should the Group be unsuccessful in continuing ordinary shipbuilding operations and securing contracted customer backlog, or unsuccessful in complying with the shipyard lease minimum employment condition without obtaining additional waivers, there is a material uncertainty that exists that may cast significant doubt as to whether the Group will be able to continue as a going concern. In this scenario, the Group may elect to undergo an orderly liquidation process. Therefore, it may be unable to realize its assets and discharge its liabilities in the normal course of business at their stated net book values in the interim consolidated financial statements, resulting in the impairment of property, plant and equipment assets; termination payments relating to PSI's multi-employer union selected pension plan; and the potential acceleration of debt repayments.

Despite the material uncertainties above, the Board's assessment is that it is appropriate to apply the going concern assumption. The Board anticipates that the Group can continue its shipbuilding activities, and will have the financial resources to apply the going concern principle as the basis for the financial statements. The Board's assessment is unchanged from the Board's year-end 2018 assessment included in the 2018 annual report, with no material changes in the assumptions described therein.

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* (IAS 34). 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 2018.

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 2018, with the exception of implementation of the IFRS 16 lease standard described below.

IFRS 16 *Leases*

IFRS 16 *Leases* (effective from 1 January 2019). The IFRS 16 lease standard (IFRS 16) replaces IAS 17 *Leases* and the related interpretations. The new standard introduces a single, on-balance sheet lease accounting model for lessees, with optional exemptions for short-term leases and leases of low value items. A lessee recognizes a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments.

The Company has applied IFRS 16 initially on 1 January 2019, using the modified retrospective approach. Based on this, a potential cumulative effect of adopting IFRS 16 will be recognized as an adjustment to the opening balance of retained earnings as of 1 January 2019, with no restatement of comparative information. There has been no such adjustment of retained earnings as of 1 January 2019, following the implementation of IFRS 16.

As part of the 2011 Authorization Agreement, the Philadelphia Shipyard Development Corporation (PSDC) purchased certain shipyard assets from PSI for a purchase price of USD 42.0 million with funds provided by the Commonwealth of Pennsylvania. PSI leases back those same assets from PSDC subject to the terms of its shipyard lease and the Authorization Agreement. For accounting purposes, the transaction was accounted for as a sale/leaseback, and no adjustments were made to the accounting value of the assets at closing.

The net book value of assets under financial leasing agreements recorded in the statement of financial position at 30 June 2019 amounts to USD 13.8 million. From 1 January 2019, the net book value of the assets PSDC purchased from PSI in 2011 has been reclassified from property, plant and equipment to right-of-use assets.

The operating leases are for facilities, vehicles and printing and copying equipment. These leases consist of smaller amounts for printers and copiers, and leases that are up to 12 months for a training facility and a vehicle. Based on this, and no material impact from these leases, no right-of-use asset or lease liability has been recorded when the new IFRS 16 lease standard became effective 1 January 2019.

The building lease for PSI's plate priming facility has been extended on a month-to-month basis. The base rent is USD 16 thousand per month. This amount is not included in the operating lease rentals recorded above. Due to the short term of the lease, on a month-to-month basis, no right-of-use asset or lease liability has been recorded as of 1 January 2019. This treatment will be revisited if the shipyard signs a contract or contracts that secures long-term activity.

PSI operates on land leased from PSDC through April 2038. Annual payments under the lease agreement include rent, taxes and operating expenses (operating expenses are subject to an annual revision based on PSDC's operating expenses). PSI has options to renew the lease for three consecutive periods of 20 years each and one final period of 19 years. At expiration of the first lease period in 2018, the lease was renewed for the first of the three 20-year option periods. PSI can acquire the land for USD 1 after the expiration of all renewal periods. Lease payments for rent due under the finance lease are USD 1 per year.

The shipyard lease is treated as a government grant under IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* (IAS 20). On transition to IFRS 16, the shipyard has continued to use this policy to record the government grant under IAS 20 against the investment. This gives a USD 0 balance for the right-of-use assets and the lease liability at 1 January 2019, as the grant is deducted to arrive at the carrying amount of the right-of-use assets. For more details regarding the shipyard lease, see note 14.

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 2018 unless described elsewhere in this report.

Due to the limited backlog to Q2 2019, an impairment trigger has been identified for the carrying amount of property, plant and equipment, the same triggering event as per 31 December 2018. The Company has estimated the recoverable amount using the value-in-use method determined by discounted future cash flows, the same estimated recoverable amount as per 31 December 2018. No impairment of property, plant and equipment balances was 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. Further details on determination of recoverable amounts and impairment testing can be found in note 8 of the 2018 annual report. Through the end of Q2 2019, no major changes have been identified.

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 30 June 2019 and 30 June 2018, 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 and year-to-date periods ended 30 June 2019 and 30 June 2018. Accordingly, 12,107,901 ordinary shares was used in the calculation of earnings per share for the quarters and year-to-date periods ended 30 June 2019 and 30 June 2018.

8. Interest-bearing debt

The following shows changes in interest-bearing debt during 2019:

Amounts in USD millions	Non-current debt	Current debt	Total interest-bearing debt
Balance 31 December 2018	**59.6**	-	**59.6**
Repayment of debt	-	-	-
Reclass of debt	(59.6)	59.8	0.2
Balance 30 June 2019	**-**	**59.8**	**59.8**

PSI has a secured term loan of up to USD 60.0 million (USD 59.8 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 has a five-year term and 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 is secured by a first lien on USD 60.3 million of restricted cash to cover all remaining debt service, including repayment in full at maturity. Substantially all loan covenants, including all financial covenants, have been released. USD 60.0 million is drawn under this term loan at 30 June 2019.

PSI had an unsecured three-year revolving credit facility for up to USD 10.0 million from TD Bank, N.A. The facility terminated in Q2 2019. The loan accrued interest at 30-day LIBOR plus 2.50% per annum as defined in the credit agreement.

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 30 June 2019. 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 30 June 2019.

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 30 June 2019 were USD 30 thousand (USD 30 thousand for the same period in 2018) and for the six-month period ending 30 June 2019 were USD 60 thousand (USD 60 thousand for the same period in 2018).

PSI entered into an administrative services agreement with Philly Tankers LLC (PTLLC) whereby PSI supplied certain administrative services to PTLLC. 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 and was terminated on 31 December 2018. Related revenues for the three-month period ending 30 June 2019 were USD 0 (USD 30 thousand for the same period in 2018) and for the six-month period ending 30 June 2019 were USD 0 (USD 60 thousand for the same period in 2018).

10. Capitalized interest

	Q2		6 Months Ended 30 June	
Amounts in USD millions	**2019**	**2018**	**2019**	**2018**
Interest expense	(0.4)	(0.4)	(0.8)	(0.8)
Interest capitalized on construction contracts	-	-	-	-
Net interest expense	**(0.4)**	**(0.4)**	**(0.8)**	**(0.8)**

11. Construction contracts

The order backlog is USD 0 at 30 June 2019 as the Matson project is now 100% complete. 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 30 June 2019	Order intake 6 months to 30 June 2019	Order backlog 31 Dec. 2018
	-	**0.3**	**17.4**

The loss recognized on long-term contracts (Hulls 029-030) as of 30 June 2019 is as follows:

Amounts in USD millions	Actual 30 June 2019
Contract revenue recognized to date	408.8
Less: contract expenses recognized to date	(418.3)
Loss recognized to date (Hulls 029-030)	**(9.5)**

Typical variable consideration elements identified in the Company's contracts with customers include liquidated damages, performance guarantees and warranties. Under the Matson contract for Hulls 029-030, liquidated damages are considered as variable consideration, whereas performance guarantees and warranties are not categorized as variable consideration.

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.

As of 30 June 2019, the Company had no more contracts in place. During Q1 2019, the Company was building one containership for Matson: Hull 030 delivered on 28 March 2019. Philly Shipyard recognized contract revenues and expenses for the two-containership order from Matson as one project. As of 30 June 2019, the Matson project is 100% complete. The contract loss was provided for as of Q2 2019.

Customer milestone payments as of 30 June 2019 and 31 December 2018 totaled USD 0 and USD 391.8 million, respectively. Customer milestone payments from Matson were made at intervals that were intended to be cash neutral, and as such are not representative of a significant financing component present in the contract.

Customer advances, net as of 30 June 2019 and 31 December 2018 totaled USD 0 and USD 1.2 million, respectively. Customer advances, net represents the difference between cash advances received from the customer and costs incurred for those vessels.

As of 30 June 2019, PSI has non-cancellable purchase commitments for materials and equipment (unpaid liabilities) of approximately USD 2.4 million for the construction of Hull 030.

12. Operating revenues and other income

	Q2		6 Months Ended 30 June	
Amounts in USD millions	**2019**	**2018**	**2019**	**2018**
Operating revenues	-	40.3	18.9	83.2
Profit in equity-accounted investments (Hulls 025-028)	-	0.1	-	0.2
Operating revenues and other income	**-**	**40.4**	**18.9**	**83.4**

Profit in equity-accounted investments (Hulls 025-028) represents the Company's 53.7% share of the total comprehensive profit of Philly Tankers, which for the six months ending 30 June 2019 and 30 June 2018 amounted to USD 0 and USD 0.2 million, respectively.

13. Financial instruments

As of 30 June 2019, the Company had no forward exchange contracts or other financial instruments.

14. Commitments and contingencies

Pursuant to the shipyard lease between PSI and 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 79 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. Due to a forecasted breach of this condition caused by the gap in shipbuilding activity following the delivery of the last vessel in its order backlog (Hull 030) in Q1 2019, Philly Shipyard has obtained a temporary conditional waiver of this minimum employment condition until 31 December 2019. If PSI obtains a new order during this waiver period, the waiver of the minimum employment condition will continue until PSI reaches the 200 full-time employee requirement.

15. Subsequent events

On 2 July 2019, Philly Shipyard was awarded a contract to perform modernization, repair and maintenance work on the *SS Antares*, a U.S. Maritime Administration cargo ship.

Effective 15 July 2019, Brian Leathers assumed the position of Chief Financial Officer (CFO). Mr. Leathers brings deep government contracts experience to Philly Shipyard and replaces Jan Ivar Nielsen, who is resigning as the company's CFO to pursue another executive role within the Aker group.

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