QNB FINANCIAL SERVICES

Moderator: Shahan Keushgerian
May 1, 2014
8:00 a.m. ET

Operator: Thank you for standing by and welcome to the MILAHA Company First Quarter 2014 Financial Results conference call.

At this time, all participants are in a listen only mode. There will be a presentation followed by a question and answer session, at which time, if you wish to ask a question, you will need to press star one on your telephone. I must advise you that this conference is being recorded today Thursday, the 1st of May 2014.

I would now like to hand the conference over to your speaker today, Mr. Whitney. Please go ahead, sir.

Keith Whitney: Hi thanks, Operator, very much. Hi, everybody, this Keith Whitney from QNB Financial Services. I'd like to welcome everybody to the MILAHA Q1 2014 financial results conference call.

I guess first of all everybody I would like to apologize for the technical assistance that we had – technical issue we had yesterday. And I am hopeful that it didn't cause too cause too much inconvenience for everybody.

In terms of the MILAHA management team, I'd like to welcome Gautam Bellur, who's the Senior Vice President of Corporate Development & Communications. As well as Sami Shtayyeh, who is the Vice President Financial Planning & Analysis for today's call.

In terms of agenda, we'll walk through a company presentation and overview covering some of the Q1 numbers from Sami and Gautam. And then we'll go ahead and open the call up to questions and answers.

So without further ado I'll go ahead and hand the call over to MILAHA.

Gautam Bellur: Thanks, Keith. Thanks everyone also for joining in the call today. As Keith mentioned our agenda is pretty similar to previous calls. I'm just going to make a few opening remarks and then turn it over Sami to discuss the Q1 results in detail.

And then I'll come back and provide a brief outlook on the rest of 2014 for each of our segments. And then we'll throw it open to questions.

In terms of our results overall, I think it's fair to say Q1 was mixed at best. While we managed to maintain overall profit numbers relative to Q1 2013, we're obviously somewhat disappointed with the results in a couple of our core segments. The good news is that the gas and (petchem) segment which has remained relatively steady in the last couple of years without too much growth one way or the other, delivered some pretty strong growth in Q1 over a 30 percent in terms of both revenues and net. And our capital segment also performed strongly with obviously dividend growth being one of the key drivers.

On the flip side both the maritime and logistics in the offshore segments delivered pretty weak results in Q1 a sharp drop in profits in both segments are relative to Q1 last year. And while some of the causes were beyond our control to be fair we nonetheless fully recognized the need to refocus our efforts on some fundamentals to turn around these results for the rest of the year. I'll talk about a little bit more about that later on.

With that, I'll just turn it over to Sami to discuss the financials in more detail.

Sami Shtayyeh: Thanks Gautam. To start things off let me go over the published consolidated financial results for our first quarter. Operating revenues for Q1 2014 were QR699 million compared QR703 million in 2013, for a decrease of 1 percent.

Operating profit for Q1 2014 was QR273 million compared to 283 million in 2013 for a decrease of 3 percent. And net profit for Q1 2014 was QR349 million compared to 345 million for an increase of 1 percent.

I'm now going to get a little more into the figures highlighting the large variance items versus 2013 and explaining them. But the approach I'm going to take this quarter is to walk through really pillar by pillar so if you're looking at our presentation that was posted to our website earlier this week you should be able to follow along with me.

Starting off with maritime and logistics overall revenue decreased year over year by QR11 million. And the main contributing factors for this were lower than expected activity in our ship yard, logistics and container feedering businesses. Container feedering was negatively impacted by lower export volumes out of Mesaieed port – sorry out of (Mesaieed) which was due to plant shutdowns at one of our major exporters. The shutdown bled through part of April and we expect to be back to business as usual in May. Partially offsetting those issues was modestly higher port volumes.

On the expense side from maritime and logistics overall though it was flat versus 2013, we had some higher variable expenses related to the increased port volumes particularly salaries and wages. And lower variable expenses for the ship yard.

Container feedering and logistics are in large part fixed costs in nature so their revenue dropped really went right down to our – right down to the bottom line. On the non-operating income side of things in 2013 we sold more underutilized and aged equipment than what we sold 2014 so you can see a drop in the gain on sale of assets which drove a negative variance of approximately QR3.8 million.

On to offshore overall revenue decreased by QR12 million and this was almost entirely from one of our main revenue generating units within offshore which is our diving operations. We had a series of issues that hit all at once including a dry docking for vessel that took over twice as long to complete than was originally planned.

We had the delay of a new built vessel that we anticipated would be joining the fleet in Q1 but didn't. And we had some equipment breakdowns on other existing vessels all that effectively hurt our utilization percentages.

On the cost side we were – we had higher operating expenses related to the new diving vessel which essentially incurred full crewing costs. In shore we lost revenue due to these events but yet continued to incur costs and unfortunately that's, you know, a perfect recipe for a disappointing quarter which is exactly what we had.

On to the gas and petrochem, overall revenue increased by QR13 million and this was driven really by increase rates in our five wholly owned product tankers as well as additional revenue from our port and marine operations where we gradually have been receiving more boats. These are the harbor boats I'm referring to.

On the expense side costs increased mainly related to the addition of some of these new harbor vessels. Under the non-operating income and expense category we saw an increase of QR16 million from our JV's and associates with 10 of that coming from our 30 percent share of Nakilat and the balance coming from our other joint ventures.

Our trading pillars saw a decent uptick in revenue to the tune of QR5 million Riyal's with associated costs of goods sold in the amount of QR4.6 million and both increases came mainly from our bunker sales unit. Last but not least our capital pillars saw an increase of 8 million Qatari Riyal's in additional revenue. And although the net increase was only 8 million this included overcoming a QR30 million gain on a sale of a portfolio from 2013, which did not repeat obviously.

In addition our Qatari Quarry subsidiary saw a drop of QR4 million overcoming both of these capital posted at QR3 million – QR3 million additional rent revenue and very strong returns from our investment portfolio both in terms of dividends as well as realized and unrealized gains.

On the expense side you'll see some drops in several categories and that is really tied to the drop in Qatari Quarries revenues. That really sums up our operations and brings us to an overall net income of QR349 million. And with that I'll now turn it over to Gautam who will go over our outlook.

Gautam Bellur: Thanks, Sami. In general I think it's fair to say our operating outlook for the rest of 2014 is more positive than Q1. As I mentioned earlier we'll be refocusing our efforts on both the top line and the bottom line in the maritime and logistics segment.

Some of the factors that contributed to a weak Q1 as Sami mentioned such as the unexpected plant shutdowns will go away from May onwards. So we expect a recovery in the feeder business which took a big hit in the first quarter. In the port management business we hope to see higher growth than the six percent we saw in Q1.

That said and as we've said in previous calls we remain extremely cautious about a sustained ramp up in infrastructure projects. There is a element of unpredictability about the growth in volumes and it's not a question of if but when and how fast. In addition to the revenue side of things we're taking a much harder look and have been for the last few weeks at driving costs and process efficiencies across the different units of the maritime and logistics segment. On to offshore, we expect the offshore segment to improve strongly over Q1.

We are pretty close to sorting out some of the main operational issues like the breakdown that Sami mentioned and the consequent (fire) that went with it. And we'll be taking – deploying a new diving service – diving support vessel into service in the coming weeks. Both of these will help the diving operations numbers recover from Q1. And diving operations as Sami said have a fairly significant impact on our overall offshore segment financials.

In other parts of the offshore business our focus is going to be utilization – utilization – utilization. We're looking beyond our traditional core markets in the region for opportunities to improve our utilization numbers over the rest of the year and deploying some of our fleet outside of our core markets. In addition we're taking delivery of eight new vessels offshore vessels between May and October – November this year.

Although, given the timing of the deliveries and the contracts start dates which are not necessarily always in sync the impact on overall revenues is likely to be less than what we had originally anticipated for 2014. And as we've said all along we're spending a lot of time looking at both organic and inorganic growth opportunities in both our existing as well as new markets in offshore and will continue to do so. Though the timing is obviously not something we can predict at this time.

You know, gas and petrochem segment, we either expect to maintain steady stake or grow moderately depending on the specific markets within that segment. As, you know, we're involved in the LNG the LPG, ammonia, clean and dirty petroleum product sectors as well for historical reasons harbor marine operations.

In the LNG space we expect limited fluctuation of the results from the nine jointly owned LNG carriers due to the long term nature of the contracts. We may incur some refinancing costs over the next 12 months on some of these vessels but that's about it.

We're seeing a stronger year for VLGC's finally. Of which we own – jointly own four in a JV. Recent rates have gone through the roof and while, you know, we obviously don't believe this is – that those kinds of rates are sustainable we still think it's going to be a better year overall for VLGC's. Something we'd anticipated last year and it's good to see that it's actually coming true.

We expect our product anchors and our ammonia carriers to remain steady or perhaps marginally improve over the rest of the year. And then in the harbor vessel operations, the harbor marine operations we refer to we're going to be taking delivery of the remaining eight vessels of the 19 vessel order in the coming months.

So as we have said before these are to be deployed in a 20 year harbor marine operations contract with Qatar petroleum. And in addition to the 19, we're also likely to redeploy some of the existing vessels that we have that are currently working on that contract. We're likely to redeploy them to other contracts. So overall, I think we'll get a nice bump in both the top line and the bottom line from these operations in 2014.

You know, our trading (filler), we're starting to see strong demand in our trucks and heavy equipment agency business. The order backlog looks strong. So we expect stronger performance in that particular unit going forward. And the story is similar for our agency – for our travel agency business as well. Bunker already looks higher this year but it's hard to – a little difficult to predict what the rest of the year looks like on the bunker side.

And in our capital segment our plan realistic development projects are progressing according to plan. We expect to complete a commercial development later this year towards the end of Q3 or by the end of the year hopefully, which we'll use as our new headquarters in all likelihood. The other projects that we have in the pipeline are likely to come online between Q1 2015 and sometime around mid-2016.

With that, we'll throw it open to questions.

Operator: Thank you, sir. As a reminder if you wish to ask a question please press star one on your telephone and wait for your name to be announced. If you wish to cancel your request please press the hash key. So that is star one to ask a question.

You have a question from the line of Shahan Keushgerian. Please ask your question.

Shahan Keushgerian: Hi, Sami and Gautam, just a few questions on my end regarding the offshore segment. What would you say the utilization rate was during the first quarter and what do you expect for the rest of the year approximately?

Gautam Bellur: The utilization rate for the first quarter was – it depends on the segment. They have – they vary from segment to segment. If you look at – well I'll give you an example, give me just a second. If you look at sort of the non-diving vessels and the non-construction vessels utilization was in the range of about 86 percent.

You look at the construction and maintenance vessels they are in the range of about 75 percent. We had an issue with one of the vessels there. And then on the diving side which Sami talked about we had a net utilization – I won't give you a number but let's just say it's (sub)-50 percent. So that's obviously the big reason for the numbers this quarter.

Shahan Keushgerian: And what do you expect for the rest of the year or is it too early to…

Gautam Bellur: I think it's difficult to say what we expect for the rest of the year. Historically we've been – currently we've been, you know, higher than – much, much higher than that and it also depends on whether you're in the spot market or the long term market, right. So the utilization rates defer quite significantly depending on which market you're in even though the rates make up for the lower utilization on spot market versus the long term charter market.

So it's hard to say what the utilization is going to be but obviously not where we have it right now.

Sami Shtayyeh: Yes, let me just add, Shahan, diving operations makes up by far the biggest – they're by far the contributor to offshores – hello?

Shahan Keushgerian: Hello.

Sami Shtayyeh: Yes, I was saying, offshores contribution to the net income is by far larger than any other and that's really where the utilization really, really took a hit. That's the one where we expect to recover definitely higher then Q1 but for us to place a figure on it we really would rather not so we'll just leave it at that.

Shahan Keushgerian: All right and the other question is regarding the investment income. How much realized and unrealized gains did you guys incur the first quarter?

Sami Shtayyeh: So, in 2013 we sold a portfolio which brought in a again of QR30 million. We overcame that. The realized and unrealized is approximately QR60 million.

Shahan Keushgerian: OK, great, great. Thanks, that's all from me.

Sami Shtayyeh: OK, thank you.

Operator: Once again if you wish to ask a question please press star one on your telephone and wait for your name to be announced. If you wish to cancel the request, it's the hash key.

You have another question from the line of Prashanth Uppuluri. Please ask your question.

Prashanth Uppuluri: Good afternoon, Sami and Gautam, thanks for doing this. If I can ask again about offshore? Are the Q1 issues kind of behind you or are you still kind of working through some of that? And can you give me kind if the expectation of timing was it end of April, May?

Sami Shtayyeh: Yes, some of the issues, Prashanth, thanks for the question. Definitely some of the issues are behind us. To be quite frank with you some of the issues are kind of still with us. This is why we said we expect better than – Q2 to be better than Q1 but the issues that are still with us we really feel like it's an issue of a matter of weeks rather than months to fully rectify them.

Prashanth Uppuluri: Right.

Sami Shtayyeh: The new vessel we're – the new vessel that Gautam mentioned and I briefly touched on that right now is in seas trials and in the commissioning phase. So we've taken possession of it. We expect that to hopefully add revenue to our business in the coming, you know, weeks …

Gautam Bellur: Three to four weeks, yes, max.

Sami Shtayyeh: So that's really going to help matters. So, it's not fully recovered in the sense that it's not earning revenue today but, like I said, it's in the sea trials and commission phase. It's in the local waters and the regional waters. So, you know, does that answer your question?

Gautam Bellur: Yes, it's a question of weeks, Prashanth, yes, not a question of months.

Prashanth Uppuluri: Yes, OK, OK, I guess kind of a long the same lines the kind of (inaudible) fields you had a maritime business in Q1. Is that, kind of, again, completely behind you or are you still working through some of that as we speak?

Gautam Bellur: Well some of the – the maritime is a little bit different because the maritime a chunk of it was driven by unplanned plant shutdowns which restricted exports or which reduced the exports going out of Mesaieed.

That I think is being resolved right now. The expectation is starting May, I think, that it was fixed in April, we're in April the end of April now, but May we expect to see volumes return to normal on that one. But that's what – that's just one aspect of it, right.

Sami Shtayyeh: Yes, and this was well – this was well publicized in the paper so.

Gautam Bellur: Yes, if you look at some of the other (elicit) companies in Qatar that are involved in Mesaieed, you will see their numbers taking a hit in first quarter.

Prashanth Uppuluri: Right.

Gautam Bellur: And it's not going to effect on us. The parts that we're impacted by which is really the polymers export, which is what we do on the container side, that should be resolved, you know, from May we should be seeing normal, you know, business as usual on that.

The rest of the maritime a logistic pillar it's a little bit of a different issue. You know, we obviously have volume growths that we expect in the ports, import volume growth due to the, obviously, the projects and so on.

We've seen about 6 percent growth probably below what we would have expected in the first quarter. But that's why we're a little hesitant to say what it's going to be going forward. It seems to spike and drop and spike and drop and there isn't a sustained, you know, 10 percent, 12 percent annually that you would expect.

Prashanth Uppuluri: Right, OK. Thank you for that.

Operator: There are no more questions at this stage, sir. Please continue.

Keith Whitney: We will wait another minute or so for questions.

Gautam Bellur: Yes, I believe one may be coming through.

Keith Whitney: Sure.

Operator: Yes we actually have one question from the line of Shahan Keushgerian. Please ask your question.

Gautam Bellur: Go ahead, Shahan.

Sami Shtayyeh: Hello?

Gautam Bellur: Hello?

Operator: I'm not sure what's happening.

We have another question from the line of Prashanth Uppuluri. I'll let him ask his question first.

Prashanth Uppuluri: Hi, hi, thanks there. Just on gas (petchem), I guess the LNG – the LGC businesses, I mean, we've – yes, they've been around the new one really is the QP contract for 20 years and I recall that contract value at QR1.9 billion. Now is it as simple as saying 1.9 divided by 20 is the revenue you expect to make from that?

Gautam Bellur: Yes, roughly that's about right.

Prashanth Uppuluri: And any indication on margins?

Gautam Bellur: Nope, not that we – we obviously can't talk about margins on contracts but a good question. But the revenue side yes it was I would publically announce that it was QR95 million a year over 20 years.

Sami Shtayyeh: Yes, Prashanth, let me just add something. So, I don't want you to think that it's QR95 million incremental. A couple of things, we actually were performing the – that contract prior to its renewal.

So we've got vessels that we're performing, you know, against the old contract, it was renewed and the renewed contract stipulated the fact that we were going to go out and purchase 19 new vessels and it was for a duration of 20 years and the contract value was QR1.9 billion.

So, it's not QR95 million incremental revenue or accretive revenue, it's kind of difficult to back in what the actual incremental is. That's one thing I want to say.

The other thing is we have not taken full position of the 19 so the QR95 million would obviously be in effect when we have all 19 vessels employed.

Gautam Bellur: Employed, yes.

Sami Shtayyeh: Which should be later this year like Gautam said.

Prashanth Uppuluri: OK, that's helpful thank you.

Operator: OK, now we can open the line of Mr. Shahan Keushgerian. Please ask your question, sir.

Bobby Sarkar: Hi, this is actually Bobby Sarkar from QNB Financial Services, as well. Just sort of quick question. You guys had a strong uptick in your Milaha gas and (petchems) this quarter. Can you just talk a little bit about what you are seeing in terms of your – the LPG market and the rate environment going forward please? Thank you.

Gautam Bellur: Yes, to the LPG our exposure to LPG is in two ways. One is the JV that we have at Nakilat which is Gulf LPG where we jointly own four VLGCs. And then we have the two smaller handy size ammonia carries that we fully own and operate.

The rates for VLGCs and, you know, large gas carriers has gone through the roof this year. It was relatively weak at the beginning of the year, I mean, or it continued on from last year which as it was starting to pick up but then over the last few weeks it's gone through the roof.

The expectation is that, you know, over the course of the year it's going to stabilize but at a higher level than we've seen in the last couple of years on the VLGC and LGC side. So they – that's the good news now in terms of what those rates are going to be it's a little hard to tell.

I mean we're currently if were to take the last couple of weeks you're looking at, you know, QR3.5 million a month in terms of the rates. Obviously that's a pretty unsustainable and this is – we're talking relative to, say, 750, 800 last year, right. So, you can imagine what the jump in.

So, presumably the rest of the year on a sustainable basis is somewhere in the middle of that. Probably closer to the QR750, I would argue then the QR3.5 but it's hard to say what it's going to be.

On the two ammonia carriers, there's a little bit of a knock on effect from the VLGCs going through the roof and so on. Further down the size spectrum, if you will, the difference is our gas carriers actually carry ammonia so we need to convert to carry OPG.

In terms of the pure ammonia itself, you know I think were – we're not expecting those rates to go up significantly this year.

Bobby Sarkar: OK, great, thank you.

Operator: There seem to be no further questions, sir. Please continue.

Keith Whitney: OK …

Gautam Bellur: No, thanks, everyone for joining and, you know, if there are any other questions feel free to reach out to us by e-mail. And we'll do our best to get back to you as quickly as we can.

Keith Whitney: All right. And just another note guys that the investor presentation is located on Milaha.com, so you can go to the Investor Relations schedule section of the website and you can find the updated Q1 presentation or you can contact us at QNBFS who can also provide the presentation as well.

But I want to thank – special thanks to Gautam and to Sami for their insight and thanks everybody on the call today for their interest and queries today to the management team. I want to wish everybody a great day and a great rest of the week.

Operator: That does conclude our conference for today. Thank you for participating. You may all disconnect.

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