Epic Gas 1st Quarter Earnings Release

Tuesday, 17th May 2016

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Operator: Ladies and gentlemen, thank you for standing by and welcome to the Epic Gas First Quarter Earnings Release 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 *1 on your telephone. I must advise you that this conference is being recorded today, Tuesday, 17th May 2016.

I would now like to hand the conference over to your first speaker today, Mr Charles Maltby. Thank you, please go ahead.

Charles Maltby: Good morning and good afternoon, and welcome to today's call to discuss our results for the first quarter of 2016. My name is Charles Maltby, Chairman and CEO of Epic Gas, and I'm joined today by our Chief Financial Officer, Uta Urbaniak-Sage.

The first quarter of 2016 is the starting point for our next phase of expansion. As we move on from the half-time interval of the past three quarters and proceed through the scheduled delivery programme over the next 15 months for a further eight new-build vessels of 7,500 cubic metre and larger; upgrading our fleet and increasing our exposure to the larger pressurised sector. Consequently, the fleet calendar days in Q1 2016, up 1% year over year, to 3,330 days illustrate the impact of both the redelivery of a smaller, older 4,000 cubic metre vessel under bareboat charter in December 2015, and the subsequent delivery of a 7,500 and 11,000 cubic metre new build vessel during Q1 2016.

Our adjusted EBITDA of $7.1 million, up 8% year over year, reflects the hard work by the team to manage costs and to drive utilisation in an ongoing weak market, where revenue of $32.2 million is down 4% year over year.

The pressurised LPG sector has seen continued weakness, driven by the ongoing growth in the pressurised fleet with a further net growth in cubic metre capacity of 2.3% after scrapping, coinciding with weaker markets for especially smaller vessels in North Asia.

On the supply side, we have seen about 40% of the vessels scheduled for 2016, delivered in the first three months of the year. We anticipate full-year growth in cubic metre capacity of about 4.5% after scrapping, illustrating the accelerating slowdown of new-build supply as we head through the year. Longer term, the low returns in the market combined with the limited yard and tank manufacturing capacity have led to just two new build orders, each is 7,500 cubic metre, placed during the period for delivery in 2018, and shows that the forward supply length is reducing considerably as we head towards a more balanced market.

In regard to scrapping, we have so far seen one vessel from the international fleet and two others from the Korean domestic fleet scrapped in Q1 with a further three vessels since the end of the quarter. There remains 20 pressure vessels and 27 semi-ref vessels over 25 years of age trading under a similar sub-OPEX rate environment to that of 2015 which suggest it is reasonable to assume further scrapping as the year progresses.

On the demand side, whilst overall global LPG seaborne trade is anticipated to grow by over 5% in 2016, it remains a very difficult market for the smallest pressurised vessels, particularly in North Asia, where the ongoing solid demand for petrochemicals such as butadiene and VCM has been more than offset by a further cut in propylene imports as the growth in LPG imports on VLGC continue apace to provide the propane required for domestic propylene production in China. Within Epic Gas, we continue to step away from the direct consequences of this market, focusing on both expanding demand in other regions and our evolving fleet size towards larger vessels.

Looking at our business by region, Epic Gas currently has 38 vessels on the water with an industry-leading average age of 8.7 years. Of these vessels, we have 24 ships trading west of Suez and 14 ships trading east of Suez.

With the delivery of our 7,500 cubic metre and 11,000 cubic metre new-build vessels, we initially expected this split to see increased focused west of Suez. However, having placed the first vessel in Southeast Asia and with further interest from customers in the region, the present demand suggests a few more could find homes trading LPG and petrochemicals in the East.

During the quarter, the average size of our vessels increased 4% to 5,839 cubic metres and is anticipated to increase further to about 6,400 cubic metres with the balance of our new-build programme, thus leading to greater exposure to the larger pressurised LPG market and over 50% of our earnings generated from vessels of 7,500 cubic metre or larger by this time next year.

As well as the Epic Borinquen of 7,500 and the Epic Sentosa of 11,000 cubic metre, which both delivered in Q1, we also took delivery of the 11,000 cubic Epic Shikoku last Friday. This means we now have three vessels of 11,000 cubic metre on the water.

We continue to develop markets where our expertise, assets, and our network density allow us to outperform the time charter market through a combination of Contracts of Affreightment, (COA) and spot business. During the quarter, contracts accounted for 16% of our spot days compared to the same period in 2015 when we did not have any such business. Whilst the vast majority of our business will remain time charter, we expect to see a continuing growth in our COA performance over the long term.

Negative sentiment from the larger handy size and VLGC sector and a plateau in North American propane production and exports are, so far, not having a material impact on the ongoing supply-push demand growth within the pressurised sector. However, it is important to note that year on year, overall North American propane exports are higher now than in Q1 2015, and that specific to the pressurised sector; butane, not propane, is the primary demand driver accounting for 74% of our volumes in the region in 2015 and with export volumes broadly flat year on year.

It is also interesting to note that since the signing of the JCPOA in mid-January, Iran has returned as a legal exporter of LPG. With the world's second-largest gas reserves and 2015 exports of 4.5 million tonnes leading to a share, despite sanctions of just under 6% of global LPG trade, Iran is an important supply source, especially for the Indian Ocean and Asia. Year-to-date exports have already stepped up with a forecast full-year end increase of about 20% year over year. Significant further investment is also planned within Iran especially within the South Pars reserve, which is expected to lead to a doubling of exports of LPG over the next three-to-five years.

In summary, therefore, the strategic decision by Epic Gas to focus capital on larger, more efficient tonnage, combined with our trading strategy, has enabled us to mitigate some of the impact of the weaker markets and post time-charter equivalent earnings of 8,639 per day, down 2% year over year, but a modest increase of 4% on Q4 2015, and marginally above the weighted earnings available in the market as implied by broker time charter assessments. We have taken advantage of the increased activity later in the quarter to increase our charter coverage, bringing the forward book to 43% covered for the balance of 2016. Our increasing COA exposure, where our primary engagement with customers is on voyage contract basis, is also giving us increasing flexibility to manage our fleet in the spot market.

As a team, we are focused on maximising utilisation on our fleet, while improving the efficiency of our business. Despite our evolving fleet, weak markets, and ongoing exposure to the spot sector, we have achieved a respectable 95.3% operational utilisation during the quarter.

We will continue to fine tune our fleet to deliver a high-quality, long-term, low-cost asset base, especially in the larger segments of the pressurised sector, where we take delivery of five newbuild vessels during the 10 months ahead. These assets are expected to be the workhorses of the future servicing the growing trades in the Atlantic basin whilst also fulfilling niche demand growth in Asia.

I would now like to hand over the call to Uta to step through our financial results.

Uta Urbaniak-Sage: Thank you, Charles. Our TCE earnings per calendar day of $8,639 were lower than the $8,857 we achieved in the first quarter of 2015, but up by almost 4% from the fourth quarter of 2015 as larger vessel sizes partially offset the weak rate environment. In regards to the earnings impact from our two new builds, the Epic Borinquen delivered directly into a long-term time charter whilst the Epic Sentosa sees revenue commence in April, as she has ballasted to Europe and completed loading her first voyage under a COA in April. We look forward to her positive impact in the second quarter.

Vessel operating expenses per calendar day increased marginally from $4,440 in the first quarter of 2015 to $4,449 this year. Our first quarter operating expenses were negatively impacted by $1.1 million of unplanned cost associated with the takeover of technical management on one vessel and unplanned maintenance on two other ships. Without these unplanned costs, our OPEX per calendar day would have been lower by $330 or 7.5%.

Our charter-in costs were $3.5 million and are expected to remain flat until the company redelivers existing charters at expiry. In the first quarter, we had eight ships on bareboat charter, representing 728 calendar days.

We have held our SG&A tightly to $1,001 per day, down by 22% on a cost-per-day basis from the first quarter of last year. With Epic's integrated business model, this expense reflects the full cost of commercial and technical management of the fleet as well as the ownership and corporate-level expenses of the entire platform. Except for two ships managed by third parties, we do not pay any fees for services to any outside or affiliated entities.

The company reported an adjusted EBITDA of $7.1 million, an improvement by 8% year over year. We finished the quarter with a net loss of $1.4 million, an improvement by 42% compared to Q1 2015. As mentioned earlier, Epic Gas took delivery of the first two ships of its new building programme with the remaining six ships to be delivered by the first quarter of 2017. All of our new buildings are being built at high-quality Japanese yards. During the period, we paid $31 million towards the construction of the new buildings, of which $28 million was drawn under a Term Loan Facility. As of 31st March 2016, the company has remaining capital expenditure of $87 million, which will be funded with a combination of debt and equity.

In this respect, our lenders have agreed to amend the credit agreement to lend 60% of the fair market value rather than 65% of the contract price, which will increase the overall loan amount by $13.5 million. We expect to finalise the documentation in the second quarter of this year. After signing, we will have an undrawn loan facility of $86.5 million to finance the remaining five owned newbuildings. That leaves only $0.5 million in payment obligations to be funded with existing cash from our balance sheet, which stood at $43 million at the end of March. Epic Gas is therefore in a comfortable position to fund its remaining capital expenditure.

We have now reached the end of our presentation. Thank you all for joining the call today. We will now take any questions you may have. Operator, please open the line.

Operator: Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. If you wish to ask a question, please press *1 on your telephone and wait for your name to be announced. If you wish to cancel your request, please press the # key. Once again, if you wish to ask a question, please press *1 on your telephone and wait for your name to be announced. Once again, if you wish to ask a question, please press *1 on your telephone and wait for your name to be announced.

There are no questions at this time. I would now like to hand the conference back to today's presenters. Please continue.

Charles Maltby: Thank you very much. Thank you to everyone for making the time to join us and listen today. We appreciate your interest in Epic Gas. If you would like to discuss further, please do contact Uta or I directly. In the meantime, we look forward to catching up further in August for our Q2 update. Thank you.

Operator: Ladies and gentlemen, that does conclude our conference for today. Thank you for participating. You may all disconnect.

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