Q3 2023 Earnings Call ***(Corrected version)***

Event Details

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Company: Methanex Corp.
Ticker: MX-CA

Company Participants

Sarah Herriott - Methanex Corp., Director-Investor Relations
Rich Sumner - Methanex Corp., President, Chief Executive Officer & Director

Other Participants

Ben Isaacson - Analyst
Joel Jackson - Analyst
Steve Hansen - Analyst
Hassan I. Ahmed - Analyst
Matthew Blair - Analyst
Joshua Spector - Analyst
Kevin Estok - Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good morning. My name is Julianne, and I'll be your conference operator today. At this time, I would like to welcome everyone to the Methanex Corporation 2023 Third Quarter Results Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session.

I would now like to turn the conference call over to the Director of Investor Relations at Methanex, Ms. Sarah Herriott. Please go ahead, Ms. Herriott.

Sarah Herriott

Thank you. Good morning, everyone. Welcome to our third quarter 2023 results conference call. Our 2023 third quarter news release, Management's discussion and analysis and financial statements can be accessed from the reports tab of the Investor Relations page on our website at methanex.com.

I would like to remind our listeners that our comments and answers to your questions today may contain forward-looking information. This information, by its nature, is subject to risks and uncertainties that may cause the stated outcome to differ materially from the actual outcome. Certain material factors or assumptions were applied in drawing the conclusions or making the forecast or projections which are included in the forward-looking information. Please refer to our third quarter 2023 MD&A and our 2022 annual report for more information.

I would also like to caution our listeners that any projections provided today regarding Methanex's future financial performance are effective as of today's date. It is our policy not to comment on or update this guidance between quarters. For clarification, any references to revenue, EBITDA, adjusted EBITDA, cash flow, adjusted income or adjusted earnings per share made in today's remarks reflect our 63.1% economic interest in Atlas facility, our 50% economic interest in the Egypt facility, and our 60% interest in Waterfront shipping.

In addition, we report our adjusted EBITDA and adjusted net income to exclude the mark-to-market impact on our share-based compensation and the impact of certain items associated with specific identified events. These events – these items are non-GAAP measures and ratios that do not have any standardized meaning prescribed by GAAP and therefore unlikely to be comparable to similar measures presented by other companies. We report these non-GAAP measures in this way because we believe that they are a better measure of underlying operating performance, and we encourage analysts covering the company to report their estimates in this manner.

I would now like to turn the call over to Methanex's President and CEO, Mr. Rich Sumner, for his comments and a question-and-answer period.

Rich Sumner

Thank you, Sarah, and good morning, everyone. We appreciate you joining us today as we discuss our third quarter 2023 results. For the third quarter, our average realized price of $303 per tonne and produced sales of approximately 1.5 million tonnes generated adjusted EBITDA of $105 million and adjusted net income of $0.02 per share. Adjusted EBITDA was lower compared to the second quarter, due to a lower average realized price and lower produced sales.

Through the third quarter, we saw improving methanol – market conditions with stronger demand from certain sectors, as well as moderation in global operating rates, mainly from various supply outages in North America, Middle East and Southeast Asia. Methanol demand improvements were primarily driven by stronger demand in China, with increased demand for MTBE and other fuel applications, as well as improved demand for methanol to olefins with a number of MTO plants restarting operations in the third quarter.

We are currently seeing very high operating rates across the MTO sector, which we believe is driven by the completion of planned downstream expansions as well as some improvements in affordability from a higher energy and olefins pricing during the quarter. However, we believe that economic pressure remains on this sector under current market conditions.

We continue to carefully monitor the global macroeconomic environment. And during the third quarter, we saw relatively flat demand outside of China for methanol and to traditional chemical applications compared with the second quarter. Coal pricing in China increased during the third quarter from around RMB 800 per tonne to above RMB 1,000 per tonne currently, which we believe was primarily driven by the various industry supply disruptions. We currently estimate the global cost curve to be over $300 per tonne based on current coal pricing in China.

Overall, continued high energy pricing and improved supply demand fundamentals has led to slightly higher pricing throughout the third quarter and into the fourth quarter. Our November posted prices in North America, Asia Pacific and China are posted at $549, $370 and $360 per metric tonne respectively. And our fourth quarter European price was posted at €375 per metric tonne. Based on our October and November posted prices, we estimate our global average realized price to be approximately $310 to $320 per metric tonne for these two months.

In the third quarter, we had lower production due to scheduled turnarounds, in New Zealand and Chile, and seasonal gas restrictions in Chile. We are encouraged by the pace of gas developments in Argentina and the continued supply rates from ENAP in Chile. Increasing gas supply from Argentina allowed us to restart our second Chilean plant in September, earlier than previous years. We expect both plants to run at full rates from the end of September through April 2024, and Southern Hemisphere summer months, and are increasing our Chile production guidance for 2023 from a range of 800,000 tonnes to 900,000 tonnes to a range of 900,000 tonnes to 1 million tonnes based on improved gas availability from Argentina.

Earlier in October, we also announced that we signed a two year natural gas agreement with the National Gas Company of Trinidad and Tobago to restart our fully owned Titan plant and simultaneously idle the Atlas plant in September 2024. I want to thank our team for their hard work to ensure that we maintained operations in Trinidad, which is a strategic part of our global portfolio. The gas situation in Trinidad in the near-term is challenging, which is reflected in the short-term of the new gas contract. We remain committed to working with the NGC and the government to secure long-term economic gas supply. We entered the third quarter in a strong financial position with approximately $500 million of cash and $300 million of undrawn backup liquidity. Our capital priorities are to complete the Geismar 3 project and allocate any excess cash to repay rather than refinance the $300 million bond due at the end of 2024.

Construction of our G3 project is progressing safely to plan. Construction is nearly complete and the team is in the final handover testing and commissioning phases. We expect to achieve commercial production around the end of the year and within our budget range of $1.25 billion to $1.3 billion. The remaining $140 million to $190 million of cash expenditures, including approximately $50 million in accounts payable, is fully funded with cash on hand.

Looking ahead to the fourth quarter of 2023, we're expecting higher adjusted EBITDA with a higher realized methanol price and higher produced sales. We remain focused on delivering strong operational results from our existing assets and completing the G3 project. We are well positioned during this period of economic uncertainty with growing cash flow generation capability from G3 and a portfolio of assets that can generate cash flow across a wide range of methanol prices.

We would now be happy to answer questions.

QUESTION AND ANSWER SECTION

Operator

Thank you. Our next – our first question comes from Ben Isaacson from Scotiabank. Please go ahead. Your line is open.

Analyst: Ben Isaacson

Question – Ben Isaacson: Thank you very much. And good morning, everyone. Rich, question on Trinidad. You said that the gas situation has been challenging, which was the reason for the short-term deal. Does that mean that you don't have confidence that it will get better? Is that why, I mean, if it's challenging, presumably it's challenging in the short-term.

And then as part of that, that same question, what was the rationale to idle a plant that was running and then bring on an interim CapEx (8:59) to restart Titan? Is that because there was going to be a major turnaround for Atlas that you wanted to avoid? Just want to understand the whole Trinidad story.

And then just maybe as my follow-up, can you just talk about any risk to EMethanex due to the shutdown of the Tamar platform off of Israel? Thank you.

Answer – Rich Sumner: Okay. Thanks, Ben. On Trinidad, and I'll talk about the kind of the near-term and the reason we call it challenging is, I think, well previously that you know, that the gas markets tightened in

Trinidad. And then, in the near-term what we see today is there's about, when you look across LNG, ammonia and methanol, that's about 4.5 Bcf of demand per day. Current production is in the range of 2.5 Bcf to 3 Bcf. And the government – no, we haven't given up on the fact that that situation is going to get better, because there's a lot of things happening in Trinidad, and we believe there's a lot of incentives, today, to restart capacity that is there in, across the estate. And these are long assets that have run really reliably over time in that, in Trinidad. So, certainly not. We are working to understand all of the initiatives that are being taken. And we remain really committed to working with NGC as they and the government of Trinidad, as they work with the upstream on improving that situation.

The reason we started up – the decision around Titan versus Atlas is because of the – this is the near-term situation. They were offering a fairly short-term contract. And when you look at the economics under that contract, in the short-term, it made sense around Titan. And as you said, we don't have a turnaround in front of us like we do in Atlas. That plant had gone through a major maintenance just before we'd idled it. I think that was back in 2019. So, it made sense from an economic perspective and also, I would call it, an organization perspective. We want to keep our team in place. Our global manufacturing team is part of our – huge part of our organization. And we're really pleased that we've got that – we'll have the Titan asset running at the end of next year. And we will shift and create a Titan restart team now that will be focused on getting that plant up and running safely and reliably.

You asked about Egypt.

Question – Ben Isaacson: Right, yes.

Answer – Rich Sumner: I'll answer that. I think as of right now, what we've seen is there has been a shutdown of that – so Israel is an exporter of gas to both Jordan and Egypt. Israel has shut in the Tamar field, which has had impacted the flow of gas into Egypt. That is not affecting the available of gas to the industrial producers there. We do understand there may be impact to the – to LNG producers. So as of right now, that's not impacting our operations or other industrial producers in Egypt.

Question – Ben Isaacson: Appreciate it, Rich. Thanks so much.

Answer – Rich Sumner: You're welcome.

Operator

Our next question comes from Joel Jackson from BMO Capital Markets. Please go ahead. Your line is open.

Analyst: Joel Jackson

Question – Joel Jackson: Well, good morning. A couple questions, short-term and then I'll do a long-term. I'll do short-term first. Just looking at some of your guidance for Q4, can you say if you expect Q4 EBITDA to be higher, you said everything will be higher, will be higher than Q4 of 2022? And when you gave your price guidance of $310 to $320, looks like you're using a higher discount rate than Q3, and then would you be having some inventory build in Q4 like you normally do?

Answer – Rich Sumner: Okay. So for Q4, I haven't done that comparison. Wait, our reference was in comparison to Q3, Joel, for higher pricing and higher produced sales. As it relates to the discount rate, we don't expect a big difference in the discount rate, so maybe we can take that one offline.

And then inventory build, yes, we do. We have seen a number of quarters here with inventory build on our produced sales. So we probably, accounting for accounting, but we would expect that at some point we'll also be seeing a benefit of pulling through produced sales as well. So, hopefully that answers. It's a bit of better context to the quarter for you.

Question – Joel Jackson: Okay. And then my...

Answer – Rich Sumner: Is that helpful?

Question – Joel Jackson: ...longer-term question – yes, that one, I asked for 2024 (14:00). But that's a particularly longer-term now.

Answer – Rich Sumner: Yes. Yes.

Question – Joel Jackson: If you look at the production profile for 2024, can we talk about like off a base of little more than 6.5, can we talk about what you expect for 2024? So I would imagine you expect G3 can ramp across Q1. You have almost near production there next year. I would imagine you switch over from Atlas to Titan, but there might be a hiccup there, like would you lose some tonnes? Would you be running both plants overlapping for a month or would you lose some tonnes on a ramp down and a ramp up? Any other changes? New Zealand or anywhere else? With better gas in Chile? Like should we expect, 2 million tonnes more in production next year? 1.5 million tonnes, like can you just give us some idea?

Answer – Rich Sumner: Yes. And we will update our guidance formally towards the end of this year. But I will also – maybe I'll give you a kind of some preliminary thoughts there.

We are, we will for Chile, like I said, we will be operating two plants at full rates until, at least until April of next year. So already, we've got those gas contracts in place today and we'll be working on the similar contracts for next year. We – this is the first time in a very long time that we've operated two plants at full rate. So, we're really excited about that. And we'll be working on replicating that out in the, for the summer month periods for next year. So, I would expect, when we were at 800,000 to 900,000 (15:31) this year, that, that number will be higher for Chile.

For Trinidad, we will – we are going to be working as – the gas contracts are working simultaneously. So, we will be trying to – I don't expect a lot of overlap there, but we will try. It will be kind of an idling and then a start-up of Titan. So, you can kind of do the numbers on how that change happens. And then, I think the big one will be also G3. We'll – intention here is obviously to start up around the end of the year, but it will take time before our G3 actually works through our inventory flows. So, you probably got a 45- to 70-day inventory build before G3 starts, kind of coming through the earnings.

Egypt, we would expect similar results too. We've been operating at high rates. And New Zealand, we'll update our guidance today. It's at 1.3 million tonnes to 1.4 million tonnes, and we'll – we'll be, that's probably a similar level we would be at. But we'll update it more formally and we also have to factor in scheduled turnarounds as well, so more to come there.

Question – Joel Jackson: Thank you.

Operator

Our next question comes from Steve Hansen from Raymond James. Please go ahead. Your line is open.

Analyst: Steve Hansen

Question – Steve Hansen: Yes. Thanks, guys. Rich, can you go back to the Chilean gas situation just a little bit more detail? It sounds like on the back of the recent success, there's an opportunity to secure some more gas going forward. Just trying to understand what that means for the production profile next year, I guess, through the summer months in particular down there, and how we should think about maybe even the medium, longer term profile for the production of the company?

Answer – Rich Sumner: Yes. Thanks, Steve. So a bit of background on what's happening in Chile. And a lot of this is what's happening in Argentina. Argentina is developing that Vaca Muerta Field in the Neuquen Basin and this is quite a prolific field. What they're trying to do is they're investing in the pipeline infrastructure. So, gas development is – a lot of success around gas development.

And what they have done is they are working on connecting that field into the major grid in Argentina. Argentina consumes about 120 million cubic meters a day in gas. What they did is they commissioned a pipeline that is now delivering, in the third quarter, that's now delivering 10 million cubic meters into the grid. They're working on adding compression to that pipeline, which would add another 10 million cubic meters per day into the grid as well. So, and that will happen sometime in the first half of 2024.

And then, what they are also working on is another pipeline connection which would double that capacity that would come on in the 2025 timeframe. In addition to that, there's a development that's happening in the Austral Basin by Total and Wintershall in a consortium there called the El Fenix Project (19:01). And that's really located really close to our plants.

So, all of these developments are significantly improving the domestic gas balances in Argentina, and as well that supports export markets, which we are very well positioned there with our assets. So, we're really pleased to say that we're going to be operating two plants, at full rates, during this sort of eight-month period. And as like I said, the first time in a very long time we've been doing that and we're going to work on longer-term gas. We think that focusing on the non-winter months is the right thing now. And over time, we also be hoping to improve our gas position during the winter months. But these are things we'll continue to update on as we progress through.

Question – Steve Hansen: Very good. Thank you. And just one follow-up on the G3, in terms of the commissioning and the inventory build that you described. I know it's early. But can you give us a sense for whether the 45 to 60 or 70, when do you describe will all take place in Q1 from your standpoint today or will that start to build through the later part of Q4?

Answer – Rich Sumner: Yes, I think right now the way to do is starting in Q1. That would be probably the right way to think of it, around – starting in around the beginning of the first quarter.

Question – Steve Hansen: Okay. Very helpful. Thank you.

Operator

Our next question comes from Hassan Ahmed from Alembic Global. Please go ahead. Your line is open.

Analyst: Hassan I. Ahmed

Question – Hassan I. Ahmed: Good morning, Rich.

Answer – Rich Sumner: Good morning.

Question – Hassan I. Ahmed: You guys saw a nice uptake across all your regions, obviously, Europe pricing wise, Europe's obviously for the quarter is of no reflection there as yet. I'm just trying to understand the delta between sort of North American pricing and China/Asian pricing. I mean, even if I were to discount North American pricing, there is still call it, as much as a $70 a tonne, $80 a tonne delta between those pricing levels in the regions. So just trying to get a better sense of why that exists. I mean, it seems to me above and beyond shipping.

Answer – Rich Sumner: Yes, Hassan. Thanks for the question. I think hopefully I'll answer your question the right way here for you to make sense of it, is, I think if you were to look at discount levels, across the regions, rather than our global discount, you will be – you can't really apply the average discount to all the prices. It's really that each region does have its own kind of market discount levels, which do vary quite widely depending on which region you're looking at. So our ARPs, if you were to look at our ARPs by region that would probably make more sense and probably more reflective of kind of reasonable pricing differentials between those. So, it's hard to look at the global discount and apply that and try to make sense of those prices relative to, say, spots or other markers.

Question – Hassan I. Ahmed: Understood. Understood. And just coming back to sort of broader question, I know it's all sort of recent occurrences and the like in the Middle East. But I mean, are you guys seeing any meaningful shifts, as a result of that in-trade flows? I mean, I guess, more specifically, what are you guys hearing in terms of Iranian product?

Answer – Rich Sumner: Yes. So, as of right now, we're not hearing any disruptions as of today. First, we're monitoring this situation very closely, and really hoping for a peaceful and sustainable resolution here for everyone. But we haven't seen any disruption.

Israel doesn't have any meaningful really methanol demand, nor is there any supply. And in the area there, there's no methanol trade routes that are impacted. Now, if this were to escalate, in the region, a lot of things could be impacted, including methanol, so. But we haven't seen any of those disruptions yet.

But that could impact crude. It could impact LNG trade flows, methanol trade flows. And so, those could have really meaningful impacts, on the industry. But we haven't seen any of that yet. But we're really closely monitoring to see, obviously what – what's going to – how this is going to unfold.

Question – Hassan I. Ahmed: Very helpful, Rich, thanks so much.

Operator

Our next question comes from Matthew Blair from Tudor, Pickering, Holt. Please go ahead. Your line is open.

Analyst: Matthew Blair

Question – Matthew Blair: Hey, good afternoon or good morning. Sorry. Could you talk about any opportunities you're looking at for your underutilized assets? Is there a chance that you could take a per Atlas, move it to the U.S. like you do with some of your Chile plants long time ago? Or is there an opportunity for converting those assets into an e-methanol plant?

Answer – Rich Sumner: Yes. So, so, we in terms of relocation in Trinidad at this point, we remain committed to Trinidad. And we are you know, we think there's a lot of incentives today, to get assets, underutilized assets, operating in place where they are today. And that assets operated really well for us in Trinidad. So we are focused there.

Now, we have – we do have experience relocating plants. We moved Chile 2 and 3 to Geismar. Our experience on plant relocation is that the capital cost savings are really not that meaningful. It's really about speed. The construction timeframe can probably be, you know, we could probably save a year on in terms of the construction timeframes versus building new. So, it has advantages there. We're not considering that today for Atlas as we want to work on getting longer-term sustainable gas in Trinidad. But that is something that we've done before. We have a lot of experience with. And there is that speed advantage in the event that you wanted to move quickly on a project.

Question – Matthew Blair: Sounds good. And then, could you talk a little bit about the moving parts on cash flows in 2024? Should we think of your CapEx moving down to the – I don't know, $150 million to $200 million or $200 million range. I think you mentioned the debt pay down of about $300 million next year. There's also the dividend, the $50 million plus, potentially a working capital build as you ramp up G3 with the remainder, any remaining cash flow go to buybacks in that scenario?

Answer – Rich Sumner: Yes. So I think the right number to use is on the CapEx is at the lower of your range, they're around $150 million. And I think you've got all the numbers in terms of the other cash outlays. So yes, we're focused on the $300 million bond. And I think as of today, at today's pricing, we're probably that's the main focus.

We generate a little over $200 million in free cash flow with G3 at $300 methanol price. Above that, then you're probably getting above the bond if you get closer to $350, we still see the market environment today is supportive of what we need to repay the bond, but we're really focused on that. If we were to have a really stronger methanol market, then you start looking at free cash flow beyond the debt repayment. We don't have any major capital ahead of us, and so we would be looking at returning excess cash and likely some balanced approach between looking at the balance sheet further on de-levering. But we're really focused on the $300 million bond today.

Question – Matthew Blair: Great. Thank you.

Operator

Our next question comes from Josh Spector from UBS. Please go ahead. Your line is open.

Analyst: Joshua Spector

Question – Joshua Spector: Yes, hi. Thanks for taking my question. I guess, first, I guess, wanted to have some follow-up on the cash flow side. So when you think about the working capital build next year with the G3 start-up, I mean, you're already purchasing and reselling some tonnes. So is there a way to size kind of the net impact that you expect that to be in terms of cash used to build that inventory?

Answer – Rich Sumner: Yes. We're not really concerned with the working capital build up here. I don't think that there's any strategies we're having in terms of managing that down, where you will see we are buying a lot of product today, which we will significantly reduce with G3 coming online to this, we're not going to be growing our sales by 1.8 million tonnes next year. We've already grown our sales. So, you just see a lot of purchase product being displaced by produced product, which would be supportive of lower inventory values anyways.

Question – Joshua Spector: Yes, I appreciate that. I guess that's where I was kind of going. This is a two kind (29:15) of net offset each other. So it's not really a major cash use. Is that kind of what you're saying or should we...

Answer – Rich Sumner: Yes. Yes.

Question – Joshua Spector: ... be thinking about it as a somewhat of a cash use?

Answer – Rich Sumner: Yes. Yes.

Question – Joshua Spector: Okay. And then, the other question I have is just more on cost curve. It is methanol price support. If I heard your comment correctly, you talked about $300 a tonne methanol price support. Your posted pricing in China is higher. I guess, what do you view as the pricing driver here? Is it the fuel value? Is it coal? And then, how does it evolve into next year in your view?

Answer – Rich Sumner: Yes. Our posted price is higher, but after discount we're probably in, we're kind of closer to that, those levels. What's driving the price today is really it's going to be the marginal producer cost, which is a coal producer cost in China. And then, the other factor that we look very closely at is the affordability of methanol into – primarily into the olefins industry. And I think, right now, we would say that both of those factors are kind of pointing to the levels, where we are today, in China, at around $200 spot pricings in around $280 to $300.

We have seen some improvement in the olefins market. And I would say that that sector relative to oil pricing today is pricing well under where it would be on a kind of mid-cycle basis. So we've seen tonnes of pressure on, on that sector that we would in a normal, in a kind of mid-cycle energy pricing at $90 oil, we would expect much, much higher pricing. And especially, when MTO is operating at the highest rates, I think we've ever seen today, as an example that, that sector is operating at 90% operating rates over a very high base, because we've added MTO plants, last year. So, if we had a better market there, I would expect that would be driving methanol prices higher than where we are today.

Question – Joshua Spector: Okay. Thank you very much.

Operator

Our next question comes from Laurence Alexander from Jefferies. Please go ahead. Your line is open.

Analyst: Kevin Estok

Question – Kevin Estok: Hi. Good morning. This is actually Kevin Estok on for Laurence Alexander. So, listening in, most of my questions have been asked. But I guess I was wondering if you could give maybe any updates from since the last calls around your strategy on Green and Blue methanol? And I guess maybe how current interest rates might impact future investments. I guess I just want to get a sense of your rate sensitivity too, as it relates to your strategy. Thank you.

Answer – Rich Sumner: Yes, thanks. Maybe when you think about the low carbon space, the strategy is really looking at both sides, both the demand and the supply side. I didn't mention it in the opening comments, but there continues to be a lot of momentum in marine fuels.

Right now, over 200 ships plan to be in the water in the 2027-2028 timeframe. Represents around 7 million tonnes of demand, if those ships were to run on a methanol 100% of the time. So, we are working with major international shipping companies. This is a container shipping segments leading the way, but there's interest in dry bulk tankers, and so at cruise ships. So we're working with that. Actually, we've got a number of MoUs signed, working closely with the shipping industry, on their desire for Green Blue conventional methanol, say Green looks like for Green methanol, it's mainly being driven by the European market for in-shipping, and that a lot is on the back of what's happening on the emissions trading scheme as well as E.U. maritime regulations around carbon emissions. We're having a lot of other discussions around Blue and conventional methanol as well, so.

And then on the supply side, we're working on a number of projects. I would say first and foremost, we've been certified to be able to purchase our renewable natural gas in North America and produce Green methanol at our Geismar plants, and our marketing regions are certified to be able to sell that product through to customers – certified product through to customers. And then, we're looking at the feasibility of projects, at our sites, and that would be using renewable hydrogen and CO2 to sort of green the assets. And we're looking at multiple feasibility within our existing sites.

We're also in discussions with other projects that are out there that would like to work with us on offtakes. And so we're trying to understand how we can open up as many economically-efficient supply alternatives for the marine industry around Green methanol. And look, there's a lot of discussions happening, and we'll hope to be able to report more as we progress in this area.

Question – Kevin Estok: Great. Thank you very much.

Operator

There are no further questions at this time. I will now turn the call back over to Mr. Rich Sumner.

All right. Well, thank you for your questions and interest in our company. We hope you will join us in February, when we update you on our fourth quarter results.

Operator

This concludes today's conference call. You may now disconnect.