QNB FINANCIAL SERVICES

Moderator: Shahan Keushgerian
July 23, 2014
12:00 GMT

Operator: Thank you for standing by. And welcome to the Milaha YTG June 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'll need to press star and one on your telephone keypad.

I must advise you that this conference is being recorded today on Wednesday 23 July, 2014.

I would now like to turn the conference over to your speaker today, Shahan Keushgerian. Please go ahead.

Shahan Keushgerian: Thank you. Hi. This is Shahan Keushgerian from QNB FS. I'd like to welcome everybody to Milaha's first half 2014 earnings call. So I'd like to introduce management first. We have with us Gautam Bellur, Senior VP Corporate Development and Communications; Sami Shtayyeh, VP Financial Planning and Analysis; and VP Finance, (Samil Hamet).

So the way we will do this is management will discuss their results. And then we'll open up the floor for a Q&A session. Gautam?

Gautam Bellur: Thanks. Thanks, Shahan. And thanks, everyone, for joining the call today. Sorry if it's a little bit early in New York this morning, if there's anyone joining from New York or from the U.S. East Coast.

Our agenda is similar to previous calls. I'm going to make a few opening remarks on our first half performance. And turn it over to (Sami) to discuss the financials in more detail. And then following which, we will provide a brief outlook on the rest of 2014 for each of our segments. And after that, we'll throw it open to questions, once we're done with the presentation.

Overall, the story is similar to the one we had in Q1. We had a disappointing first half of the year by our standards. Net profit year-on-year was down 10 percent – the first time in a while that we've had a year-on-year decline – while revenues were essentially flat.

If we did go one level deeper from the group financials, our three core business segments – offshore, gas and petrochem, and maritime and logistics – were down 6 percent overall. And Milaha Capital was down 15 percent year-on-year.

If we go one level deeper still, the offshore and maritime and logistics segments declined pretty significantly. Offshore declined 74 percent on the back of a poor first half for its most profitable unit, which is diving services. And maritime and logistics was hit with reduced export volumes due to plant shutdowns in Mesaieed. And we also saw some declines in our logistics and shipyard activities.

The good news is that the gas and petrochem segment, which remained relatively steady flat the last couple of years, grew its profit by 60 percent as the (VLGC) market recovered quite strongly from previous years. And we expanded our presence in the Hubbard Marine servicing space. So that accounted for a good first half for the gas and petrochem segment.

Milaha trading, while it contributes a pretty small percentage of our bottom line, also grew strongly in the first half, as the expectation of increased project activity drove higher sales of trucks and heavy equipment.

Let's be clear. While some of the events affecting our performance in the first half were outside our control, especially things such as volumes, we fully recognize that there were some operational issues that we did not handle as well as we could have. We're taking a pretty hard look at how to recover some of the lost momentum from the first half, particularly in our core businesses. And I'll get into more on that later.

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

Sami Shtayyeh: Thanks, Gautam. I will first go over the published consolidated financial results for our first half, and then get into a bit more detail on the segments.

Operating revenues for the first half of 2014 were 1.244 billion, compared to 1.240 billion in 2013, for a slight increase of 0.3 percent. Operating profit for the first half of 2014 was 339 million, compared to 442 million in 2013, for a decrease of 23 percent. And net profit for the first half of 2014 was 518 million, compared to 574 million for a decrease of 10 percent.

I'll now get into the segment results, highlighting the large (variance) items versus 2013, and explaining them.

Starting off with maritime and logistics, overall revenue was slightly up year-over-year by 2 million, but several moving parts are important to understand within that 2 million. Port services revenue increased substantially due to a 9 percent increase in TE.U. traffic compared to 2013. Similarly, we saw increased import volumes in our container shipping unit. Export volumes, however, took quite a hit due to a client plant shutdown in Mesaieed. This also impacted our Q1 results and was discussed back then. With all indications at the time that operations would be back to normal at mid-May; but that obviously didn't happen. We now expect normalcy in August. That's what we're being told.

Our bulk shipping unit had higher revenue due to them chartering out more vessels than they had chartered in. And you'll see expenses go up because of this.

And, lastly, our logistics and shipyard activities also posted weaker than 2013 revenues.

On the expense side, salaries and wages increased. And that was mainly out of our port services unit related to higher volumes as well as some wage increases.

Operating supplies and expenses were higher due to chartering-in expenses out of our bulk unit. As I mentioned when discussing revenue, they had higher chartering revenue and, similarly, the higher chartering expenses.

We also had higher port charges related to the increased import volumes out of our container shipping unit.

On the non-operating income side of things, we gained approximately 9 million more in 2013 from selling assets throughout the year. And that did not recur this year.

On to offshore. Overall revenue decreased by 56 million. And this was, by far, the result of lower revenues in our diving operations. We really had a series of issues that really tanked the utilization. And the issues included a schedule dry docking for a vessel that took over twice as long to complete than was originally planned. We had equipment breakdowns. But, lastly, and most importantly, continued delays in receiving and employing a new vessel, the name of which is El Shaddad. This vessel has been a sore topic for quite some time. Last we spoke on the call in Q1 we expected to take possession of that in May. We did, in fact, get it. But, unfortunately, the client had some issues with it. So we've been working diligently to rectify those issues along the last leg of finalizing things with the client, and expect it to be employed in August.

The good news is that it's already under contract, so the minute they accept it, the minute we start earning revenue. The client is anxious to get it. And we're more anxious to give it to them. That should really help improve our second half results for offshore overall, really.

On the cost side, we had higher operating expenses, including higher depreciation related to new vessels we took possession of last year, as well as expenses related to the diving vessel I just spoke about.

Moving on to gas and petrochem, overall revenue increased by 39 million. And that was driven by increased rates in our wholly owned vessels, as well as additional revenue from our Port Marine operations where we gradually have been receiving more boats. As of the end of Q2, we had a total of 15 in our possession. Since then, we've actually received one just yesterday. And we're going to get another one tomorrow, which would leave just two more left, which we expect to get in August.

On the expense side, costs increased, mainly related to those new boats. And on the non-operating income and expense side, we saw a 56 million increase from our joint ventures and associates with 27 million of that coming from our 30 percent share of (Naciadad), and 28 million coming from our Gulf LPG joint venture, which shot up due to the steep increase in LPG market rates.

Our trading pillar saw a very large increase in revenue to the tune of 59 million, with associated cost of goods sold in the amount of 52 million. And those increases really came both from higher equipment and bunker sales. In fact, slightly higher equipment than bunker sales.

And last, but not least, our capital pillar saw a decrease of 49 million in revenue. The drop was due to two main factors, primarily. The first being, in Q1 2013, we took a gain of 30 million from the sale of one of our subsidiaries available for sale portfolio. And the second reason – the market dip in June really hit us hard. Overall, the market dropped 16 percent in June. Through May, we were up pretty nicely. But June really, really hurt us. And it's worth noting that things have since rebounded. And we've gained back those losses that we had at the end of June.

Partially offsetting those two factors were 3 million in additional (rent) revenue and approximately 20 million in higher dividends.

And that pretty much sums up our operations and brings us again to an overall net income of 518 million.

And with that, I'll turn it back over to Gautam who will discuss our outlook.

Gautam Bellur: Thanks, Sami. Going to the outlook, in general, our operating outlook for the rest of 2014 is significantly better than the first half, I'm happy to say. Particularly for the segment that did not perform well in the first half – offshore and maritime and logistics.

As I mentioned earlier, we have spent a lot of time in the last couple of months to find short term measures on both the revenue side and the cost side to recover as much as we can the rest of the year, at least, in these two under-performing segments.

Let me go through the outlook segment by segment. Sami has mentioned some of it. I'll take it through a little bit more on this. On the maritime and logistics side, the numbers, as you know are driven by the two large units – container shipping and port services. For container shipping, we expect the export volumes, as Sami mentioned, to return to normal levels in Q3, which will help drive better results in the unit now for the rest of the year. We're also looking – in parallel with that, we're also looking at a number of short and medium term initiatives to drive incremental revenues out of that unit.

For port services, we certainly expect a significant improvement in the second half of the year. We saw some relatively strong growth of 10 percent plus in import volumes in Q2 higher than Q1. And we're optimistic that this growth trajectory can be maintained the rest of the year.

Side-by-side with that, we're also targeting a number of ancillary revenue streams where we can leverage our fixed cost base, and expect some upside from that in the coming months.

Going to offshore, we expect the offshore segment to also improve strongly over H1. But I think it is safe to say that we will not achieve anywhere near last year's numbers.

Fixing the diving services issues that we've had – the diving service unit issues that we've had is obviously a priority. And, as Sami talked about a little earlier, getting the new diving support vessel, Shaddad, to start generating revenues is critical. So it's already contracted to (QP) for five years. However, because of the modifications we've had to undertake, it's still not earning revenues. We expect to complete that in the next few weeks. So, hopefully, we see revenues for at last four months of this year from the vessel, which will make a big difference.

Beyond the Shaddad, we're also expecting to take delivery, barring any unforeseen delays, of four or five additional vessels towards the end of the year. And expect some positive impact on the bottom line for this year from the – from the new vessels. But the bigger impact from these vessels is likely to be in 2015, not so much in 2014.

We're targeting new markets beyond our traditional core of Qatar and Saudi Arabia to improve utilization across the existing and incoming fleet, while, at the same time, keeping options open on potentially rationalizing some of the existing assets that we have, particularly the older ones.

In our gas and petchem segment, which had an excellent first half. We expect to continue to see strong results overall for the rest of the year. We expect the VLGC rates to come down from the record highs that we saw in Q2. But still expect a much stronger market than we've seen in recent years.

Our LNG sector plays are largely of a long term nature, so any fluctuation will mainly be due to (lucky) performance.

We have managed to put both of our fully-owned and operated ammonia gas carriers on time charter. And so we expect a stronger and more stable second half of the year on the gas side. On the flip side, however, the private tanker markets have declined since a relatively strong start at the beginning of the year. Again, the expected increase in supply of medium (range) tankers being (maritime) on the market, we expect the rates to eventually further weaken the rest of the year.

In the harbor marine operations, as Sami mentioned, we expect it to take delivery of the four remaining vessels. (All pilot boats), two of them are pretty much there at this point out of the 19 vessels already that we have placed. And we will officially start the 20-year marine operations contract for QP.

In our trading pillar, we also expect to continue the strong momentum for the Q2 in our trucks and heavy equipment sales, in particular. The order backlog continues to be strong. So we certainly expect to maintain performance going forward.

And last, but not least, in our capital segment, the Qatar equities market has – again, Sami talked about this a little bit – has already bounced back in July from its sharp decline in Q2. But beyond that, we're not going to comment on expected performance the rest of the year, except to say that it'll be more or less in line with the market.

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

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

There are no questions. As a reminder, to ask a question, please press star and one on your telephone keypad.

We now have a question from the line of (Umar Farouki). Please ask your question.

(Umar Farouki): Yes. This is (Umar Farouki) from Global Investment of Kuwait. My first question is on the reason that you said that got delayed and is likely to get delivered in 2014, and at least it will operate for four months. Can you give any idea about (the revenue donated) vessel? And my other question is what are the (current) utilization (rates)? And where do you guys see yourselves going in terms of utilization?

Gautam Bellur: To take the first question on the Shaddad, as I said, we received the vessel. It's undergoing minor modifications. And we will see revenues, probably, the last four months of the year from that vessel – much less than what we were expecting earlier. But in terms of – in terms of the actual rates on the revenues on that particular vessel, we don't have that.

(Umar Farouki): OK. And (the utilization levels) for the (rest of the year)?

Gautam Bellur: The utilization …

(Umar Farouki): Yes.

Gautam Bellur: The utilization levels are generally the – in the range – it depends on the type of vessels we are talking about. We're in construction and maintenance vessels we're talking about in the mid to high 80s on utilization. On the diving side, this is the part that we suffered this year. We're down below 50 percent on that operation, which is what we're trying to improve the rest of the year. And on the rest of the vessels – your PSVs and your anchor handlers, and so on, again, the utilization numbers are actually pretty good. They're up in the 85 to 90 percent range.

(Umar Farouki): OK.

Gautam Bellur: It's really – that's why we focused the presentation, really, on the diving unit because that is the one that is the – pretty much the main cause of the results for offshore this year.

(Umar Farouki): OK. OK. And in terms of CAPEX, can you give guidance for the next two or three years and reducing CAPEX? Do you see the company accelerating the spending?

Gautam Bellur: We don't have guidance on CAPEX going forward. We've given guidance on this year. We don't have a firm number yet on the upcoming years. We will do that going forward, I guess, in the next year's calls. But we don't have guidance on that just yet.

I mean, the CAPEX that we've already talked about that's already what we've talked about is what is already in the plans, which is the vessels and the offshore, both this year and next year.

(Umar Farouki): OK.

Gautam Bellur: There's the CAPEX around the 19 harbor vessels, which should be done this year. And then there is ongoing CAPEX on the real estate side which will spread into 2016 as well, based on current trends. But that's subject to change, obviously. We don't have a full picture yet of the coming three years.

(Umar Farouki): OK. And one more question. You mentioned that the (petroleum) and the gas have performed well. But in the future, you don't – we're likely to see it stabilizing because of the (charters) are likely to come down. Can you give more insight about why they became so high recently?

Gautam Bellur: That's a good question. If we could answer that question, we would be – we wouldn't have to face the volatility that is inherent in some of these. There is a range part of it are really whether rates affect us is in where we're in the spot market. In the spot market is, essentially, our VLGC segment, which if you think about where we started the year, we're talking round about a million a month at the beginning of the year for VLGCs. We went up in April – in the April, May timeframe. And so then it fell down to about 500 in February, March. And then it went up to 3.5 million, which is a record in April, May. Then it came back down to 2 million. So volatility is the name of the game – just to give you an idea.

We're taking a (2.5 million) just given that its record high numbers, we're taking a view that, on average, over the rest of the year, you're not going to get that kind of – that kind of rate. Still, relative to what we've seen in recent years, this is well above anything we've seen in recent years. So we still expect a good year.

(Umar Farouki): OK.

Gautam Bellur: And we're only talking about 50 percent share of four vessels. So that's (one). The only other place we are exposed on the spot market, is on our (Cardiff) tanker side. And those – they started well earlier this year. But there's been a lot of capacity-building in that sector over the past year or so. And much more are coming on line. So it's much more – other than to say that there is going to be some pressure on rates is what we expect over the rest of the year.

(Umar Farouki): OK. OK.

Gautam Bellur: The rest of them are long term charters so we don't really impacted by the spot market trends.

(Umar Farouki): But I was wondering whether the segment will get affected by the sharp increase in oil and gas production in the U.S.? I mean, that will have an effect on exports from the GCC. So, do you think that impacting in the long term?

Gautam Bellur: No. No. I think if you look at how most analysts think about this. Opening that up actually opens new trade lanes that don't exist today. So, if anything, the opening of the U.S. market and exports from the U.S. market actually expands the transportation element quite a bit. And most of that is – we don't know how much of that is going to be on the gas side versus the product side just yet. But the overall market will be – in an overall global sense, it will be a positive for the market, not a negative.

(Umar Farouki): OK. OK. OK. OK. I think that's it for me. Thank you very much for answer the questions.

Gautam Bellur: No worries.

Operator: Once again, to ask a question, please press star and one on your telephone keypad.

We have a question from the line of (Tubin Helsire). Please ask your question.

(Tubin Helsire): Hi. My question is regarding the – there is a net profit margin conversion in America in the (logistics) segment. I just want to confirm. Is it something to do with the (content) shipping business segment? Or it's more than that?

Gautam Bellur: I'm sorry. I didn't get the full question. Could you repeat that question?

(Tubin Helsire): I was asking about the maritime and logistics segment. The net profits margin (off-rate) is coming down. So it's currently at around (9,000), (9,500) from 2013 high of (14,000). So is it because of the container shipping segment which is not doing good? Or is there any other reason?

Sami Shtayyeh: You're talking about the net profit margin decline? Is that correct?

(Tubin Helsire): That's correct.

Sami Shtayyeh: Yes. OK. There's a couple of reasons for the net profit margin decline. One, like I mentioned, last year we sold approximately 9 million of assets – sorry – we took a gain of 9 million on the sale of assets. So that's not really a recurring thing that you an expect year in year out.

(Tubin Helsire): OK.

Sami Shtayyeh: We might have some additional assets underutilized – assets that we might sell later on in the year. But I don't foresee it coming to the level of what we had last year. So that's one reason.

On the operating side of things, the container shipping unit, as you mentioned rightfully, that really hurt the numbers because – let me pain the scenario here. We have these vessels that are coming in from the UAE to Doha. They're coming in with containers. Going out, they were going out with containers with exports. So we're incurring the cost coming and going. However, the exports have now really taken a big hit because of the plant closure. So we're basically maintaining the same cost structure, but we're not getting any of that revenue that we were getting in the past.

(Tubin Helsire): Got it.

Sami Shtayyeh: That's the second big thing. And then the third thing is the fact that, really our – we earned some revenue in chartering out vessels with lower margins. The nature of that business is you make a – you make a margin, you make a mark-up. But the margins are very much lower than what you would expect from any of the other segments within the maritime and logistics segment.

So those are the three main reasons.

(Tubin Helsire): OK.

Gautam Bellur: You are combining asset-heavy businesses with asset-light businesses. So when you have more in the asset-light side, which is the bulk shipping – that (rain and chart) revenues obviously but marginal squeeze on the overall numbers that you'll see.

But the other stuff is not systemic, is, I guess, the point. Right?

(Tubin Helsire): Yes. Got it. But going forward, what will be the normalized net margin we should be looking at from this business at this segment?

Sami Shtayyeh: I think the best way to get that is look at last year, take out the gain on the sale of assets. And it's closer to what it should be, minus a point or a point-and-a-half because of the bulk shipping activities that they're now doing, chartering in and chartering out.

(Tubin Helsire): OK. Got it. Thank you. Just one more question from my side. It's regarding the offshore segment. You're expecting two more vessels to be delivered toward the end of 2014. Do you think that will be deployed immediately, or there could be some changes to be made in those vessels as well?

Sami Shtayyeh: I think you got – we said two more in the gas and petrochem, which is part of the port marine operations. Those are – we have two more coming on line in the month of August. Those are under contract – 20-year contract with QP. Unless you're referring to the offshore vessels. But those are not two. Those are five vessels. Which one are you referring to exactly?

(Tubin Helsire): I'm sorry. I was specifically mentioning about the offshore segment. So I just want to know they will be utilized as soon as you'll be getting it?

Gautam Bellur: Two of those have already been – they're already under contracts. And we are awaiting delivery on those contracts. There's a couple that are not yet contracted that we still have time. And we're obviously beginning in the business development stage, in the tender stages of multiple opportunities.

But two of those are already contracted to (Saudi) when they arrive. So a lot of these vessels, it's important to keep in mind that a lot of the new builds that are coming on line have been built with the Saudi market in mind.

(Tubin Helsire): OK.

Gautam Bellur: There's a lot of activity going on in Saudi Arabia at the moment.

(Tubin Helsire): OK. OK. Perfect. I got it. That's all for my side. Thank you so much.

Gautam Bellur: You're welcome.

Operator: And we now have another question from the line of (Umar Farouki). Please ask your question.

(Umar Farouki): This is (Umar) again. I want to ask regarding the QP (project). I mean, it was expected to come on line in May, but now I think it's expected to come on line in August. And how confident are you that it will come on line in August? And my second question is how much does this contract contribute to the maritime logistics segment?

Gautam Bellur: I'll answer the first question – or not really answer it, but I would suggest that's really a question for the manufacturer. But our view is – the view that we're taking is we expect to be back to normal in August or September, at the latest.

Sami Shtayyeh: (Umar), that's actually not our view. That's what …

Gautam Bellur: That's the view that we received from the manufacturer.

(Umar Farouki): OK.

Gautam Bellur: The volumes are there. It's starting to come back, but it's not back to the full normal levels yet. So we're expecting that according to the producers themselves by September.

Sami Shtayyeh: On the second part of your question regarding the impact, all I will tell you – I can't really get into commercial terms or rates, or anything like that. But what I can tell us is the decrease year-over-year has cost us – we're talking in the low teens millions.

(Umar Farouki): OK.

Sami Shtayyeh: It has a direct hit on container shipping. But there's an indirect hit on some of the other units that also do some services and some work and activities surrounding that decrease. So container took the bulk of it. But there was some bleed onto the others. But you were talking – low teens – over 10 million.

(Umar Farouki): OK. Over 10 million.

Sami Shtayyeh: That's not the contribution that we get form them, but that's the impact because of the shut-down year-on-year. It's in that range.

(Umar Farouki): OK. OK. OK. OK. Thank you.

Operator: We have no further questions.

Gautam Bellur: OK. Well, I guess with that, if there's any questions later on, feel free to reach out to us. Otherwise, thank you all for joining. Look forward to a better second half. And we hope to have better news for you in three month's time.

Operator: That does conclude our conference for today. Thank you for participating. You may all disconnect. Speakers, please remain on the line.

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