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Q4 2018 BW LPG Ltd Earnings Call

EVENT DATE/TIME: FEBRUARY 28, 2019 / 1:00PM GMT

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PRESENTATION

Operator

Welcome to BW LPG's Fourth Quarter 2018 Financial Results Presentation. We will begin shortly. You will be walked through the presentation by BW LPG's CEO, Martin Ackerman; and CFO, Elaine Ong. They will be pleased to address any questions after the presentation. (Operator Instructions)

Certain statements in this conference call may constitute forward-looking statements based upon management's current expectations and include known and unknown risks, uncertainties and other factors, many of which BW LPG is unable to predict or control, that may cause BW LPG's actual results, performance or plans to differ materially from any future results, performance or plans expressed or implied by such forward-looking statements. In addition, nothing in this conference call constitutes an offer to purchase or sell or solicitation of an offer to purchase or sell any securities.

With that, I am now pleased to turn the call over to BW LPG's CEO, Martin Ackerman. Thank you, sir. Please go ahead.

Martin Ackermann ***BW LPG Limited - CEO***

Thank you, Anna. Welcome to the presentation of BW LPG's results for the fourth quarter of 2018, the financial period ending 31st of December. I'm joined by our CFO, Elaine Ong, as always. And we appreciate your interest, and we will take questions at the end of the call.

The Baltic VLGC index relevant for VLGC's earnings went up 33% in the fourth quarter of 2018 compared to the previous quarter, an average at $43.3 per ton or $25,300 per day. The Baltic Index reached the year high at $48.3 per ton in October, but started to soften in November. The primary reasons for an overall rebound into the freight market for the fourth quarter are as follows. Improved price spreads between the U.S. Gulf and Far East supported the widening of geographical arbitrage in the fourth quarter of 2018. North America seaborne exports grew by 12% in the fourth quarter year-over-year. Exports to China decreased in fourth quarter, but more volumes were absorbed by Japan and Southeast Asia due to the U.S.-China trade spat. This supported overall ton miles. Middle East seaborne export volumes increased 2% year-on-year as Iranian volumes were offset by increased exports from Saudi Arabia, Qatar and the UAE. However, VLGC freight rates weakened again from November onwards, driven by a cold winter in the U.S. causing higher-than-normal fourth quarter domestic LPG consumption, a sharp reduction in oil price and OPEC production cuts.

Looking further into 2019, we expect continued high U.S. LPG production and consumption reverting to normal levels to support widening of the geographical LPG price spreads. This should support a recovery in freight rates. For the full year of 2019, we remain cautiously optimistic due to sustained U.S. LPG production growth and incremental export volumes being added from other key loading areas such as Australia and Canada. However, increased demand from VLGCs from growing U.S. exports will in part be offset by high level of new-build deliveries. We maintain our neutral view on Middle Eastern VLGC exports, as incremental regional growth is expected to compensate the effects from the reimposed sanctions on Iran.

Turning to Slide 4, we review the highlights of the fourth quarter. We generated net revenue of $85 million based on daily rates of $21,300 for the VLGC segment, with the VLGC contract coverage of 15% and total contract coverage of 15% for the quarter. Our EBITDA came in at $36 million for the quarter. We recognized the provision for vessel impairment of $34 million, mainly driven by ship brokers reducing the vessel value estimates towards the end of the year. Earnings per share before nonrecurring items was below $0.01. Including the nonrecurring charges, we recorded a loss of $0.24 per share for the fourth quarter.

On 8th of October 2018, we withdrew our proposal to merge with Dorian LPG.

I'll now turn to Slide 5 for an overview of our commercial performance. In 2018, TCE rates on our VLGC fleet averaged $18,400 per day including offhire, and $18,700 per day, excluding offhire. Our VLGC spot earnings came in at $19,400 per day, excluding waiting time, compared to the Baltic spot index rate of $17,300 per day for the year.

Turning to Slide 6. In the fourth quarter, TCE rates in our VLGC fleet averaged $21,300 per day, including offhire, and $22,000 per day, excluding offhire. Our VLGC spot earnings came in at $23,400 per day, excluding waiting time compared to the Baltic spot index rate of $25,300 per day for the quarter.

The fleet availability was 97%, with a commercial utilisation at 91%, reflecting a 9% waiting time for the available fleet. We strive to make it as clear as possible for you by reporting our earnings per day on both calendar days and available days. Available days are simply calendar days less offhire days where the vessels are technically not available. If we were to report our earnings on operating days, which exclude offhire and waiting time, under the definition of one of our peers, our earnings would increase to $24,000 per operating day. This is, however, an incomplete measure of performance and peer comparison are more -- as more waiting days translate into higher earnings per day. The sharp drop in the oil price and to a certain extent the extraordinary cold winter in the U.S. led to fewer cargoes being lifted out of the U.S. compared to the historical normalized end-of-the-year trading pattern.

We had correctly anticipated a weak first quarter of 2019, and our chartering strategy was to secure optimal coverage throughout this seasonally low period while locking in coverage in the historically busy period towards the end of the fourth quarter. Unfortunately, we had not anticipated the sharp reduction in oil price and the exceptionally cold winter, which led to fewer U.S. cargoes, thus forcing us to take idle time with market rates continue to fall. However, we would like to emphasize that BW LPG consistently has outperformed the market since our IPO, and we're pleased to see that we also outperformed our listed peers for the full year of 2018.

Turning to Slide 7. On Slide 7, we see that the global fleet of VLGC stands at 265 vessels as of 31st December 2018, after growing by 10 vessels during the course of the year. The current order book to fleet ratio stands at 14%, 18 delivering in 2019 and 19 delivering in 2020.

Our VLGC market share is 16%. Including LGC's newbuildings, our total owned and operated fleet comprises 50 vessels.

On Slide 8 we provide an overview of seaborne LPG trade in the fourth quarter of 2018. Global seaborne LPG trade grew by 4% year-on-year in the fourth quarter mainly due to strong export from North America and the Middle East, supported by increased demand from Southeast Asia, South Korea and Japan. Chinese imports were down 8% in the fourth quarter of the year -- in fourth quarter year-over-year, following the 25% increase in tariffs on U.S. LPG imports into China, effective end of August 2018. However, total China 2018 imports increased by 6% from 2017, as the first 9 months of 2018 showed growth compared to last year.

On the export side, North American seaborne LPG grew year-on-year by 12% to $8.9 million tons driven by stronger regional trade and increase in volumes to Europe. Exports to the Far East increased as lower exports to China was countered by higher exports to Japan and South Korea. Middle Eastern seaborne LPG exports also grew by 2% to 9 million tons despite a decrease in Iranian volumes due to sanctions, as exports from Saudi Arabia, Qatar and United Arab Emirates increased.

Turning now to Slide 9. Here we provide an updated snapshot of the EIA's outlook for LPG balances in the U.S. In 2018, U.S. LPG net exports reached 31 million tons, up from 27 million tons in 2017. This implies a production growth of 11% and net export growth of 15.1% for 2018.

For 2019 the EIA has revised its forecast for U.S. LPG net exports to 38 million tons, up from 36 million tons. This represents a net export growth rate of 23% year-over-year. For 2020, U.S. LPG production is expected to grow further by 4.4%, while domestic consumption is expected to increase by 2.7%, resulting in U.S. net exports growth at 9.2%, with net exports reaching 42 million tons in 2020.

With that, let me turn you over to CFO, Elaine Ong, who will walk you through the financial positions and our results.

Elaine Ong ***BW LPG Limited - CFO***

Thanks, Martin. Starting with our income statement on Slide 10. Our net revenue for the quarter was $85 million compared with $79 million in the same quarter last year. This is mostly due to the recovery in LPG spot earnings. EBITDA came in at $36 million for the quarter. We recognized the provision for vessel impairment of $34 million, mainly driven by ship brokers reducing their vessel value estimates in the quarter. Loss per share before nonrecurring items was less than $0.01 per share. Including the nonrecurring charges, we recorded a loss of $0.24 per share for the quarter.

Turning to Slide 11, we provide a snapshot of our balance sheet and cash flow position. We continue to maintain our leverage ratio of 56%, and we ended the quarter with cash and cash equivalents of $50 million.

On Slide 12 you'll see our net debt position at $1.2 billion at the end of the quarter. Total liquidity, consisting of available cash and undrawn facilities, was $215 million. We currently have 5 debt facilities: $800 million facility with $337 million outstanding and $165 million of undrawn credit; a $400 million ECA facility with $324 million outstanding; a [$221 million] (corrected by company after the call) ECA financing with $181 million outstanding; a third ECA facility at $290 million with $257 million outstanding; and finally, a $150 million term loan with $136 million outstanding.

We are in advanced discussions with our banks regarding the refinancing of our $800 million facility maturing in November 2020. We will announce the details of the refinancing once the documentation is finalized.

In December 2018, all existing loan facility agreements were amended to reduce the minimum adjusted equity ratio from 35% to 25%, and the minimum BW Group ownership was reduced from 35% to 20%. The covenant related to BW Group's ownership in BW LPG was amended in conjunction with our proposed merger with Dorian LPG, which, if successful, would have resulted in a dilution of BW Group's ownership. Despite the decrease in minimum ownership by BW Group, the larger shareholder in BW LPG has increased their shareholdings in BW LPG from 45% at the beginning of first quarter 2018 to 48% at the end of January 2019.

Effective from 1st Jan 2019, the new lease accounting standard IFRS 16 came into effect. The new accounting standard will result in a lower adjusted equity ratio as lease obligations, currently reported as off-balance sheet items, are added back to the balance sheet. To offset this effect, the adjusted equity ratio covenant for all of our debt facilities was reduced from 35% to 25%. As of 1st Jan 2019, our adjusted equity ratio was 41% with the adoption of IFRS 16. We have provided a slide in the appendix to outline the main effects expected from IFRS 16 on our financial statements and debt covenants.

On the 25th of February this year, we announced the establishment of a new Product Services Division and have the support of 2 lenders for our trade financing. For financial reporting purposes, we will report this as a new segment in our financial statements. We do not expect the net profits from product services to have a material impact on our overall results since shipping remains our core business.

With that, I'd like to hand it back to Martin to conclude our presentation.

Martin Ackermann ***BW LPG Limited - CEO***

Thank you, Elaine. So if you please turn to Slide 13, I will summarize our presentation. Earnings per share before nonrecurring items was below $0.01, including the nonrecurring charges we recorded a loss of $0.24 per share for the fourth quarter. We would also like to highlight the subsequent events. On 21st of January 2019, BW Helios was delivered for recycling in accordance with Hong Kong convention, generating USD 7 million in liquidity and a net book gain of USD 2 million. Secondly, on 25th of February 2019, BW LPG established the Product Services Division to support the core shipping business. The Product Services Division will provide existing and new customers with reliable and integrated LPG delivery services. This initiative is expected to translate into improved fleet utilization and better returns for our shareholders.

We've been working on the Product Services Division for more than a year. And as you can expect, we have been very thorough in the process of evaluation, feasibility studies, risk and credit management system set up, et cetera. A dedicated team is now in place, including product trading, operations, risk management and credit management, and the team will further enjoy the support of the existing BW LPG infrastructure and client relationships.

For the sake of clarity, I wish to emphasize that Product Services will not take positions involving LPG product price exposure, but will hedge all transactions.

First and foremost, our focus is to deliver the best possible shipping solution to new and existing clients, whereas Product Service is an extra in toolbox to increase our shipping performance. In addition, we believe that the even closer focus on the product markets will improve our overall service offerings as well as provide us with deeper intelligence on the freight markets.

Our current contract coverage for 2019 stands at 13%. Looking further into 2019, we expect continued high U.S. LPG production and consumption reverting to normal levels to support widening of the geographical LPG price spreads. This should support a recovery in freight rates. We remain cautiously optimistic for the full year of 2019 due to sustained U.S. LPG production growth and incremental export growth from all U.S. loading areas as well as Australia and Canada.

We maintain our neutral view on the Middle East VLGC exports as incremental regional growth is expected to compensate for the effects of the reimposed sanctions on Iran and effects from the announced OPEC cuts.

Furthermore, increased VLGC ton mile demand will partly be offset by a high level of newbuild deliveries, and we maintain our view that no further newbuild orders remain key to rebalancing the VLGC market.

With that, I'd like to open up the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question is from Lukas from ABG.

Lukas Daul ***ABG Sundal Collier Holding ASA, Research Division - Analyst***

Regarding your scrapping decision of the LGC, I was wondering, when you look around across the space, do we see more owners taking that kind of a decision during the course of 2019? And if yes, so would you be able to sort of quantify the potential impact of that?

Martin Ackermann ***BW LPG Limited - CEO***

Hi Lucas, thanks for calling in and showing interest, which is appreciated. According to our files, we have 12 VLGCs above the age of 25. And of these 12, we estimate 5 to 6 strong recycling candidates for scrapping in 2019. And I think I've said it before, our philosophy around this is, of course, that when you have a ship older than 25 years or you're looking at your, say, even fifth special service, coming at year 25, facing a significant CapEx investment both on the docking itself but also on ballast water treatment systems and receiving relatively high steel values from the subcontinent right now, we think that might be the way that more owners are thinking. And of course, on top of that -- yes, 5, 6 strongly recycling candidates.

Lukas Daul ***ABG Sundal Collier Holding ASA, Research Division - Analyst***

Okay, that's good. And then could you just sort of just shed maybe a little bit more color how you expect the -- your newly setup division sort of to operate in day-to-day context?

Martin Ackermann ***BW LPG Limited - CEO***

Well, of course, we're enormously excited with the new initiative. And as I emphasized, it's low risk, it's fully integrated, and the overall objective here is to service our shipping clients and improve the utilisation of our overall business. But the -- as they said, (inaudible) in place, there is a -- the desk is there. We have hired the people, we have implemented the systems. For the last couple of months the team has been working on, say, dummy fixtures. So everything is ready. Elaine and her team has worked on getting the credit finance in place. So that -- there's, of course -- the team will be working by being in direct contact with the market. And then, of course, when there is a ship -- shipping position within our fleet where we have no takers, no clients that can see use for the ship, then that is an ideal candidate for the use for our Product Services team.

Lukas Daul ***ABG Sundal Collier Holding ASA, Research Division - Analyst***

Okay. And do you sort of intend to -- predominately, is it on the U.S. Far East trade? Or could it sort of apply globally?

Martin Ackermann ***BW LPG Limited - CEO***

It could certainly apply globally. And I think we'd like to keep the cards a little bit closer to the chest right now on exactly where our focus will be. But we do have a global view on this. Our ships are globally, so will the team be.

Operator

Your next question is from Peder, who's from Fearnley Securities.

Peder Nicolai Jarlsby ***Fearnley Securities AS, Research Division - Equity Analyst***

Just quickly, I just have one more question on the spot performance. And as you say, you have historically been performing well above, at least, in line within -- and right now, at least, in our numbers you're well below, I was wondering if you could elaborate a bit more on exactly what went wrong in this quarter and also to what extent you have been able to kind of fix the or cover the available ships early in the first quarter?

Martin Ackermann ***BW LPG Limited - CEO***

Sorry, I didn't hear the end of that sentence. If we have also what, sorry?

Peder Nicolai Jarlsby ***Fearnley Securities AS, Research Division - Equity Analyst***

If you can talk a bit about to what extent you have been able to cover, call it, the idle ships early in the first quarter?

Martin Ackermann ***BW LPG Limited - CEO***

Yes, I think -- I try to deliberately be as precise as possible during the script, so -- but of course, I'd be happy to elaborate on it further. I think the two main items that -- so as I said on the call, our strategy was to position our ships well into December where we normally see a bit of hectic period ahead of the holiday seasons. So that was also what our market intelligence showed us to do this year. Then the oil price dropped quite a bit. And then sort of to be very specific, it actually had a very small hike. It came up a little bit shortly thereafter and after which is dropped significantly again. And I think at that point this is where the market -- buyers retract from the market, the -- and that basically led to considerable reduced number of exports from the U.S.

The other main factor is the very cold U.S. winter. We saw last year, when we look at the meteorological data, we saw last year's winter as a strong outlier in terms of the LPG domestic consumption in the U.S. due to the winter heating demand. And unfortunately, this year's winter turned out to be just as bad, so to say, from an LPG export point of view. So those were the two main factors that took us a little bit by surprise. And of course, when you then start fixing in a falling market, you just don't get the best fixtures out there. And of course the idea was to get those fixtures within the month of December so we could go along on most of these voyages well into Q1 where we expected the market to be weak. So we're working on that right now, as we speak. The market in the first quarter is certainly weak and quite top for everyone concerned. But as I said on the call, we're quite optimistic when we look at into the year, and we think soon as the cold spur in the U.S. disappear, we'll see exports coming out with quite some strength in just both new -- and there's new volumes being added to the market as well.

Peder Nicolai Jarlsby ***Fearnley Securities AS, Research Division - Equity Analyst***

Okay. And just another question, I probably asked this before, but speaking to most owners, most people don't seem to be concerned that the majority of the order book now is trader controlled. But we see time and time again that the traders are having a massive impact on the market. Then I was wondering, has this view from you guys changed or is it still the same that the ship is a ship?

Martin Ackermann ***BW LPG Limited - CEO***

Well, I mean, it's absolutely true that about 80% of newbuild orders are trader controlled, and we have definitely seen a lot of relet in the market, which has certainly pushed down the Baltic. Of course, if we were to consider those 2 types of traditional owners, on one side trader relet, on the other, of course, most traders consider their shipping cost as sunk. And of course, if they need to do corrections, it's more about salvaging the P&L on an immediate basis without necessarily thinking overall too much about the wider Baltic market. Whereas, of course, the traditional shipowners, including ourselves, are in the other camp trying to support the freight level, so we get to a regional basis. And I think that's kind of the -- that's the environment we're in right now.

Operator

(Operator Instructions) As there are no questions in queue, we will now take questions from the webcast.

Iver Baatvik ***BW LPG Limited - Head of IR***

Hello, we have one question on the webcast here. It's from Axel Styrman from Nordea. And he asks, which vessels were affected by the impairment, the VLGCs or LGCs or both? And if VLGCs, old or new or both? LGCs or LVPs.

Elaine Ong ***BW LPG Limited - CFO***

Both the LGCs and LGCs are affected by the impairment.

Martin Ackermann ***BW LPG Limited - CEO***

Yes, I think that answers that question.

Iver Baatvik ***BW LPG Limited - Head of IR***

And he also asked, new or old?

Elaine Ong ***BW LPG Limited - CFO***

It's a mix.

Iver Baatvik ***BW LPG Limited - Head of IR***

Okay.

Martin Ackermann ***BW LPG Limited - CEO***

Did you want to add a comment on our overall impairment policy?

Elaine Ong ***BW LPG Limited - CFO***

Well, I think it's important for us to note here that our accounting policy is the higher of discounted cash flows and the broker valuations. However, historically, at BW LPG, we have been more conservative than most by looking at our valuation at each quarter-end using the average of 2 broker valuations. And so this impairment that we have taken on our books at the end of this quarter reflects the average of 2 broker values that we've been using consistently since we -- even before we IPO-ed as a company. So this is the $34 million that we've taken at the end of Q4.

Iver Baatvik ***BW LPG Limited - Head of IR***

Okay. Then there's no further questions on the webcast.

Operator

Thank you. Ladies and gentlemen, we have come to the end of today's presentation. Thank you for attending BW LPG's Fourth Quarter 2018 Financial Results Presentation. More information on BW LPG is available online at www.bwlpg.com. Goodbye.