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NWR.L - Q4 2014 New World Resources Plc Earnings Call

EVENT DATE/TIME: FEBRUARY 24, 2015 / 10:00AM GMT

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CORPORATE PARTICIPANTS

Radek Nemecek *New World Resources Plc - IR*

Gareth Penny *New World Resources Plc - Executive Chairman*

Marek Jelinek *New World Resources Plc - Executive Director & CFO*

CONFERENCE CALL PARTICIPANTS

Rob Slater *Silver Rock Financial - Analyst*

PRESENTATION

Operator

Good day, and welcome to the NWR full-year 2014 results conference call. Today's conference is being recorded. At this time, I would like to turn the conference over to Mr. Radek Nemecek. Please go ahead, sir.

Radek Nemecek - *New World Resources Plc - IR*

Thank you, operator. Good morning, everyone, and thank you for joining us on this conference call to discuss our full-year results. We are joined today by our Executive Chairman, Mr. Gareth Penny, and our Chief Financial Officer, Mr. Marek Jelinek, who will present the highlights. At the end of the presentation, we will open the call for questions from participants.

May I also take this opportunity to remind you that this event is being recorded and that the recording will be made available on our website shortly after the presentation.

With that, I'd like to invite Gareth to begin.

Gareth Penny - *New World Resources Plc - Executive Chairman*

Thank you, Radek; and good morning, everyone. And welcome to this results presentation. I wanted to start by giving an overview of the performance for the full year 2014. Then, I'll hand to Marek, who will present in more detail the financials. And I'll conclude by outlining the outlook for the current year along with an update on our longer-term goals.

If we move then on to slide number 5, let me start by saying that, obviously, 2014 has been another very challenging year. We have experienced prolonged and unprecedented global pressure on coking and thermal coal prices, which have been in decline since 2011.

Coking coal prices have continued to suffer from global over-supply as companies have increased their production in order to bring down their costs per tonne, while European steel manufacturers' demand has been muted, as we'll note in a minute.

Thermal coal prices continue to be affected by the fallout from the displacement of thermal coal by shale gas in the US, and this has led to increased volumes being redirected towards Europe. And the relatively mild winter so far has not helped the European market either.

This weak pricing environment has seen our average coking coal price fall 13% year on year, and our average thermal coal price fall 4%. Together with the decline in thermal coal sales volumes, these are the principal drivers behind the 20% fall in revenue that you've seen from our results.

To help offset this weakened top line, however, we've made great strides towards lowering our operational costs in line with our stated strategy. Our mining unit costs were down 14% and reached EUR67 a tonne, in line with our target for 2014. Furthermore, our selling and administrative expenses came down another 18% to EUR135 million, which is encouraging. And we recorded positive EBITDA for the year of EUR11 million.

On the non-cash impairment, Marek will talk about this in detail later on.

Let me quickly summarize then the successful capital restructuring which we completed in October last year, and which has put New World Resources on a much firmer and sustainable financial footing.

EUR185 million of new capital was raised, resulting in a reduction in total debt from EUR825 million to EUR535 million, and a significant fall in debt servicing costs. Furthermore, the maturity of the new senior notes has been extended from 2018 to 2020.

As you can imagine, this was a major exercise backed by all our stakeholders, and it means that we can now fully focus on the actual mining business and the selling of coal.

At the end of last year, our net debt stood at EUR281 million, including cash on hand of EUR128 million.

If we move then on to slide number 6, before going into production and sales levels, let me stress that our business, namely deep underground coal mining, is inherently fraught with risks, and we will always strive to minimize those risks as far as we possibly can. The lost time injury frequency rate was up year on year, mainly due to increased seismic activity. Comparable figures that we're seeing for this year to date are encouraging and confirm for the long-term, improving trajectory.

Although we sadly have to report the loss of eight lives over the course of the year, three of which were directly associated with seismic events, the fact remains that we are still one of the safest, deep level, underground mining operations in Europe, and we believe we're on track to achieve our lost time injury frequency target of 5 by the end of 2015.

As you can see from this slide, our coal production for the year was 8.6 million tonnes, with external sales of 8.3 million tonnes, and with 57% of total sales being coking coal sales. I'm pleased to report that we managed to contain CapEx with capital costs from continuing operations down 45%.

Looking at steel production at the bottom right-hand part of this slide in the regions, it's clear that our customers have also continued to operate in a very challenging environment. The chart on the right, so steel production and our customers' market basically flat compared to the previous year, and global utilization rate of around 77%.

In terms of the Debiensko project, we've now completed the pre-feasibility study of the project, which has resulted in 186 million tonnes being classified as JORC-compliant, marketable, hard coking coal reserves. Our next step is to identify a suitable strategic partner, or partners, to help develop the site.

Finally, the recently approved aid from the Czech State for Paskov Mine, that should remain operational until the end of 2017, aims to ease the closure process and provide financial support to those working at Paskov. The agreement was conditional upon the approval of the European Commission, and has now come into full force.

With that, let me hand over to Marek who will walk us through more detailed financials.

Marek Jelinek - *New World Resources Plc - Executive Director & CFO*

Thank you, Gareth. Good morning, everyone, and thank you very much for being on the call this morning. We are now on page 8 of the presentation looking at the P&L.

Gareth has alluded to the difficult pricing environment, which combined with the thermal coal volumes, really was the driver behind the revenue development. And I'll very shortly speak about the development in thermal and coking coal revenues separately.

Looking at costs, the total cost of sales were down 27%. And taking out the inventory impact from the cost of sales, you get to a decline in cost of sales of about 19%. This clearly demonstrates our ongoing focus on containing costs and optimization of the Czech mining operations.

A very similar trend has been seen in the selling and admin expenses which were down even 18% in 2014. And together with cost savings in 2013, selling and admin expenses are down approximately 40% over the last two years.

We've seen positive EBITDA for the year of EUR11 million, clearly reflecting the successful operational optimization at our Czech mines.

There are two one-off items in the P&L this time. First, the impairment charge of EUR183 million. This is a write-down of the carrying value of our fixed assets, and it's really driven by reflecting the current pricing environment and the long-term production outlook into the carrying value of these assets.

The second one-off is the accounting gain incurred on the financial restructuring. This was EUR342 million. And I want to make clear this is a non-cash gain. This is simply netting off the profit realized on a write-off of the nominal value of the debt against the costs incurred in putting the restructuring together.

Looking at the net cash flow from operations, that was negative, but we have seen an improvement quarter after quarter in this item over the course of the year. And we clearly remain committed to further improvements on costs and, obviously, cash generation.

And finally, looking at CapEx, we ended the year with EUR60 million of CapEx, which is even lower than our original target. And it represents about 45% reduction of CapEx relative to the year 2013.

Moving on to page 9 for an illustration of the current pricing environment. I think for those of you who are looking at the slides, the chart on the left-hand side really speaks for itself. The increased supply of coking coal in the global market which, combined with relatively meager demand from European steel manufacturers, has resulted in the ongoing downward pressure on coking coke.

This led to an average realized coking coal price of EUR85 a tonne, which as a coincidence, applies to both the fourth quarter 2014 as well as the full calendar year 2014. And it's a 13% drop which follows a 22% drop the prior year.

The price agreed for approximately 75% of our coking coal in 2015 represents a 9% improvement relative to the 2014 average.

In thermal coal, the situation is quite similar. The development in the North America energy mix has led to increased supplies of thermal coal into Europe as well as Central Europe. And we've also seen excessive thermal coal inventories around Central Europe.

This has led to an average price for thermal price in 2014 of EUR54 a tonne, or a 4% decline relative to the year before. The price that we agreed for thermal coal in calendar year 2015 is EUR52 a tonne.

Moving on to analysis of the key EBITDA drivers on page 10. The EUR11 million of EBITDA in 2014 is a significant improvement over the negative EBITDA of EUR10 million the year before. Lower coking coal and thermal coal prices, together with lower thermal coal volumes, took EUR173 million from the revenues. However, this was offset by the cost improvements, better coal mix and the change in inventories, and resulted in a EUR21 million improvement in EBITDA for EUR11 million of EBITDA in 2014.

Moving on to more detailed analysis of the thermal coal and coking coal parts of our business separately. This is page 11, or slide 11. You can see that our coking coal revenues were EUR406 million, or an 11% decline year on year, which is a combination of a 3% improvement in tonnage, more than offset by a 13% decline in the average coking coal price.

Thermal revenues were down 32% to EUR193 million. This is a combination of a 30% drop in price and a 4% decrease in tonnage. Sorry; obviously, the other way around.

The development in cash costs has seen a 14% decline, which is despite a 2% reduction in production. And again, I think this is clearly a result of our very, very sharp focus on controlling costs. And just to say that again. The selling and admin expenses were down 18% to EUR135 million.

Moving on to page 12 that describes our financial position. Gross cash flow from operations after working capital was negative at EUR23 million. We paid EUR34 million in interest and spent EUR60 million on CapEx.

Net debt at the end of 2014 was EUR281 million, helped by the EUR511 million reduction following the balance sheet restructuring.

Our cash balance at the end of 2014 was at EUR128 million, and as you can see from the bottom right-hand side chart, there is very little debt maturities within the next five years. It's essentially the amortization of the ECA facility over time.

So that, I think, is a quick summary of the financial aspects of the results, and I'd like to hand back to Gareth to talk about the outlook.

Gareth Penny - *New World Resources Plc - Executive Chairman*

Marek, thank you. And if we move on to slide 14, looking ahead at this year, it's clear that we remain in one of the toughest environments that the industry has ever experienced.

Marek has already mentioned that we have agreed coking coal prices at EUR93 for the full year for the majority of our expected production, which represents a 9% improvement of the realized price in the fourth quarter; and [EUR52 a tonne] (corrected by company after the call) for thermal, representing a 4% decline on the full year in 2014.

Against this backdrop, our targeted -- our operational targets for the year remain as follows. We plan to produce somewhere between 7.5 and 8 million tonnes of coal for the year, and sales from our own production and stocks of around 8 million tonnes.

We again target 60% of coking coal in the sales mix. We target cash costs in the mid 60s per tonne, and a further reduction of CapEx to around EUR30 million to EUR40 million.

And as I mentioned earlier, in terms of lost time frequency rate, we want to trend down towards the 5 that we set ourselves for a target. You may be interested to note at the end of January, lost time injury frequency rate was 6.6.

If we then go on to slide 15, in addition to managing our way through a difficult commercial environment, we remain focused on the strategy that we outlined at the beginning of 2013. We intend to become Europe's leading miner and marketer of coking coal by 2017 in a safe and sustainable way.

As we've said before, there are three pillars to the strategy. First, we aim to optimize our current operations, which we have gone some way, or I would say a very considerable way to achieving, and I think that's evident from the numbers. And Dale Ekmark and his team will continue working on this aspect of our business.

Secondly, we aim to offer a full range of coking coal qualities to our existing and future customer base, becoming what we call a one-stop shop for coking coal needs in Europe.

And thirdly, we intend to develop our future business around existing mines and resources and new opportunities.

As production capacity at OKD declines, we have to deliver our strategy through a mix of mining projects and new marketing initiatives, including trading, and in particular, the import of seaborne coking coal.

Our sales and marketing, and our new business development teams, are making strides in these two areas, and we hope to be able to update the market on these aspects as we work our way through the coming year and beyond.

In the past, we have imported relatively small volumes of coking coal on an as-needed basis to blend with our own coking coals to meet customer needs.

Thanks to our longstanding customer relationships, we have acquired a unique understanding of their requirements. And from this year on, we'll be aiming to fully meet those requirements by significantly increasing our trading and blending capacities, and by increasing greater volume of coking coal -- by importing a greater volume of coking coal. This is the pattern you will see developing between now and 2017.

So with that, if I can hand back to Radek.

Radek Nemecek - *New World Resources Plc - IR*

Thank you, Gareth. Operator, we are now ready to take questions.

QUESTIONS AND ANSWERS

Operator

(Operator instructions). Rob Slater, Silver Rock Financial.

Rob Slater - *Silver Rock Financial - Analyst*

A few questions from my side. Based on the projections you've provided today, with respect to the toggle debt securities that came out of the restructuring last year, can you comment on whether or not you'll be paying cash interest on both the senior notes and the convertible security in calendar 2015?

Marek Jelinek - *New World Resources Plc - Executive Director & CFO*

Yes. Thanks for the question. The PIK toggle mechanism is different in the two securities. The senior note has a formula that -- where there's a cash level of EUR110 million. If a payment of a coupon in cash would result in the post-coupon cash level to be below EUR110 million, then that coupon is [PIK-ed]; whereas in the convertible, it's a discretionary PIK. Based on our budget, we think it's very likely that we would PIK the coupons in 2015.

Rob Slater - *Silver Rock Financial - Analyst*

And that's both for the convertible security and the senior bonds?

Marek Jelinek - *New World Resources Plc - Executive Director & CFO*

Well, for the senior bonds, it's easier to say because it's a formula. For the convertible, it's a decision by the Company and it will be taken closer to the coupon date. But I think where we are today, it's likely that we will be [PIK-ing].

Rob Slater - *Silver Rock Financial - Analyst*

Okay. Next question. In the press release this morning, one of the bullet points on the first page talks about material uncertainty relating to the use of going concern in the year-end audit. Can you just provide us a little more context for how you as a company think about that? That's an important point, but just wanted to get a little more context for how the Board was thinking about this decision in respect of the audit.

Marek Jelinek - *New World Resources Plc - Executive Director & CFO*

Yes. That's a good question. So there are, I think, two levels of analysis in this. One is: What do we --? What's our outlook for the next 12 months? And as you know, we have priced about 75% of our coking coal and all of our thermal coal for the year so we have a reasonable level of visibility there. And we are comfortable that the Company is a going concern from that point of view.

Once you look beyond a 12-month period to a, say, 18-month period, the pricing uncertainty becomes much more significant. The current outlook in terms of coking coal price is not positive. In fact, the current, right now today prices of coking coal are significantly below what we locked in at the beginning of the year. And so that's one level of uncertainty, the pricing environment.

And, of course, as is inherent in a deep, underground mining operation, there is always a level of uncertainty with regards to the ability to meet our own production targets.

And so that's why, in thinking about going concern, we were trying to strike the right balance between what we know about the next 12 months and the admittedly significant uncertainties beyond that period.

Rob Slater - *Silver Rock Financial - Analyst*

Okay. And then last question from my side. I just wanted clarification from the positive news from a few weeks ago regarding the European Commission's approval for state aid.

There was a note in your press release that suggested that if hard coking coal benchmark prices fell below $110 per tonne for three consecutive quarters, the agreement with the government would be reassessed and/or renegotiated. It seems like we're close to that sort of a price level currently.

So could you just either remind us, or give us an update, on how you expect those negotiations would go and what would potentially be renegotiated under that circumstance?

Marek Jelinek - *New World Resources Plc - Executive Director & CFO*

Let me try to provide the context in which this works. The basic -- the fundamentals of the agreement with the Government of the Czech Republic are we continue to operate the Paskov Mine until the end of 2017 at our own cost. And if we do that, the Government then will partially cover the costs of shutting the mine down. Specifically, the Government would pay for the social costs of shutting down the mine.

We were happy to enter into that agreement provided that there was a mechanism that allow us to renegotiate the terms if Paskov's financial performance became much worse. And the reason for that potentially happening was a collapse in coal prices.

That's why there are these provisions that say if the benchmark, the Australian benchmark is below $110 for three consecutive quarters, parties will attempt to go back to the table and renegotiate.

Yes. We are now probably in an area where this is beginning to be triggered. But again, its three consecutive quarters, so there's still a long way to go.

Rob Slater - *Silver Rock Financial - Analyst*

Okay. That's clear. Thanks very much.

Operator

(Operator instructions). It appears there are no further questions at this time.

Radek Nemecek - *New World Resources Plc - IR*

Okay. Thank you, operator; and thank you, everyone, for participating in the call. Should you have any further questions, please contact our investor relations department.

Thank you again, and goodbye.

Operator

Thank you. That will conclude today's conference call. Thank you for your participation, ladies and gentlemen. You may now disconnect.