

THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

DNORD.CO - Q3 2016 Dampskibsselskabet NORDEN A/S
Earnings Call

EVENT DATE/TIME: NOVEMBER 09, 2016 / 02:30PM GMT



CORPORATE PARTICIPANTS

Jan Rindbo *Dampskibsselskabet NORDEN - CEO*

Martin Badsted *Dampskibsselskabet NORDEN - CFO*

PRESENTATION

Operator

Good day and welcome to the NORDEN Q3 report 2016 conference call. Today's conference is being recorded. At this time, I would like to turn the conference over to Jan Rindbo, CEO. Please go ahead.

Jan Rindbo - *Dampskibsselskabet NORDEN - CEO*

Thank you very much and welcome to the presentation of NORDEN's results for the third quarter of 2016. And thank you for calling in. My name is Jan Rindbo, and I'm the CEO of NORDEN. Myself and our CFO, Martin Badsted, will be presenting our results today.

I trust you have all found time to download the accompanying presentation from our website. We'll go through selected slides, and we'll 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. So the agenda for today will be as follows: I will start by outlining the highlights for the quarter, along with the key financial figures for the period. Afterwards, Martin will give you our view on the liquidity and the market developments. Finally, I will conclude with our guidance for the year, and we will open up for the usual Q&A session.

Slide 3, please. NORDEN reached an adjusted result for the third quarter of minus \$12 million U.S. dollars, which was \$30 million lower than last year's third-quarter result. The result reflects a still-challenging dry cargo market and a continued deterioration of the tanker market. The dry cargo market saw a slight increase in rates, compared to the second quarter. However, rates are still only at the same level as operating expenses. The adjusted result for the period ended at minus \$8 million.

The tanker market continued to weaken in the third quarter as oil demand grew slower than expected, while the tanker fleet supply continued to grow. Rates continued to decline, and NORDEN's product tanker business generated a result of minus \$4 million. In line with the strategy, focus & simplicity, and based on the Company's expertise, brand, and position in the market, NORDEN will strengthen its operating activities significantly.

Focus is on asset light growth within the dry cargo business to utilize NORDEN's strong global network and to make earnings less dependent on market conditions. The guidance for 2016 is maintained at minus \$60 million to minus \$20 million.

Please skip to slide number 5, please. In dry cargo, NORDEN managed to outperform the market benchmarks by 31%, and this can be attributed to our efforts to secure cargo cover while the expansion of our operator activities continue to contribute positively. In tankers, NORDEN has outperformed the benchmark by an average of 7% over the past 12 months.

I will now hand you over to Martin for an update on our financials and the state of the markets. Slide number 6, please.

Martin Badsted - *Dampskibsselskabet NORDEN - CFO*

Thank you, Jan. During the course of the third quarter, we realized a substantial reduction of \$150 million in what we call our net commitments, which is the number which comprises total bank debt, time charter obligations, new building installments, less cash and cover. This is the result of two tanker vessel sales and two long-term cargo contracts that we did on the dry cargo side.



With these activities, we have overall reduced the net commitments by 40% since the end of 2014. Our outstanding new building installments remain well-covered with close to \$600 million in cash, securities, and undrawn bank facilities in total.

Now for a look on the dry cargo market, turn to slide number 7, please. Looking at asset values first, the downturn in the tanker market led to continued declines in second-hand values, which have now declined by 23% year to date. In dry bulk the value increases seen over the summer seems to have leveled off, and overall values are back at the levels seen by the beginning of the year. The Supra's up a little and Panamax is down a little year-to-date. Next slide, please.

Spot rates did see improvements in the third quarter, primarily led by a surprisingly strong demand picture. The level of spot rates is similar to normal seasonality, but just marginally better than what we saw last year. Though Cape rates have quickly fallen back somewhat, both Panamax and Supramax rates have held up somewhat better. Slide 9, please.

As I said, demand was surprisingly strong in the third quarter, mainly led by Chinese imports being up 7% year-on-year overall. The two biggest contributors were iron ore and coal: Iron ore supported by stimulus-led improvements in construction activity in China, and coal imports suddenly reversing years of decline as a result of regulatory constraints on Chinese coal output, which opened up room for more imports.

As you can see in the graph on the lower right, the drag from European coal import reductions have leveled off somewhat, whereas the pressure from coal import declines to India remains a negative. However, we do see low coal stocks and weakening coal output in India, which could add to imports in the near term. Slide 10, please.

The market remains hampered by over-capacity, and we don't think the recent demand uptick marks the starting point for a sustained upturn. Stimulus-based support, to the extent we have seen recently, is most likely unsustainable, so we still need scrapping to continue to fundamentally improve the market balance. The good story is on the supply side that ordering remains at a complete standstill. And with only 1.7% net fleet growth forecasted for 2017, and FFA rates below 6,500 in both Panamax and Supramax, the market is certainly capable of temporarily surprising to the upside. Slide 11, please, for a look at the tanker market.

In the tanker market, the weak development that we saw during the summer continued and spot rates are now at the lowest we have seen for five years. And one-year TC rates are even lower, and we have to go back 15 years to find a similar level of one-year TC rates. Overall, the Atlantic has been weaker than the Pacific, and Handy's have been hit harder than MR's. Slide 12, please.

The market downturn is mainly the result of weaker demand. Total oil demand growth is estimated at below 1% in Q3, and the derived exports of gasoline and diesel declined on a quarter-on-quarter basis. Product export volumes are expected to start growing again in 2017, although still elevated inventory levels might dampen the upside. Slide 13, please.

We think the current downturn in tankers is a normal cyclical downturn which will correct itself. And here supply is key. The peak of product fleet growth now seems firmly behind us, but crude tanker ordering made last year means the total tanker net fleet growth will be around 5%, which is unlikely to be fully absorbed by demand growth. We therefore need to get further in 2017 before we expect the outlook for TC rates to improve.

And now back to Jan for a look at guidance.

Jan Rindbo - Dampskibsselskabet NORDEN - CEO

The guidance for 2016 is maintained at minus \$60 million to minus \$20 million. While the overall guidance is maintained, we have adjusted the expectations for the two individual segments.

Based on slight improvements in the dry cargo market, we have increased expectations for the dry cargo segment to minus \$60 million to minus \$40 million, but lowered the expectations for the tanker result to zero to \$20 million. That means that the overall guidance is maintained at minus \$60 million to minus \$20. Next slide, please.

And this just a reminder that there are uncertainties related to any forward-looking statements. Next slide, please.

This concludes our presentation. We are now ready to open up for our Q&A session. Please await the conference host instructions.

QUESTION AND ANSWER



Operator

(Operator Instructions) Dan Togo, Handelsbanken.

Dan Togo - Handelsbanken - Analyst

Yes, good afternoon. Just a few questions here for my side. On the product tanker side, your guiding (inaudible) in the high end (inaudible) for a zero results here in Q4. Don't you see so say any impact from seasonality that they might take -- take rates to a level that could -- could support even a profit in Q4?

Martin Badsted - Dampskibsselskabet NORDEN - CFO

Hi, Dan. Of course we do think that there's some seasonality in the market, and we have seen some strengthening in spot rates recently, mainly driven by this Colonial Pipeline explosion - or issue at least.

But -- but overall the start to Q4 has still been quite weak during October, with spot rates not much better than what we saw in Q3. So I think within the range that we are guiding, which is quite broad considering how many days, I think we think that it's a reasonable mid-point.

Dan Togo - Handelsbanken - Analyst

All right. And you also allude to that crude is part of the sort of the reason for the depressed product tanker market. But in crude we have actually seen rates spike, suggesting that -- that this market seems closer to some sort of balance. Why don't it have impact in product tanker these spikes we're seeing in crude at the moment?

Martin Badsted - Dampskibsselskabet NORDEN - CFO

Well, our view is basically that in the -- in the very short term, call it a couple of months, the product tanker and crude tanker rates can easily diverge quite a bit, and that is what we've seen in Q3, or at least in October-November. And it's not unusual -- or actually it is quite usual -- that especially VLCCs have a significant but short-lived pick up in October-November.

And, as you're correct, we haven't seen that feed down into product tankers. So combining the two is mainly a sort of, you know, when we look at the one-year outlook for 2017, that we feel that it's right to focus on overall free growth. So the -- the segments in the middle with LR2s and Afra's, where there is some interchangeability, it's not something that will change significantly in the course of a few months. But over a couple of quarters, it's enough in our view to -- to even out most of the discrepancies.

Dan Togo - Handelsbanken - Analyst

And then just a one question, if I may, on the dry side. You are increasing your exposure here by taking in more days. Can you -- can -- what are, so to say, the average commitment you are -- you're making here on -- on the operating part? And -- and do -- do you also -- does this also include so to say extension of extension options, if we are seeing rates increase further into 2017?

Jan Rindbo - Dampskibsselskabet NORDEN - CEO

You're right, we have an ambition to increase our operating activity, but that does not mean that we are increasing our exposure to -- to the market. The operating activity mainly is for short-term charter ships that we match with cargo in the market. And therefore it's a margin business without a huge amount of exposure.

Dan Togo - Handelsbanken - Analyst



OK, so you're not so to say taking a capacity in for six months, one year it's -- on a, you know, a voyage by voyage basis?

Jan Rindbo - Dampskibsselskabet NORDEN - CEO

Yes, but I mean we do also take ships in for six or 12 months, but that is mainly to match the cargo commitments that we have for a similar period.

Operator

Frans Hoyer, Jyske Bank.

Frans Hoyer - Jyske Bank - Analyst

Thank you. Can you remind me of the loss provision in dry bulk? How much did you benefit from reversing that loss provision in the third quarter?

Martin Badsted - Dampskibsselskabet NORDEN - CFO

Yes, hi, Frans. That number for Q3 was \$14.7 million.

Frans Hoyer - Jyske Bank - Analyst

Only 14.7. OK. So it has taken a step down then from earlier, even though there was two different levels of...

Martin Badsted - Dampskibsselskabet NORDEN - CFO

Sorry, sorry, Frans. It's 26.5. It was the wrong column.

Frans Hoyer - Jyske Bank - Analyst

OK. Nonetheless it looks to me like it's a step down. OK, but that's good. Secondly, these short-term charters that you are expanding in dry bulk, and doing much more of that, or planning to, what sort of daily margins do you get on -- on what's available in the market at the moment? I mean the difference between what you pay and what you can get.

Jan Rindbo - Dampskibsselskabet NORDEN - CEO

Yes, I mean it's we're talking about relatively thin margins on this type of business. You can say that in a very low market it is hard to get sort of a very large margin.

But it is -- you know, we're talking about margins between, you know, a couple of hundred dollars, maybe up to \$500, depending on where in the market cycle we are. So relatively thin margins, and also why we say that we need to see a significant growth in this activity before it has a meaningful contribution on the bottom line.

Frans Hoyer - Jyske Bank - Analyst

Are there any other reasons, apart from just making that -- that profit which makes sense, even if it's a tiny one? Are there any sort of other thoughts behind this idea to -- to expand that quite significantly, the way I understand it anyway?

Jan Rindbo - Dampskibsselskabet NORDEN - CEO



No, I think it is taking advantage of our expertise, our brand, our market position, and our global organization that we see this, you know, opportunity that even in a weaker market, that we can generate, you know, a profitable margin in the market. And that's why we're going for that opportunity.

Frans Hoyer - Jyske Bank - Analyst

OK, the final question regarding China and the news out a few days ago that China now -- well, correct me if I'm wrong, but the way I read it was that they plan to increase coal-fired electricity generation by 20% over the next few years. How would that play out for -- for the type of ships that you're involved with?

Jan Rindbo - Dampskibsselskabet NORDEN - CEO

I think that very much depends on the -- you could say on the price arbitrage between domestic pricing and imported pricing. So, you know, China's already a huge consumer of coal. And, you know, we see periods in the market where China's importing much more coal, like we have actually seen in the third quarter. Then other periods where -- where they depend more on -- on local coal. And it's much to do with the price arbitrage between buying locally and then importing. So I think it's hard to say -- it's hard to say specifically whether this will have, you know, a very positive impact. I don't think it has a negative impact, but it -- it's not a foregone conclusion that it will have a major positive impact either.

Frans Hoyer - Jyske Bank - Analyst

OK. All right, thanks.

Operator

(Operator Instructions)

[Marcus Bolander], [Carnegie].

Unidentified Participant

Thank you. Two questions, if I may. The operator or increased focus on -- on operatorship. If that goes well, and you get a lot of volumes in that way, will you continue to sell off vessels? Are you moving towards some more asset-light business model?

Jan Rindbo - Dampskibsselskabet NORDEN - CEO

I think the answer is, yes. We are moving towards more of an asset-light business model. But we are not necessarily expanding the asset-light part of the business at the expense of the ownership of the vessels that we already have. So the operator focus is simply to take advantage of this opportunity that we see in the market to grow with our current position. But it's not necessarily at the cost of owning ships.

Unidentified Participant

All right. And will there be any form of investment, or will you be hiring -- hiring more staff when -- when you're increasing focus on operatorship?

Jan Rindbo - Dampskibsselskabet NORDEN - CEO

Yes, I think fair to say that with a significant expansion of our operating activities, we will also need more hands. We already have, you know, a great team that can do a lot of this. But we also think that looking at margin-based business, you know, there are opportunities, to hire people that has the right expertise or the right cargo focus, then, you know, we would welcome them into the team.



Unidentified Participant

All right. Then last question, just how easy is it to -- to do this? To grow this business significantly? I mean, it sounds like a good idea to make a few bucks extra here and there. But -- but why hasn't it been done before so to speak?

Jan Rindbo - Dampskibsselskabet NORDEN - CEO

No, I think that's fair. That's a fair question. I mean it is a -- we are talking about, you know, relatively small margins and, of course, if you can make much bigger margins by waiting for a much better market, then that's what people do. Now we think that we have a -- quite a strong position here from the outset because of our brand, our position, and this is not something that everyone can do easily. We think that we have an advantage, you know, with our starting position and name in the market.

But also I don't think we should sort of take it for granted or conclude that this is very easy to do and, you know, we just do it because, you know, it's there and easy to do. You know, this requires a lot of focus, a lot of attention, and requires, you know, that our team is fully focused on generating this margin in the operating business.

And it's -- it's a slightly different sort of attitude or skill set you need there, compared to just being, you can say, a traditional ship owner, where you are just trying to get, you can say, the best time charter rates on your ships. You know, this -- this margin business is -- requires, you know, slightly different types of -- of, you know, expertise and skills in the business.

Operator

We have no further questions over the telephone at this time. (Operator Instructions)

We have no further questions over the telephone at this time.

Jan Rindbo - Dampskibsselskabet NORDEN - CEO

All right. I think we should conclude then the presentation. So, first of all, thank you very much for your interest in NORDEN, and thank you for listening in on our presentation. Have a good day and look forward to speak to you at the next opportunity.

Operator

Thank you. That does conclude our conference for today. Thank you for your participation. You may now disconnect.

DISCLAIMER

Thomson Reuters reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Transcripts are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT TRANSCRIPTS IS A TEXTUAL REPRESENTATION OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND WHILE EFFORTS ARE MADE TO PROVIDE AN ACCURATE TRANSCRIPTION, THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES THOMSON REUTERS OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT TRANSCRIPT. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

© 2016 Thomson Reuters. All Rights Reserved.