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Q2 2017 Dampskibsselskabet NORDEN A/S Earnings Call
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C: Jan Rindbo; Dampskibsselskabet NORDEN A/S; CEO
C: Martin Badsted; Dampskibsselskabet NORDEN A/S; EVP, CFO

+++ presentation
Operator^ Welcome to the NORDEN Second Quarter Report 2017 Conference Call.

Today's conference is being recorded.

At this time, I would like to turn the conference over to Jan Rindbo, CEO.

Jan Rindbo^ Welcome to the presentation of NORDEN's Second Quarter Results for 2017. Thank you for calling in. My name is Jan Rindbo, and I'm the CEO of NORDEN, and together, with our CFO Martin Badsted, I will be presenting our results today.

I trust you have all found time to download the accompanying presentation available on our website. We will go through selected slides, and we will refer to the specific slide pages as we go along. Please note that this presentation and the following Q&A session will be recorded, and made available on our website.

Slide 2, please.

The agenda for today will be as follows. I will start by outlining the highlights of second quarter, the key financial figures for the period, and a strategy update. Martin will then give you our view on asset values and market conditions. Finally, I will conclude with our guidance for 2017, and we will open up for the usual Q&A session.

Slide number 3, please.

In the second quarter of 2017, the adjusted net result was minus-$3 million, which is slightly lower than in the first quarter of 2017. The dry cargo market continued its gradual improvement from the first quarter driven by strong Chinese imports. However, this was not enough to secure a positive net result in the dry cargo department, which ended at minus-$7 million.

The tanker market weakened further during the second quarter of 2017, which also lowered the tanker result. However, the adjusted net result remained positive at $3 million on the back of strong operational performance.

We have in the second quarter bought to second-hand MRs. This is part of an effort to start increasing our tanker exposure after a period where focus has been on selling vessels, and taking cover.

We have narrowed the guidance range for 2017 to minus-$20 to plus-$20 million. In light of the results in dry cargo for the first half of 2017, it is no longer realistic that we reach the upper range of the previous guidance of a positive result of $40 million.

Please skip to page number 5.

Going forward, dry cargo will be split into two separate units with separate reporting. This is done to strengthen the focus on the very different parts of NORDEN's dry cargo activities, as well as to increase the level of transparency of value creation.

The dry cargo operator unit will aim to generate value through short-term activities and optimization, while the dry cargo owner unit will manage NORDEN's position towards the longer-term market developments. The split is expected to be fully implemented during the third quarter of 2017.

For tankers, we have besides buying the two MRs -- used the weak market to expand our long-term tanker capacity at attractive rates. This capacity expansion combined with expectations of an improving tanker market makes NORDEN well-positioned to gain from market upsides.

Lastly, project cost drive is on schedule, with annual savings of more than $18 million achieved.

And now, over to Martin for a closer look at the developments in asset values and markets.

Please turn to page number 7.

Martin Badsted^ Thank you, Jan.

Following strong dry cargo asset price increases in Q1, the market took a bit of a breather in the second quarter, ending the quarter about 3% lower.

In tankers, buying interests and a lack of sales candidates pushed prices higher, but with a weakening of spot markets over the summer, the increases have leveled off for now.

Please note that, in addition to its own fleet, NORDEN has close to 30,000 open vessel days in dry cargo over the next five years on long-term charter, which will also appreciate significantly in value if the market improves as expected.

Next slide, please.

Even though spot rates declined at the beginning of the quarter in dry cargo following the strong finish to Q1, the market continued its gradual improvement on a year-on-year basis. Supramax and Panamax rates were about 50% and 80% higher than last year, respectively.

Demand continues to be driven by strong Chinese import growth, whereas the contribution from demand in the rest of the world is very limited. As for Chinese imports, iron ore has been the big factor in Q2.

Coal imports still improve significantly on a year-on-year basis, but volumes have been falling slightly, and growth rates could turn negative on a sequential basis in the near future, mainly as a result of rising local production following the easing of mining restrictions put in place last year.

Minor box also contributed strongly, especially within bauxite and soybeans.

Next slide, please.

The gradual market improvement is expected to continue in dry cargo. Even though the demand push from Chinese fiscal stimulus and coal mining restrictions is likely to decelerate, demand is still supported by strong steel margins, and new iron ore capacity coming on stream. Coupled with a much slower supply growth, this should provide the basis for a tighter market.

Although newbuild ordering has picked up, it remains at a low level, which provides an important foundation for future market normalisation.

Next slide, please.

The tanker markets have a strong start with Q2, but ended on a weak note similar to last year. High supply growth in both crude and product tankers continues to put pressure on rates, and high inventories mean that temporary imbalances are quickly absolved without significant rate increases.

On a positive note, the MR segment did relatively well compared to other vessel types proving that, even in weak markets, NORDEN's commercial vehicle, the Norient Product Pool, is able to generate above average earnings due to triangulation and voyage optimisation efforts.

Next slide, please.

Looking forward, the product tanker market is expected to remain relatively weak in the rest of 2017, but gradually improve in 2018. Product tanker supply growth is declining substantially in the coming quarters, whereas, demand growth is expected to keep momentum due to a world economy expected to grow at a decent pace.

Crude supply growth is expected to remain elevated through 2018, which we think will limit the strength of the expected product tanker recovery, though not completely eliminating it.

Now back to Jan for a look at our guidance.

And next slide, please.

Jan Rindbo^ Thank you, Martin.

As mentioned earlier, we have reduced the adjusted net result guidance level for 2017 to minus-$20 million to plus $20 million, as it is no longer realistic to reach the upper range of the previous guidance.

As a consequence of the results from the first half of 2017, the dry cargo expectations have been lowered to between minus-$25 million and minus-$5 million. It should be noted here that after the end of the second quarter, we've opened up the book in dry cargo, and as of primo August, we have around 5,000 open vessel days for the balance of the year.

The tanker market, however, developed as expected, and the guidance for the tanker segment has been maintained.

Next slide, please.

And please remember that there are uncertainties related to any forward-looking statements.

Next slide, please.

And this concludes our presentation. We will now open up for the Q&A session. Please await the conference host's instructions.

Is the conference host available?

+++ q-and-a
Operator^ (Operator Instructions)

Frans Hoyer, Jyske Bank.

Frans Hoyer^ Two questions, really. What -- I haven't quite picked up the point about the cost savings drive. Maybe you could talk about the -- well, the scale of the benefits, I heard about the timing, and also, the new organization, the split of the organization, into two entities in dry bulk.

How, if you were to kind of flesh that out in greater detail, what do you expect to be able to achieve, I'm thinking financially, in terms of P&L, and also timing, please.

Martin Badsted^ Yes, hi, Frans. Let me just reply to the first part of your question about the operational cost savings.

Where we have worked on what we call our project cost drive for some time now, where we have set ourselves a target of saving $20 million on an annualized basis by the end of 2017. And with the projects that have been implemented so far, we are at about $18 million, as we have said, and we believe that we are still on track to reach the full $20 million by year end.

The main focus of these cost efforts are within the technical management costs, saving on OPEX on our own fleet, and also, on dry docking costs, and also, on the voyage costs that we incur for all the voyages that we have on both dry and tankers. There's a little bit also on the administrative side, but the bulk of the savings are clearly within technical cost and voyage costs.

Frans Hoyer^ And the $20 million savings is relative to which year? 2015, or?

Martin Badsted^ Yes, that is relative to 2015.

Frans Hoyer^ Thank you.

Jan Rindbo^ And, Frans, with respect to your second question regarding the new organization in dry cargo --

Frans Hoyer^ Yes.

Jan Rindbo^ -- what we have done is, that we reorganized the dry cargo team into smaller, more specialized teams, that each will have their own P&L responsibility. So what we in the future will be reporting is financial figures for the dry cargo owner unit, and then separately for the dry cargo operator unit. And that is to more clearly show the value generation that we get. Because actually, the two teams have quite a -- different approaches to the market. You know, the owner is of course about the long-term positioning in the market, whereas the operator is much more agile and changing positions in relation to the market dynamics and therefore, is quite a different business than the ownership.

Frans Hoyer^ Yes, got you. Presumably, it's going to -- the hope is that it will produce better decisions, and therefore, better results.

Jan Rindbo^ That's absolutely right.

Frans Hoyer^ Yes. But I realize it's a difficult one, but is it possible to give an idea of quantity and timing?

Jan Rindbo^ Well, in terms of timing, we have now set up these teams into these new units. And so organizationally, we are in place. And we will start reporting financial figures for the operator from third quarter onwards.

Frans Hoyer^ Okay. Right, I'll leave you for now. Thanks.

Marcus Bellander, Carnegie ^ One question from me concerning the purchase of two MR vessels. What is it that has made you decide that now is a good time to enter the tanker market, or -- sorry, increase your exposure to the tanker market?

Jan Rindbo^ Well, we think we are in the lower end of the market cycle. So we think it's generally a good time to be starting to look at these opportunities. And we think we've identified two good units that fit into our fleet, and that's why we've decided to move ahead now.

You should not read into this that we think that the market is about to turn so imminently, but we generally think that we are in a good phase of buying ships. And then, I think we also are comforted by the fact that we have a strong operational performance. So even in the current markets, these ships will be profitable.

Marcus Bellander, Carnegie.^ Okay, so even if rates stay at these levels, you'll get decent returns on investments?

Jan Rindbo^ Well, they'll be profitable. I mean, whether we are -- I think it's fair to say that we will not be happy at the current rates forever, but we do think that with the upside there is both on asset values, and hopefully also in the market, especially with the winter season ahead of us, that we think that there is -- there's good upside.

Marcus Bellander, Carnegie.^ Understood, thank you.

Operator^ (Operator Instructions)

There seems to be no further questions at this time, gentlemen. I'll hand back over to you for any closing remarks.

Jan Rindbo^ All right, well, thank you very much, and thank you for your interest in NORDEN. Have a good day, and good-bye.

Operator^ Ladies and gentlemen, that will conclude today's conference call. Thank you very much for your participation today. You may now disconnect.