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NWR.L - Q1 2015 New World Resources Plc Earnings Call

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PRESENTATION

Operator

Good day, and welcome to the NWR Q1 2015 results conference call. Today's conference is being recorded. At this time, I would like to hand the conference over to Mr. Radek Nemecek. Please go ahead, sir.

Radek Nemecek - *New World Resources Plc - IR*

Thank you. Very nice morning, ladies and gentlemen, and thank you for joining us on this conference call to discuss our Q1 results.

We are joined today by the Chief Financial Officer of NWR, Marek Jelinek, who will deliver the presentation. At the end of the presentation, we will open the call for your questions.

As mentioned by the operator, this call is being recorded. And the recording will be made available on our website, shortly after the presentation.

With that, let me hand over to Marek.

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

Radek, many thanks for this. Good morning, everyone. Thank you very much for joining us for today's results presentation.

I'd like to start by summarizing our financial and operational highlights for the first quarter. I'll then drill down to the financials in a little more detail, and I'll conclude by commenting on the outlook for the rest of 2015.

So, let's get right to it. For those of you who are following the slides, I'm now on slide 5. And let me start by saying that the opening months of 2015 saw a continuation of the difficult markets that we've had to contend with over the past couple of years, or so.

Our revenues for the period were 22% down to EUR135 million, which is a result of lower sales prices, as well as lower tonnage sold.

Our coking coal sold for an average price of EUR90 per tonne, which represents a 1% year-on-year decline. And our thermal coal sold for an average of EUR56 per tonne, which is down 7% on the same period last year.

Lower prices and sales volumes were somewhat mitigated by our continued cost improvements. Cash mining unit costs per tonne were at EUR71 per tonne, which is 7% up on constant currency basis. But please note that production during the same period was down 20%.

So we are very much on track to achieve our target of mid-EUR60s per tonne in terms of unit cash costs for the full calendar year 2015.

Our selling and administrative expenses were significantly down, 25% to EUR25 million.

We recorded a negative EBITDA of EUR2 million for the first quarter.

And going further down the profit and loss, we reported a non-cash gain of EUR49 million on the fair value revaluation of the convertible notes, which resulted in a earnings per share of 0.37 eurocents.

We ended the quarter with net debt of EUR278 million, which includes a cash of EUR84 million at the end of March.

Moving on to a summary of the operational performance, this is on slide 6, I'm pleased to say that our safety performance continues to improve. In the period under review, we had a 22% improvement, relative to the prior year, in lost time injury frequency rate, which clearly attests to our safety-first policy, and the great work of everyone in our operations in the Czech Republic.

Our coal production for the quarter was 1.8 million tonnes, and external sales were 1.6 million tonnes, which is down 20% and 18%, respectively.

The coal sales mix was very good at 64% coking coal and 36% thermal coal. So that's quite significantly ahead of the targeted 60/40 split.

CapEx in the quarter was EUR15 million, which is EUR2 million higher than in the same period of 2014. This is really due to timing. And it's still very much in line with our full-year guidance of EUR30 million to EUR40 million to be spent on CapEx in 2015.

We ended the quarter with inventories at 875,000 tonnes, which represents a 26% increase year on year, primarily caused by an over supplied local market. And we are working very hard to monetize the inventory, this is predominantly thermal coal, so we are looking to extract cash out of that inventory.

In terms of the broader market picture, steel production in Central Europe was up 1% year on year, and the global steel utilization was around 72%.

Now, looking at the profit and loss on page 8, as I already mentioned, our revenues were down by 22% to EUR135 million. This is a result of lower prices, combined with lower volumes. However, our total cost of sales were down 16%. And, even more impressively, our selling and admin expenses in the first quarter were down 25% year on year.

The EBITDA stood at negative EUR2 million for the first quarter.

And we record an operating loss of EUR13 million.

We do, however, report a net income for the quarter of EUR26 million, which reflects a non-cash gain of EUR49 million. This is simply an accounting impact of the change in the fair value of the convertible notes that we now carry on our balance sheet.

Our net cash flow from operations after working capital was negative for the period, but was, in fact, very much in line with our own projections for the quarter.

Looking at the pricing situation on page 9, this is obviously a familiar picture with those of you that follow the coal industry. Coal prices are still significantly challenged.

However, as we reported earlier this year, we have managed to agree an average price of EUR93 per tonne for coking coal with many of our customers for the full year. This price is applicable to 74% of our expected production, and so that serves as a very effective protection against the short-term volatility in the market.

Thermal coal remains under significant pressure, as well. Our average realized price for thermal coal in this quarter was EUR56 per tonne, which represents a 7% decline on the same period last year. The average price that we agreed and expect for the calendar year 2015 is EUR52 per tonne.

Looking at the EBITDA drivers on page 10, there you can see that we went from a positive EBITDA of EUR12 million in the first quarter of 2014 to a negative EBITDA of EUR2 million in the same period this year.

You can see that the market situation, so a combination of prices, volumes, mix, and inventories, has eaten about EUR36 million of our EBITDA in the year-on-year comparison. Whereas, the impressive cost performance has clawed about EUR22 million back from that negative market impact, again, for the negative EUR2 million EBITDA for the first quarter of this year.

Looking at the operating review on page 11, splitting the two main product categories, you can see that our coking coal revenues, at EUR90 million, were down 20%. Again, that's a combination of a 20% reduction in tonnage, and a 1% reduction in price.

Thermal coal revenues saw a similar 21% decline to EUR32 million. Again, this is a combination of a 7% decline in price, and a 15% reduction in tonnage.

The development in unit cash costs is an increase of 7%. However, it's important to keep in mind that this is against a backdrop of a 20% lower production. So, in fact, costs, in absolute terms, have declined very significantly. Most significantly, sales and administrative expenses were down 25%.

Looking at our financial position on page 12, we see that our net debt was at EUR278 million at the end of Q1 2015, which includes an available cash balance of EUR84 million. And the net debt development also includes a non-cash gain of EUR49 million, due to the change in fair value of our convertible notes.

Gross cash flow from operations after working capital was negative EUR27 million; cash interest was just under EUR1 million; and we spent EUR15 million on CapEx.

And finally, as you can see at the bottom right-hand chart on this page 12, there is virtually no debt maturity within the next five years.

And just one note on the debt situation in general, we are currently in early stage talks with potential providers of a refinancing of the EUR35 million senior secured credit facility. This is an early stage at this point, and we will report to the market, in due course, on any progress.

That, I think, summarizes the key elements of the results announced this morning, and I'd just like to move on to talk about the outlook for the rest of the year.

Again, we have agreed coking coal prices of EUR93 per tonne for the majority of our expected sales of coking coal, and thermal coal prices of EUR52 per tonne.

Our production guidance remains unchanged. We continue to aim at production in the range of 7.5 million tonnes to 8 million tonnes.

And we are looking to sell around 8 million tonnes. We expect to produce not less than 60% of coking coal in the mix.

And we target unit cash costs of EUR65 per tonne, and CapEx in the range of EUR30 million to EUR40 million.

And, as always, our focus very much remains on maintaining a safe operation with the lost time injury frequency rate being targeted below 5.

A quick note on our longer-term strategy. Despite the difficult market, at the moment, we are definitely not losing sight of the three pillars of our strategy that are illustrated on slide 15.

We intend to become Europe's leading miner and marketer of coking coal by 2017 in a safe and sustainable way, and we have, as I said, a three-prong strategy to arrive at that goal.

First, we will run our current operations in the Czech Republic safely and efficiently. The team, led by Dale Ekmark at OKD, is making significant strides in improving efficiencies. And we are now focusing on lowering cash mining unit costs still further to the mid-EUR60s per tonne.

We will contain -- or continue containing CapEx at well below EUR50 million, and we'll continue to push for an excellent safety performance.

That was the first pillar.

Second, we are seeking to develop our business around existing mines by expanding reserves and resources, and pursuing our development projects, such as Debiensko, and Morcinek.

And thirdly, we are ramping up our sales and marketing capabilities in order to be able to offer a full range of coking coal qualities to our existing, as well as new, customers, so as to become a one-stop shop for their coking coal needs, for the coking coal needs of European steelmakers.

The Central European region, in particular, continues to be short coking coal, and we will seek to address that shortage in the market by developing our import and blending capabilities.

That concludes my presentation this morning. I would like to hand back to Radek for further proceedings. Thank you very much.

QUESTIONS AND ANSWERS

Radek Nemecek - *New World Resources Plc - IR*

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

Operator

(Operator Instructions). Robert Slater, Silver Rock Financial.

Robert Slater - *Silver Rock Financial - Analyst*

A few questions from my side. First of all, could you give us a little bit more of a detailed update on the Debiensko process, and what your expectations are for next steps there?

Second question, I see this non-cash gain you've booked in the quarter for the mandatory convert revaluation. Could you explain the accounting treatment there, and on what basis you've decided to do that revaluation in the quarter?

Then, I guess, the third question, and two parts, one with respect to CapEx, one just more generally in regards to cash flows, you said that CapEx was weighted towards the first quarter. But trying to extrapolate that out, even if you take a reduced amount in the coming quarters, I'm struggling to see how you can hit this low end of the CapEx range of EUR30 million, especially in light of your historical CapEx? So if you could walk us through, a little more specifically, how CapEx through the rest of the year will be phased in, that would be very helpful.

And then, in respect of cash flows more generally, you did burn a lot of cash in the first quarter. We've talked before about your minimum cash covenants and some of your debt facilities. How should we think about your own expectations for cash flow throughout the year, in light of that EUR40 million minimum cash covenant?

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

Robert, thank you very much for the questions. Let me try to address them in the order you asked them.

Debiensko, let me make a somewhat broader comment. Debiensko is, to my knowledge, the only significant coking coal deposit. It's about 200 million tonnes of very high quality coking coal. This, in itself, represents a huge value and will be a -- or it's a significant part of our long-term future.

That said, given where the market is at the moment, given our cash flow that you are referring to, we are very much focused on delivering on the part of our strategy that deals with our Czech operations. Continue containing CapEx; very much continue aggressively attacking costs, so that we get to a position, with our operating mines, that we get to a position where they are cash generative, even in the current market environment.

So, what I'm trying to say is Debiensko is a very high-value project, which is a project of the future. The present is very much about our Czech mines. We continue to maintain the project, the option value of it is huge, but you shouldn't expect us to be spending any meaningful amounts of money on that project in the near term. That was Debiensko.

On the non-cash gain, this gets rather technical. But it's basically an accounting impact of fair value treatment, or fair value accounting of the convertible.

I would suggest, if you go to page 17 of the OFR you actually have all the detail of what happened with the values of all the pieces of debt, and I think all the information is there. So perhaps it's best to start there, and if you still have follow ups I'll be happy to take it offline with you.

On CapEx, yes, we spent EUR15 million, and the guidance is EUR30 million to EUR40 million for the full year. What you need to see is that CapEx in a deep underground mining Company is of bulky nature, so it's not that we would spend 1/4 of the budgeted CapEx every quarter, or 1/12 every month.

And we have no reason to modify the guidance for the rest of the year. CapEx is one of the things that's very, very controllable in our business and we will simply not overshoot on the budget.

And your last question was on cash flow. Yes, there was an optically significant cash burn in the first quarter. In fact, we are very much in line with what we budgeted for the quarter.

And if you look at the production record in the first quarter, you'll clearly see that production will accelerate in the remainder of the year, particularly in the second half of the year, and that will reverse the cash burn so that -- our ambition is to end the year broadly neutral as regards net cash flow.

Does that answer your questions?

Robert Slater - *Silver Rock Financial - Analyst*

Yes, thanks very much.

Operator

(Operator Instructions). Felix Fischer, Lucror.

Felix Fischer - *Lucror Analytics - Analyst*

First question from my side is in regards to the current pricing environment for coking coal. Obviously, you secured quite a bit of your sales at fairly good pricing. Could you share with us what is the current pricing for coking coal, and what is your outlook there?

Second question is in regards to the inventory build-up. Obviously, you aim to sell some of the thermal coal excess inventory, will that be done at a deep discount? Or what is your expectation there? Thank you.

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

Thank you, Felix. As regards pricing, if you look at the current coking coal spot price that would be in the high $80s per tonne, so it has come off quite significantly since the beginning of the year. It's very difficult for me to give you any sort of number as regards the potential pricing for the balance of the coking coal sales for the 26%.

I think it's instructive to look at the contracting structure this year. We have actually departed the, quote-unquote, normal quarterly pricing in Central Europe for a significant portion of annual contracts. I think that's just evidence that people are more amenable to look at creative pricing structures. I think we are all motivated by trying to provide some level of visibility, hence, the longer-term pricing this year.

We are constantly in touch with our customers trying to see if there's a deal or a series of deals that makes sense for everybody, but the truth is I can't really say at what price the balance of coking coal will sell.

Inventories, there's quite a significant buildup in the first quarter. However, we expect to end the year with approximately the same level of inventory that we started, so we will see a sell-down in the remainder of the year. And we are not engaging in any sort of fire selling of the inventory; I think that would be self-defeating.

We are not nervous about the levels. We have storage capacity. And, if anything, the relatively high inventory provides more comfort as regards logistics and the ability to deliver the right thing at the right time to customers.

Felix Fischer - *Lucror Analytics - Analyst*

Okay. Thank you very much.

Operator

(Operator Instructions). Petr Bartek, Erste Group.

Petr Bartek - *Erste Bank - Analyst*

I only wanted to ask about production, which is quite low in Q1. If you can comment on the progress in production into the second Q, if there is an improvement. That's it.

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

Thank you for the question (inaudible). Yes, the production has accelerated in the second quarter, and will continue accelerating so that we will meet the guidance for the full year.

Yes, production was 20% down year on year in the first quarter of 2015, but that was planned. And we were very much on plan as regards production, and ahead of plan when it comes to the product mix.

Petr Bartek - *Erste Bank - Analyst*

Thank you.

Operator

Ide Kearney, GLG Partners.

Ide Kearney - *GLG Partners - Analyst*

I'm not sure if this question has been asked already, but I just wanted to follow up on the cash projections for the year, and on working capital trends. It's seasonal in the first quarter, but obviously, still, it was on the disappointing side.

I wanted to know if you can disclose what the current cash balance is, and how the working capital trends have evolved as the second quarter progresses. Thank you.

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

Yes, we will announce cash levels when we talk about the second quarter, later this year. I will say that our cash flow and our cash balances are developing exactly as budgeted, so far this year. And, as I think I said earlier, the ambition is to end the year broadly with a zero net cash flow.

Ide Kearney - *GLG Partners - Analyst*

And on working capital, have you noticed any changing trends or -- because obviously the market is difficult, and everybody knows it's difficult?

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

Yes, well, inventory has grown a little bit further since the end of the quarter, but, again, in line with -- this was a planned inventory buildup.

And there is one somewhat technical thing. We have reduced the amount of factoring at the end of March, simply because we didn't need it. Had we not done that, had we continued to factor sell receivables on the usual level, you may have felt better about the working capital development. But there's a price associated with factoring, so we just chose not to do it.

But working capital is under control. Yes, inventories have grown, that is the biggest portion, but I've commented on that, I think.

Ide Kearney - *GLG Partners - Analyst*

But the revolver draw as well, because there's a price associated --

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

The revolver?

Ide Kearney - *GLG Partners - Analyst*

The revolver -- the senior line draw. Is the factoring more expensive than the --?

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

No, it's not. It's definitely not more expensive, but it's just there's a price to pay. And we use factoring to manage short-term fluctuation in our available cash. We felt very comfortable towards the end of March, and so we chose not to do it.

Ide Kearney - *GLG Partners - Analyst*

Okay. Thank you.

Operator

Jason Cook, Gramercy.

Jason Cook - *Gramercy - Analyst*

Can you just discuss the sustainability of the reduced levels of selling and administrative costs? These are down pretty strongly year over year, and even against fourth quarter. Are these current levels sustainable? Or how should I be thinking about those?

And then, in particular within that, it looks like transport costs on a per unit-sold-basis was down pretty strongly as well. Is that sustainable at those levels? Thanks.

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

Thank you, Jason, for the questions. So, there are two separate topics. On the admin costs, my view is that they are not only sustainable, but there's more work to be done there. This is very much work in progress, and you should see some further improvements there.

On the transport costs, this is somewhat more complicated because the transport costs are driven by the price per unit of transportation, which has come down. Once there is a recovery in the market, this will reverse itself.

But it also depends on the average distance travelled for our product, and that fluctuates over time as the composition of sales fluctuates over time. So there's a big difference in the cost of shipping coal to the very east of Slovakia versus shipping to some of our customers that are almost across the street in Ostrava.

So the transport costs are cyclical and will grow once the market starts growing. The admin costs are going to come further down.

Jason Cook - *Gramercy - Analyst*

Great. That's it from me.

Operator

(Operator Instructions). There is no question at this time, sir.

Radek Nemecek - *New World Resources Plc - IR*

Thank you all for taking the time. And please feel free to contact us with any further questions you might have. Goodbye.

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

Thank you very much. Bye-bye.

Operator

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