



Nakilat (QGTC) 1Q19 Results

Earnings Call Transcript

April 23rd, 2019



Hosting: EFG Hermes Holding SAE

Conference Title: NAKILAT 1Q19 Earnings Conference Call

Moderator: Yousef Hussein

Date: Tuesday, April 23rd, 2019

Time: 13:30 (UTC+03:00)

Executives:

- 1) Hani Abuaker – Chief Financial Officer
- 2) Fotios Zeritis – Head of Investor Relations

Questions by:

- 1) Mohamed Meniawy – Sico Bank
- 2) Nafaz Alabbas – Areej Capital
- 3) Shabbir Kagalwala – Al Rayyan Investments

Operator:

Good day and welcome to Nakilat's First Quarter 2019 Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Mr. Yosef Hussein. Please, go ahead, sir.

Yosef Hussein:

Good afternoon, ladies and gentlemen. This is Yosef Hussein from EFG Hermes Research. Thank you for joining us today on Nakilat's First Quarter 2019 Results Conference Call. We have with us on the call today, the CFO Hani Abuaker and the Head of Investor Relations Fotios Zeritis. Without further ado, I'd like to hand the call over to Fotios to get us started. Please go ahead, Fotios.

Fotios Zeritis:

Good Afternoon everyone, welcome to Nakilat's First Quarter 2019 Conference Call. The transcript of this call and presentation will be available on the investor relations section of our website.



Now, please turn your attention to the presentation. On slide 2, we have a disclaimer regarding forward looking statements that are made in the presentation, slide 3 has the table of contents and on slide 4, you can find the glossary.

In addition, some of our remarks contain non-IFRS financial measures such as EBITDA. A reconciliation of this is included in the note of this presentation.

Now, I would like to hand it over to the CFO of Nakilat, Mr. Hani Abuaker.

Hani Abuaker:

Thank you, Fotios. Good afternoon everyone and thank you for joining us again for our first quarter earnings results conference call. As we've always said before; your participation is much appreciated and Nakilat strives to maintain transparency and open communication with all the members of the investment community.

I will begin the call with Nakilat's financial highlights for the first quarter of 2019. Fotios will take us through an updated overview of the LNG shipping market. Then I'll take you through our business outlook for the rest of 2019 as well as Nakilat's five-year strategic map. Then we're going to open the floor for all of you for any questions that you might have.

On slide five, we illustrate Nakilat's business structure in order to familiarize our company's profile, to new institutional investors who have recently placed us on their equity coverage radar. As you can see, there are a few business developments that have recently updated Nakilat profile.

The company continues to grow its international portfolio through the recent expansion with Maran Gas ventures, which included four additional LNG carriers. With the four LNG vessels under the new joint venture, Nakilat's fleet would increase to 74 vessels accounting for approximately 12% of the global LNG fleet in terms of carrying capacity.

Furthermore, Nakilat has signed an agreement with McDermott to form a joint venture company providing offshore and onshore fabrication services in Qatar. The new joint venture comes at a strategic time, as Qatar's ambition is to localize its energy sector supply chain and increase its LNG production in the coming years. Now, please turn to slide number six and seven.



As you can see, it has been an incredibly successful quarter for Nakilat in terms of delivering sustainable bottom-line growth for our shareholders by executing our well-planned business strategy. Nakilat has also achieved unparalleled operational efficiency.

Following the strong operating performance through rationalization of operational expenses and continuous growth, today, I am delighted to report great company performance results for both EBITDA and net profit for the first quarter of 2019.

This emphasizes Nakilat's ability to deliver impressive earnings and operating cash flow during a seasonally soft LNG spot market. Now I'll take you through Nakilat's financial performance. Our profitability has increased by 9% compared to last year's 1st quarter, mainly due to the acquisition of two LNG carriers and one FSRU. Another major factor that helped us improve our bottom line was a higher level of activity at our shipyard facility. Other critical elements that had significantly contributed to higher profitability were lower operating expenses and G&As, increase in interest income from bank deposits, dividends received from shares listed in Qatar Stock Exchange that are owned by the company.

Furthermore, Nakilat's EBITDA was up by 2.2% year-over-year to reach QAR 708 million. Operationally, our total expenses and G&A decreased in the first quarter by 1.1% and 3.2% respectively, compared to the same period in 2018. This is mainly due to Nakilat's continuous effort for cost optimization and ensuring that we employ enhanced efficiencies in every element within our operating model.

Also, our total operating expense decreased by 1.1% year over year. Turning to slide number nine, we can see a strong healthy balance sheet with total assets of QAR 29.9 billion as well as a cash balance of QAR 2.5 billion. The investment in joint venture increased mainly due to the share of operational profit, hedge gain and investment in new joint ventures.

Moreover, our scheduled debt amortization continues, as the repayment is freeing up our balance sheet capacity. Specifically borrowing has reduced by almost QAR 3.1 billion over the last five years, while at the same time we have acquired 11 additional LNG carriers and one FSRU.



Now, I would like to hand it back to Fotios to give you an overview of the LNG shipping market. So, Fotios, if you can please take it forward from here.

Fotios Zeritis:

Thank you, Hani. Now, I would like to give you an overview of the LNG shipping market. The world is thirsty for clean energy. This need has created a huge demand for LNG, which produces less carbon dioxide than coal and oil. In this prospering LNG market, the most precious commodity is the vessel. You need to understand that without LNG carriers, the LNG as a commodity cannot reach to any end user worldwide. If you turn to slide 11, although we saw spot rates drop in the first quarter, long-term contracts remain robust, clearly illustrating the strong fundamentals of the LNG shipping market.

You can see that when different companies such as trading house Vitol, the world's largest LNG buyer JERA and European Utility Endesa have chartered vessel for 8 to 12 years at healthy level of 70,000 to 75,000 per day. At slide 11 shows, shipping spot rates for DFDEs dropped from 66,500 per day in the first quarter of 2018 to 49,500 per day in the first quarter of 2019.

Following the same trend, spot rates for steam vessels fell from \$40,000 per day in the first quarter of 2018 to \$34,000 per day in the first quarter of 2019. This downward trend can be attributed to a mild winter, high LNG stock levels, and low gas prices which reduced the need for Asian markets to import LNG on long-haul routes lowering the demand for LNG ships.

The short to medium-term LNG Newbuild front remains healthy, with 13 LNG carriers on orders during the first quarter of 2019. The current level of LNG Newbuild price is approximately at \$190 million per vessel. We expect this rising trend to continue in the coming quarters. In relation to LNG trade, the global LNG import rose by 13% year-on-year in the first quarter of 2019.

The main contributors of this LNG growth demand were China with an increase of 15% year-on-year, and Europe with an increase of 81% year-on-year. The LNG supply growth during the first quarter came mainly from United States, Australia and Russia. Regarding the LNG supply, we observe that the total incremental LNG fleet growth was minimal at 2% in terms of number of ships during the first quarter of 2019.



If you turn to slide 12, you can see the development of global LNG fleet with 490 vessels in operation, and 112 vessels on order book, which implies an increase of 23% of the total LNG fleet, in terms of number of vessels as of March 2019. It is worth mentioning that approximately 40% of the current order book is charter-free and available to be absorbed by the new upcoming wave of LNG supply in the coming few years. The order book is a testament of the confidence of the LNG ship owners for the solid fundamentals of the LNG shipping market. During the first quarter of 2019, 90% of the global LNG fleet was chartered for longer than six months, 6% of the fleet was lay-up and only the remaining 4% was on the spot market.

Now if you turn to slide 13, you'll see that LNG shipping market balance is expected to be much tighter by 2020 as the new LNG capacity comes to the market. From this expected \$65 million tons of LNG which will come to the market by 2022, approximately 60% will come from the United States, which translates into an increase of ton miles and the need of shipping tonnage.

In the next 18 to 24 months, the LNG charter rates are expected to be volatile due to the ramping up of global liquefaction, US LNG export and high LNG demand from Asia.

In the short term, however, the LNG shipping market is expected to experience a seasonal softness due to the volatility of LNG price, delays in the startup of export projects, and some new builds that will be delivered ahead of the long-term employment.

Last but not least, we have added an interesting graph on page 13 within our presentation. This graph shows the LNG freight forward curves for steams, DFDEs and MEGI/XDFs until the third quarter of 2020. This recent development of LNG freight forward curve was produced by Affinity and gives a picture of the evolution of forward prices through time.

The creation of LNG shipping forward curves shows the rapid evolution of LNG market to a more commoditized market. Please note that the same solution was developed for the oil crude tankers market almost 20 years back.

Overall, the LNG shipping market is still much healthier than the previous years. I would like to conclude by saying that the new liquefaction plants and an increase in global LNG demand will maintain the strong fundamentals of the LNG shipping market.



Now I would like to hand it back to Mr. Hani to give you an insight into Nakilat's business outlook. Please go ahead.

Hani Abuaker:

Thank you again, Fotios. Moving to slide 15, I will take you through our business outlook for the rest of 2019. Nakilat is committed to meet all of its strategic objectives. As the world's largest LNG shipping company, we are fully prepared to take advantage of the strong market fundamentals that Fotios talked about.

In other words, Nakilat is very well-placed to be in a very favorable strategic position to secure potential future business opportunities to expand its LNG portfolio globally. Furthermore, we have a great degree of confidence that the momentum will continue with higher utilization of our shipyard facilities, given what's going on in the shipyard with a lot of maritime initiatives through the IMO new requirements and dry dock activities.

Also, you should expect to see an increase in JV income given the full impact of the two additional LNG vessels and the inclusion of one FSRU back in June 2018. In addition, we continue to focus on expanding our business portfolio in terms of strategically balanced growth and diversification. The strong fundamentals of the LNG market that Fotios talked about earlier, improved the sentiment of owners and created an attractive investment environment for us and anyone who is in the LNG shipping market, to capture new business opportunities and profitable assets.

As we did in the first quarter of 2019, we expanded our LNG fleet with four additional LNG carriers which will be fitted with the latest technology system. These vessels will be commercially and technically managed by Nakilat with the delivery time between 2020 and 2021. As we have highlighted before in the previous quarter, we would like to share with you Nakilat's strategy map for the next five years between 2019 and 2023 that has been approved recently by our Board of Directors.

In order for us to deliver on our vision to be a global leader and provider of choice for energy transportation and maritime services, we have spent a lot of time to understand how this vision could be translated into an actual outcome. Three major elements needed to be fulfilled, in order for us to achieve that vision.



One of it is basically the size and maintaining our market share. Not only we would like to be the biggest shipowner but also, we want to demonstrate our capabilities as an operator. That's where we look to be one of the top performers in terms of operational excellence. After having these objectives delivered, we would like to be acknowledged by our all of stakeholders and customers as a global leader by improving our brand value.

So, in order to do that, we have gone through an extensive top-down and bottom-up strategy analysis, which translated into four main strategic themes that all Nakilat's employees will focus on. We're going to look at sustainable growth, operational excellence, customer engagement, and organizational performance enablement.

To give you more color on Nakilat's four main strategic themes, you can see the expected outcome of the strategy plan at the top of the three columns such as boost profitability, increase market share, Nakilat to be a top performer and improved brand value. These expected outcomes are the result of our five-year strategy and will be visible to all the shareholders and stakeholders going forward.

Let me explain further, how the flow of the process works in order to have the final desired outcome on sustainable growth. We start at the bottom with organizational performance enablement. At Nakilat, we believe that our success has been and shall continue to be internally generated through a high caliber workforce that forms our most valuable assets. After which, we move upward to our internal processes such as materializing profitable business opportunities as well as build market intelligence and capabilities to develop our growth strategies.

I just want to highlight these items that I'm talking about, have lots of initiatives and KPIs behind them in order for us to deliver the outcomes at the top. When both enablers and internal processes are set, we go ahead to deliver an integrated energy transportation service to our customers. As a result, we believe that we will be able to increase our market share and boost profit potential for our shareholders.

As per Nakilat's five-year strategy, you can also see that the same defined path for operational excellence and customer engagement. For operational excellence, the main objectives are to continue to be one of the top performers. To meet these objectives, we need to provide a safe and reliable service, improve our cost efficiency, and enhance performance through effective monitoring and evaluation. We want to be the provider of



choice; when people think about reliability, safety and cost effectiveness. We believe that we will be able to manage our cost structures, so we can save more money in the way we operate by reducing Nakilat's per-unit cost. This will translate to an actual bottom line and profit increase.

For customer engagement, the main objectives are to improve Nakilat's brand value. We're going to continue to do intensive IR activities to promote our corporate image and establish customer value. The main scope of this strategic theme is to provide the optimum outcome for Nakilat's shareholders such as boosting the profitability, increasing market share, to be a top operational performer and improve Nakilat's corporate brand.

We can now open the floor for questions.

Operator:

Thank you. If you would like to ask a question, please signal by pressing star one on your telephone keypad. If you're using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, press star one to ask a question. We'll pause for just a moment to allow everyone an opportunity to signal for questions. We'll now take the first question from Mohamed Meniawy from Sico. Please, go ahead.

Mohamed Meniawy:

Hi, everyone. Thank you for having the call. I have a couple of questions if you don't mind. How does your charter rates compare to the ones mentioned in the long-term contract, which I suppose to be of the same – with the government which is if I'm not mistaken 20 plus years?

Fotios Zeritis:

Look, the charter rate as we shared for the JERA or Trafigura is approximately \$70,000 per day to \$75,000 per day. Actually, Nakilat's long-term contracts are higher.

Mohamed Meniawy:

I'm sorry, it's what?



Fotios Zeritis:

Nakilat's charter rates are higher. Our charter rates for our long-term contracts are higher.

Mohamed Meniawy:

Okay, and when is your next contract with the government expiring?

Hani Abuaker:

Our contracts usually with Qatar Gas are long term, meaning that they are 25 years. So, if you assume that the contract started ten years ago, then we would expect that after 15 years there's an option of renewal of five to ten years. It has an option built into it.

Mohamed Meniawy:

Okay. My second question is regarding your account receivables. I can see QAR 400 million in fees and receivables in the first quarter. Can you please clarify that?

Hani Abuaker:

Can you repeat the question please?

Mohamed Meniawy:

Yeah, yeah. Regarding the receivables, I can see a QAR 400 million increase in your receivables at the first quarter. So, can you clarify on that?

Hani Abuaker:

Yes, that's mainly due to advances increased in Nakilat Agency because of new Hub agency business with Wilhelmsen. Also, you can see an increase in Accounts Payable as well. So they kind of offset each other with some time difference. I can give you more details after the call if you don't mind. I can give you the details of the breakdown and the reason for that.

Mohamed Meniawy:

Yes, that would be great. Thank you.



Hani Abuaker:

We will take it as a point and we'll send everyone the details about the increase in QAR 400 million.

Mohamed Meniawy:

Perfect, thank you very much.

Operator:

The next question will come from Nafaz Alabbas of Ajeej Capital. Please, go ahead.

Nafaz Alabbas:

Good afternoon, gentlemen. Thank you again for the call. And congratulations on the great results. I just have a question regarding the news that QP invited tenders for reserving ship construction capacity for LNG carrier fleet for its Northfield expansion project. Is this going to be separate from your company or would that bring an opportunity for Nakilat to expand their fleet because, obviously, if Qatar continues and successfully increases their capacity to the 110 million from the 77 million tons of LNG, wouldn't that require more ships from Nakilat to basically handle that capacity?

Hani Abuaker:

Yes, it's an interesting question. First of all, any information about the expansion it is a clear decision for Qatar Petroleum and Qatargas. We, as Nakilat, cannot comment on their behalf. They do their own assessment and exercises about the number the vessels that is needed. However, I would like to highlight to you that we have a long relationship and collaboration with them already through our current portfolio.

We believe that Nakilat as the largest shipping company that is based in Qatar, with a successful proven track record of commercial and technical and operational expertise. We aim to grow our portfolio internationally or locally and diversify our clientele.

However, as we said before, we are always going to be happy and ready to support Qatar's plans to expand their LNG production by providing them our LNG shipping



capacity or expertise. Definitely, we are happy to participate and be part of that expansion. However, we would always look to see if it is an economically feasible project, like any other project. So, I think it's premature to provide any further details. However, we will be aiming to really secure the same.

Nafaz Alabbas:

Thank you very much. I just have a small follow-up question. I know it's difficult to give a clear answer. We're just getting better – we are just asking for an approximate expert trajectory just to understand. Because the question basically is, do you have the balance sheet capacity to grow your main LNG fleet significantly? I mean just talking a bit about very rough numbers without any precise answers. Let's say if you need to increase by like ten or so number of large vessels to meet this capacity for example. I mean we are just talking about a hypothetical scenario. How much would you – I mean do you have the capacity to raise debt for that or do you think you will need a rights issue? – I want to get a rough understanding of what are the options for Nakilat – in case they have this demand, do you have the capability to basically do it? I understand the market will be very supportive to the company because you have done a great job so far and you're reducing your debt. That is great. And I think with the long-term contracts that you have many options I think. You can still go to the debt market and it will increase your leverage – if you want to expand their fleet. But is that an option or do you think there are limitations?

Hani Abuaker:

Okay. It goes without saying that we, at Nakilat, will aim at maximizing the number of LNG vessels that we can secure and any tender that is available for us, whether it's locally or internationally. I think we have a strong balance sheet which gives us a lot of financial strength to secure the required capital to maximize the number of vessels that we can get for any kind of a project.

So, we have a lot of options that we will explore in order for us to maximize our shareholder's returns. Yes, I can say that we've got a lot of options that we can explore to ensure that we can secure the maximum out this tender or any potential tenders that can come to Nakilat. Hopefully we will let you know, but in the near future. However, it's premature to discuss because there's a lot of details still not available such as the cost of



these vessels and the number of vessels, to be more specific. Are we as a company, getting ourselves ready for this potential opportunity? Yes, for sure. We are looking at our internal capabilities and financial strength and options to secure whatever capital that is required.

Nafaz Alabbas:

Great. Thank you very much. Thank you.

Operator:

As a reminder, if you'd like to ask your question, you can signal by pressing star zero –star one my apologies. The next question will come from Shabbir Kagalwala of Al Rayan Investment. Please. go ahead.

Shabbir Kagalwala:

Gentlemen, thank you for the call. I had just one question. You mentioned about adding four ships this quarter by Maran JV and expected time of delivery of 2020-21. Are these new vessels being currently under construction or some brownfield vessels just that's retrofitting based on the specifications? And do you have any current long-term charters on these vessels? Thank you.

Fotios Zeritis:

As we have announced, we have four vessels. They are under construction in South Korea. It's expected to be delivered in 2020 and 2021. We are formulating a commercial strategy for these vessels. We'll handle the commercial and technical management of these new vessels. Now it depends on the strategy and opportunity that we'll have. We'll look at everything possible whether it is long-term or medium term. In the end, it all depends on whatever makes economic sense.

Shabbir Kagalwala:

Also, as of now, you don't have a set charter on it. So, once it comes closer to the delivery time, you will have formal charters on it? And will it be deployed in the region or it will be outside or is anything decided on that?



Hani Abuaker:

As we have these vessels to be delivered in the later part of 2020 and 2021. We are already doing our homework by marketing them for international clients. Even if any clients that are available, whether locally or internationally. These vessels are going to be delivered in the later parts of 2020 and some of them in 2021. We should really expect them to be international customers as we've – what we have done for the last 11 vessels which were jointly owned with Maran.

Shabbir Kagalwala:

Perfect. Thank you very much.

Operator:

There are no further questions at this time. I'd now like to turn the conference back to your host for any additional or closing remarks.

Hani Abuaker:

Thank you all for participating in our conference call. We will always encourage you to participate in the future. We are very happy for any comments that you guys might have any time even after this conference call.

Fotios Zeritis:

Thank you so much for your interesting questions. All your questions were well-received. And as Hani said, we'll communicate the capital markets feedback always to Nakilat's top management. Thank you so much for taking the time to join us today. Have a great day.

Operator:

This concludes today's call. Thank you for your participation. You may now disconnect.