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Methanex Corp. (MEOH)

Q3 2017 Earnings Call

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John Floren
President, Chief Executive Officer & Director, Methanex Corp.

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MANAGEMENT DISCUSSION SECTION

Operator: All participants, please stand by. Your conference is ready to begin. Ladies and gentlemen, thank you for standing by. Welcome to the Methanex Corporation Q3 2017 Earnings Call.

I would now like to turn the conference call over to Ms. Sandra Daycock, Director of Investor Relations. Please go ahead, Ms. Daycock.

Sandra Daycock
Director-Investor Relations, Methanex Corp.

Thank you. Good morning, ladies and gentlemen. Welcome to our third quarter 2017 results conference call. Our 2017 third quarter news release, management's discussion and analysis, financial statements can be accessed from the Reports Tab of the Investor Relations page at our website at www.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 forward-looking information. Please refer to our third quarter 2017 MD&A and to our 2016 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, cash flow, or income made in today's remarks reflect our 63.1% economic interest in the Atlas facility and our 50% economic interest in the Egypt facility.

In addition, we report our adjusted EBITDA and adjusted net income to exclude the mark-to-market impact on share-based compensation and the impact of certain items associated with specific identified events. We report these non-GAAP measures in this way to make them a better measure of underlying operating performance, and we encourage analysts covering the company to report their estimates in this manner.

As I mentioned at our September 15 Investor Day in Toronto, I have moved to a new role within the company. Effective next week, Dean Richardson, Vice President of Treasury and Investor Relations will assume responsibility for the Methanex Investor Relations function. Kim Campbell has also joined the team as Manager, Investor Relations and will work with me going forward.

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

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

Good morning. Q3, 2017, was a solid quarter and demonstrates the company's ability to generate cash at lower methanol prices. Pricing improved throughout the quarter, and we delivered record sales volume. Our production also improved significantly versus Q2, not withstanding us completing our Egypt turnaround and planned maintenance at our Geismar facility. We recorded adjusted EBITDA of $143 million during the third quarter of 2017. This was $31 million lower than the EBITDA of $174 million that we achieved in the second quarter of 2017, primarily due to the impact of lower average realized methanol pricing.

Adjusted net income was $52 million or $0.60 per share in the third quarter, compared to $74 million or $0.85 per share in the second quarter. Our average realized price decreased from $327 per tonne in Q2 to $307 per tonne in Q3. We achieved record sales volume of 2.8 million tonnes in the quarter, reflecting a 12% increase compared to sales volumes in Q2.

As we move into the fourth quarter, we are encouraged to see an improvement in methanol prices. In Asia, our October posted price increased by $50 per tonne to $400 per tonne, and in North America, our October posted price increased by $10 per tonne to $396 per tonne. In Europe, our Q3 price increased by €10 per tonne to €330 per tonne. We believe that the improvement in methanol pricing is supported by strong supply and demand fundamentals.

Methanol demand in Q3, 2017, was approximately 6% higher year-over-year compared to Q3, 2016. Demand from the methanol-to-olefins, our MTO sector was strong as most of the MTO facilities that underwent planned maintenance or experienced technical issues during the second quarter of 2017 resumed production early in the third quarter and have been running at high operating rates. We expect three other MTO plants currently under construction to be completed in 2018, with combined capacity consumed over 3 million tonnes of methanol annually at full operating rates. Demand from traditional chemical applications was also solid in the quarter.

On the supply side, a number of planned and unplanned outages in the Middle East and Southeast Asia contributed to tighter market conditions in the quarter. Thermal coal prices in China continued to rise in the third quarter, increasing the middle portion of the cost curve. Natural gas prices in China remained unchanged and natural gas-based methanol production continues to set the high-end of the cost curve. We estimate the current cost curve to be in the range of $280 to $320 per metric tonne. Spot methanol prices in China today are above this range.

Our plants continue to run well during the quarter and they produced 1.8 million equity tonnes, an increase over our Q2 production of 1.6 million equity tonnes. In North America, our Geismar plants continue to perform very well. Our Medicine Hat plant also operated at a high rate during the quarter. In Egypt, I am pleased to report that we completed a successful turnaround of the plant in August, which was the first since the plant started up in 2011. Our share of Egypt production was 71,000 tonnes in the third quarter, compared to 159,000 tonnes in the second quarter.

Excluding the turnaround period, the plant has been receiving 100% of its contracted gas supply and operating at capacity since mid-November, 2016. We are advised by the Egyptian government that the overall outlook for the gas supply and demand balance in the country is improving. We continue to be optimistic that we will receive strong allocations of gas at this facility for the foreseeable future, and as a result, are increasing our guidance to 85% annual operating rates in Egypt going foreword.

We would expect close to full supply for the majority of the year with some modest risk of curtailments that could reduce operating rates during the Egyptian summer months, when electricity demand is at its peak. The Chili plant produced 78,000 tonnes during the third quarter, compared to 60,000 tonnes in the second quarter. The plant operated solely on natural gas from Chile during Q3. The production level in the third quarter reflects lower gas delivery during the southern hemisphere of winter months.

We remain optimistic that our underutilized 1.7 million-ton Chile facilities represent a very low capital cost growth opportunity for Methanex, due to the progress in developing natural gas reserves in the area. We continue to progress discussions to contract additional gas supply in the region to enable the restart of Chile IV, which is targeted for Q3, 2018. However, major capital spending on a project is subject to our ability to contract additional natural gas beyond our current commitments that extend through mid-2018.

In Trinidad, our share of production was 457,000 tonnes in the third quarter, compared to 449,000 tonnes produced in the second quarter. We expect to receive approximately 85% of our contracted gas supply for the foreseeable future. We returned $109 million to shareholders through dividends and share repurchases during the quarter. Since commencement of our normal course issuer bid in March of 2017, we have repurchased nearly 6 million common shares for roughly 6.2 – roughly 6.2 million common shares approved for a cost of approximately $277 million. We plan to complete the normal course issuer bid by the end of October 2017. This illustrates – this continues to illustrate the Company's commitment to return excess cash to shareholders.

We ended the quarter with $307 million in cash on the balance sheet. Methanex's share of the cash, including our proportionate share of Egypt and Atlas cash, was $272 million. We generated cash from operating activities before changes in non-cash working capital of $151 million during the quarter, compared to $178 million during the second quarter of 2017. Our cash balance declined in the third quarter, primarily as a result of share buybacks. Our near-term cash requirements, excluding any changes in working capital, are expected to be limited. Expected maintenance capital for the remainder of 2017 is $20 million, and the next bond maturity is at the end of 2019.

Other than our planned $55 million investment in Chile, we do not anticipate any significant growth capital expenditures in the near term. We believe we are in an excellent liquidity position, and recently extended the term of our $300 million revolving credit line by three years to December 2022. Our priority for excess cash will be to return it to shareholders through share buybacks. Our outlook for the fourth quarter is positive. Based on our posted methanol contract prices thus far in the quarter, we expect average methanol prices in the fourth quarter of 2017 to be higher than the third quarter, and we anticipate that production and sales of produced product in Q4, 2017 will be higher. As a result, we expect EBITDA to be higher in Q4, 2017 compared to Q3, 2017.

I would now be happy to respond to any questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] The first question is from Daniel Jester of Citi. Please go ahead.

Daniel Jester
Analyst, Citigroup Global Markets, Inc.

Q

Hey. Good morning, everyone. So could you give us an update on getting the natural gas contract for the Chile expansion? And I think you said that right now it's on track for third quarter 2018 to get finished. If there is any delays in getting a settlement, at what point does that maybe tip into 2019?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Yes. So we're negotiating with ENAP, which is the primary gas supply down there. I think the good news is the volume of gas is there. We haven't come to an agreement yet on the economics. So until we come to an agreement that extends for both parties on the economics, we won't spend the significant capital that we're planning for the restart of Chile IV. I'd say if we don't contract by the end of the year, probably the schedule will slip from the Q3, 2018 that we've guided to. There's other gas that we have contracted in the region from people like GeoPark, beyond mid-next year, and the mid-Next year contract is with ENAP. So we have some gas contracted beyond mid-next year, but not enough to really spend the entire $55 million that we guided to, to restart Chile IV.

Daniel Jester
Analyst, Citigroup Global Markets, Inc.

Q

Okay, that's helpful. Thank you. And then just a couple of quick ones on the quarter. I noticed that purchased volumes were up pretty substantially compared to the trend over the past year or so. Anything notable there? And I know that you – your plant in Louisiana wasn't maybe directly impacted by the hurricane, but in the quarter, did you have any hurricane-related incremental cost? Thanks.

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Yes. So on the purchase product, I think I've guided to 80% of our sales would be our equity tonnes, and that's still good guidance. I think you'll notice, Dan, we had record sales in the quarter, and as a result, our produced product was about the same as Q3 -- Q2, a little higher. So we had to supplement our sales with purchase products. And that was as a result of the planned maintenance in Egypt and Geismar. So I think in the fourth quarter, I would expect to be more in the 80% kind of area. But it will fluctuate a little bit up and down each quarter, as the inventory works its way through the different FIFO layers.

As far as the hurricane, our plants were not impacted at all. We had some logistics issues in the Houston area, which may have added a few dollars to our cost structure, but nothing significant. We managed to keep all of the customers that continue to run. Some of them couldn't run because of the flooding, but we kept all of the ones that were running fully supplied from our other facilities like Geismar and Medicine Hat. So anybody that wanted methanol from us got it. And I think that's a tribute to our logistics chain and our team in Dallas.

Daniel Jester
Analyst, Citigroup Global Markets, Inc.

Q

Okay. Thank you very much. And best of luck Sandra.

Operator: Thank you. The following question is from Jacob Bout of CIBC. Please go ahead.

Jacob Bout
Analyst, CIBC World Markets, Inc.

Q

Hi, John.

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Hi, Jacob.

Jacob Bout
Analyst, CIBC World Markets, Inc.

Q

I had a question on the discount rate to start off. Discount rate was relatively low given average contract pricing was down in the quarter. Is there something structurally that's changed there or how should we be thinking about that?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

No, I think we've guided to 15% on average. And I'm still very comfortable with that guidance. So in your models, I would be using 15% discount rate. Some quarters when prices are increasing, we'll do a little better. In some quarters when pricing is decreasing, we'll do a little worse. But I'm still very comfortable with the 15% on average.

Jacob Bout
Analyst, CIBC World Markets, Inc.

Q

Okay. Maybe turning to the share buyback. So it sounds like it's going to be complete at the end of this month. Can you talk a bit about in a flat methanol price environment, what that you're thinking? Is it 5% or 10%, kind of what should we be thinking about?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Well, assuming pricing today continues for the foreseeable future, we're going to generate significant free cash flow. And 10% is easily doable in that kind of environment. We'll complete the NCIB end of the month. We won't have the ability to start another one until March of next year. So we'll – over the next coming months, accumulate cash on the balance sheet. And depending on the price of methanol and how much cash we accumulate, we could consider a substantial issuer bid, but right now, we'll complete the NCIB and look forward to generating free cash.

What I would say is, before we did a substantial issuer bid, we would want to have the cash on the balance sheet, and we wouldn't be borrowing money to do that. So we'll see how the methanol price and market evolves. But I think, our view is, it's going to be pretty good pricing environment until the next new production comes on stream. And we're not expecting any new production till late first quarter next year at the earliest. So we'll see how things evolve.

Jacob Bout
Analyst, CIBC World Markets, Inc.

Q

Helpful. Thank you.

Operator: Thank you. The following question is from Joel Jackson of BMO Capital Markets. Please go ahead.

Joel Jackson
Analyst, BMO Capital Markets (Canada)

Q

Hi. Good morning, John.

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Hi, Joel.

Joel Jackson
Analyst, BMO Capital Markets (Canada)

Q

Going back to Dan's question in the purchase product, can you give us a little color? Did you make money on – were those profitable sales for you this quarter? And I think you built about 200,000 tonnes of methanol inventory. I mean was there opportunity here? Did you make money? I guess that's what I'm trying to get it.

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Our inventories quarter-over-quarter was the same. So we didn't build any inventory during the quarter. As far as making money, we make our money on our equity tonnes that we produce. That's where we make significant EBITDA, between $50 to $150 a tonne depending on the methanol prices and where we are in the cycle. I've guided before that on purchase product, on average, we breakeven over the cycle. Some quarters when prices are rising, we'll make a few million dollars. Some quarters when prices are declining we'll lose a few million dollars. So I'd focus on the 80% of our equity sales and the EBITDA generating, depending on the methanol price. That's where we make our money.

Joel Jackson
Analyst, BMO Capital Markets (Canada)

Q

Okay. I'm not sure if you can comment yet – so my second question, I am not sure you can comment; Southern Chemical just posted flat posting for November verses October. Is that sort of in sync with what you think November contract pricing will do in North America; about flat?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Well, we'll announce both Asia and North American contract pricing by the end of the month.

Joel Jackson
Analyst, BMO Capital Markets (Canada)
Q

Nothing to suggest wide swings either way?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.
A

We'll announce by the end of the month.

Joel Jackson
Analyst, BMO Capital Markets (Canada)
Q

Okay. It's fine. Thanks.

Operator: Thank you. The following question is from Hassan Ahmed of Alembic Global. Please go ahead.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC
Q

Good morning, John.

John Floren
President, Chief Executive Officer & Director, Methanex Corp.
A

Good morning, Hassan.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC
Q

John, came across this interesting article. I believe it was an ISIS article, which talked about a marked shift in sort of the Iranian methanol strategy. I mean this article, I think it came out maybe like a week ago or so, was talking about how Iran is no longer considering giving out licenses to – for standalone methanol facilities, number one. Number two, even the existing facilities, it seems, or at least this article seems to suggest, they were thinking of converting into MTO facilities. So would love to hear your thoughts about what you're hearing, whether this is actually going to happen, what it may do to trade shows and the like?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.
A

Yes, I think that article you're referring to, that was quoting some government officials in Iran. So I read the same stuff that you did. Basically, reiterating what you said, they said, going forward, they're not going to approve any more methanol projects, unless they have a derivative associated with the plant, similar to what we've seen in China. And I think what they've said is that the economics of producing methanol from their gas just to sell methanol is not as attractive as the derivatives, and they want to have more downstream, including MTO in the country. And the article did go on to say that even existing methanol production or methanol production that's under construction, they would be encouraging those owners to diversify and have derivatives for their current production.

So I think that's extremely positive for us and the methanol market, because one of the overhangs that many analysts have been talking about is, including ISIS, 10 million tonnes, 15 million tonnes of production from Iran over the three or four years, which we've never agreed with. But I think the Iranians themselves are now guiding the rest of the world what their plans are for their gas, and what they're going to do with their gas, including methanol and methanol derivatives. So I think overall, if this is carried out as policy, it's extremely positive for us.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC

Q

Very interesting. Now as a follow-up, on the Chinese side of things, can you just give us a sense of – you talked about obviously MTO operating rates kind of normalized. Where do you – did you see, through the course of Q3, these operating rates being on the methanol side of things? And did you see any sort of curtailment be there pollution related or the like?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Well, there's ongoing curtailments both on methanol production and derivative production in areas in Eastern China because of – they call them inspections. It's related to the environmental issues that we've been talking about for quite some time. As far as the MTO, it operated at 88% in Q3, which really is full operating rates, because one of the plants, the Fund Energy plant was – had been shut down since the end of March.

So if you exclude them, we ran at 100-plus rates in the quarter. And I was just in China a few weeks ago. I met with many of our MTO customers, and they're quite bullish about the outlook for MTO and their own operating rates. There's a plant today that's gone down for maintenance, that is planning, as part of that maintenance, to de-bottleneck their current MTO facility, which will add another 400,000 tonnes of methanol demand. And people I spoke with that are in this business are planning to do similar things next year. So although there may not be that second wave, there's another three plants under construction of 3 million tonnes of demand at full rates. We're going to see these continued de-bottlenecking opportunities. And we would expect this sector to continue to provide a very healthy demand for methanol going foreword.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC

Q

Perfect, very helpful John. Thanks so much.

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Thanks Hassan.

Operator: Thank you. The following question is from Jonas Oxgaard of Bernstein. Please go ahead.

Jonas I. Oxgaard
Analyst, Sanford C. Bernstein & Co. LLC

Q

Good morning John.

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Good morning.

Jonas I. Oxgaard
Analyst, Sanford C. Bernstein & Co. LLC

Q

Very quick follow-up on the Iranian question. And I have a different question if you don't mind. Looking at the timeline of MTO conversion, I'm assuming we're looking at maybe 5 to 10 years out. It's not really a near term thing, correct?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Well, I would disagree with you on that. I think once you start to build one of these MTO plants, it's a couple of years. So it depends on how quickly they move. And they haven't been clear in what I've read how quickly they're going to move with existing capacity or capacity that's under construction. As far as any new sanctions, I think they've been very clear, there'll have to be an associated derivative. So these things can be built. We've seen in China examples in a couple of years. So that – your estimation seems to be a little long, assuming they go forward and start to convert some of these existing units. I think it's too early to make that assumption at this time.

Jonas I. Oxgaard
Analyst, Sanford C. Bernstein & Co. LLC

Q

Okay, that makes sense. Now something completely different. When the OCI plant comes online in the U.S., it looks like that's going to back out a lot of Trinidadian volume, which has to go elsewhere, most likely Asia. How are you thinking about your Trinidadian volumes or your Trinidadian trade flows?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Yes, we have – we run an integrated supply chain. So we – on a weekly, monthly, quarterly basis, look at optimizing our supply chain based on where we think we're going to produce, based on planned turnarounds, based on our sales volume. So right now, there's quite a significant amount of methanol flowing from the Atlantic Basin to the Pacific basin already. You're right, as NAT gasoline comes up sometime next year-end and runs well, you would expect more production to have to flow to the Pacific basin from the Atlantic Basin.

And our own situation is probably not going to change that much, because you know our sales for next year is going to be in that similar guidance to what we've given by region this year. It will go up 50% in Asia and the balance in Europe, North America, South America. So our own situation won't change, but there's tremendous opportunities here for swaps and we're ongoing talking with lots of people about swaps. So I think as NAT gas comes on, there will be a lot more opportunities to do swaps, where product will stay in North America and other product will flow elsewhere and optimize the supply chains for everybody else.

Look at our Geismar site. We have now the ability to sell 600,000 tonnes on the pipeline on that site. And it's not all of our own sales, but there's lots of opportunities to prevent or to avoid product coming into that area from places like Trinidad or Venezuela, and just supply, on a swap basis, those molecules elsewhere. So I think you're going to continue to see all suppliers look to optimize their cost structures and their supply chains as new production comes on, not only in United States, but in Iran as well.

Jonas I. Oxgaard
Analyst, Sanford C. Bernstein & Co. LLC

Q

Okay. Thank you.

Operator: Thank you. The following question is from Nelson Ng from RBC Capital Markets. Please go ahead.

Nelson Ng
Analyst, RBC Dominion Securities, Inc.

Q

Great. Thanks. John, I think you mentioned in the past that you expected to see some Argentinian gas later this year. Have you seen any so far, like in Q4? And is it still your expectation that you'll see some gas under that Tolling Agreement this year?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Yes, we signed the Tolling Agreement like you mentioned. We would have expected to get some of that volume by now and we haven't. So we're still optimistic we'll get some this year. And that's what we're being told. But we're now almost into November. So if we do get any, it'll be – not significantly move the needle for this year. But in general, Argentina is looking more and more positive as a gas supplier over the medium term. If you look at what they've developed, not in the shale gas, but in the same gas areas that we used to get our supply from, there's a lot of activity and a lot of developments.

There is this agreement between Chile and Argentina that's been publicly discussed about sharing energy; not just gas, but all forms of energy more openly going forward. And there was just an election Argentina, where the current government did extremely well. So they are directionally wanting to have a more cooperative relationship with countries like Chile and their neighbors. So I think that's all positive for us. I don't think it's going to move the needle in the next quarter or two. But certainly, if you look out through the end of the decade, as we're looking to get back to a two-plant operation in Chile, I think the solution for that is not only the current negotiations we're having with ENAP, but Argentina. A lot of work to do to get there. So I'm optimistic, but we really have a lot of work to do. And having that tax removed from gas exports was another step in the right direction. So not next quarter, but I wouldn't be surprised if we got some tolling volume for Q4. But it's not going to be a significant amount. But going forward, I think more and more solution for the two-plant operation, in both Chile and Argentina.

Nelson Ng
Analyst, RBC Dominion Securities, Inc.

Q

I see. And then just a quick question on Egypt regarding the debt and the cash. So the cash is equal to about half of the debt outstanding on the project. I was just wondering, given that Egypt is operating at a high rate, do expect that the covenants will be met in the next quarter or two? And would the cash then be freed up? Or – like if not, what are your thoughts in terms of just like refinancing or just paying down the debt at the project level with the cash?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Well, you've highlighted a number of options that we're looking at. So good for you. You know, Ian and his team are working really hard to find a solution to allow us to access the cash. Not only us, but our partners, who are the Egyptians, would like to have the cash as well for funding many things that they're doing in the country. So we're working hard on that.

We don't have anything to announce today. But you're right to point out the debt and the cash. At current methanol pricing we're going to build quite a bit of cash in Egypt. And we think there is win-win solution here with the debt holders and we're pursuing that aggressively but nothing to report today. As far as once the debt is paid or refinanced to some extent, what we'll do, it's probably premature. What I'd like to see is the plant run and run well as it has been. After the turn around, we're really running at excellent rates and good efficiencies, as well as the gas is – availability has been 100%.

So this is all good news, and if I get another quarter like that under my belt, then I think we'll have a lot more confidence to consider all kinds of things for Egypt, including debt retirement or issuing new debt. But I think it's a little premature. We just came out of the turnaround in August. And here we are, about six to eight weeks later. So stay tuned.

Nelson Ng
Analyst, RBC Dominion Securities, Inc.

Q

But just on that, like if the plant runs well for few quarters, would that meet the covenants? Or are they more complicated than that?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

We haven't been specific about what covenants there are, but I think if the plant runs well for two quarters, and we're in the current methanol price, I don't think it's going to be an issue as far as covenants or otherwise. So we're working hard to get it resolved this quarter. But until we have it resolved, we have nothing to report in that manner and the cash will continue to be trapped until we can get a resolution, which like I said, we're working hard to do.

Nelson Ng
Analyst, RBC Dominion Securities, Inc.

Q

Okay. Thanks, John.

Operator: Thank you. The following question is from Laurence Alexander of Jefferies. Please go ahead.

Q

This is [ph] Jeff (30:07) on for Laurence. There have been some reports in China, angling to potentially adopt E10 as a strategy, which could be highly capital intensive. I believe M15 infrastructure is already in play there. Has there any been any change lately in the discussions of using methanol in fuel blending of late?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

No, just more continued moving forward with the trials. I think what we've seen change, and this has not been in the last quarter, it's been in the last year, is a focus on the high-level blend. The M100s, the M85s, [indiscernible] (30:40) making the 100% methanol engines, et cetera. So they seem to be focused more on the high-level blends because of the clean burning aspects of methanol and air quality. If you looked at the most recent Congress, it's continuing to get a lot of attention, not just air quality, but environment in general.

So I think you're going to see them continue to focus on high-level blends, not low-level blends. Why E10? I'm not privy to the information. I understand they have an excess amount of corn right now. I don't know if that's driving it. But when I've talked to the Chinese officials over the years, they were pretty clear on saying, they're not going to use their food to make fuel. So it was a bit of a surprise to us, when we read what you read. But we haven't, in our discussions, heard anything more than what was written in that announcement, I think, a few weeks ago. So I think on the methanol side, the focus will be on high-level blends. Not saying low level blends aren't going to continue, but I think the growth will be in high level blends.

Q

Thank you.

Operator: Thank you. The following question is from Cherilyn Radbourne of TD Securities. Please go ahead.

Cherilyn Radbourne
Analyst, TD Securities, Inc.

Q

Thanks very much, and good morning.

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Good morning.

Cherilyn Radbourne
Analyst, TD Securities, Inc.

Q

Wanted to ask, just on the three MTO plants there currently under construction, I have seen it suggested that one or perhaps two of those might come on by the end of 2017, effectively in advance of the next methanol supply increments. Is that a scenario that you foresee or consistent with your outlook? Would you see those plants as more 2018 events?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Yes, we're almost getting to the end of 2017 here. So I guess it's how you expect things to develop. The [indiscernible] (32:32) is in the process of starting up. How successful and how long, anybody knows. But I think as far as significant methanol demand, it's an early 2018 story if they're successful. The other two plants, we're continuing to monitor. And we say 2018, probably midway is as good as any expectations. And I guess it depends on what your view for NAT gas and the uranium production. The industry experts, like [indiscernible] (33:04) were saying Q3 of this year and here we are in Q4 and no sign of completion of either of those projects. So I think there's a lot of work to do to get those plants running still. So until they run and produce and produce on spec and reliable, I think the demand will continue to grow. And we'll continue to see very favorable supply/demand balances for methanol.

Cherilyn Radbourne
Analyst, TD Securities, Inc.

Q

Okay, that's helpful. And just, a more minor question, on New Zealand production in the quarter, clearly, it rebounded versus Q2. But it was a bit lower than is normal for that complex. Is that just a function the composition of the gas that you received in the quarter?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

No, I wouldn't. We're still guiding to 2.2 million tonnes or 550,000 per quarter. So you're right. We were a little lower in the third quarter. And our expectation is it will bounce back to the more 550 in Q4. So, nothing really significant, a few minor issues, but nothing significant. And 550 per quarter is still the proper guidance. We are working. And now that Shell and Todd have separated their assets, the high CO2 gas that we used to get. I think is more – going to be more available to us. We haven't secured it yet, but if we're successful in securing that high CO2 gas that we used to get, we can get back to 2.4 million tonnes. But right now, I'm comfortable with the guidance of 550 per quarter assuming no technical issues.

Cherilyn Radbourne
Analyst, TD Securities, Inc.

Q

Great. Thank you. That's all my questions.

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Thank you.

Operator: Thank you. The following question is from John Roberts of UBS. Please go ahead.

John Roberts
Analyst, UBS Securities LLC

Q

Thank you. I think before you said that $200 million in cash is kind of your minimum level. Should we expect that you'll always be materially above the minimum, that really truly is a minimum only if kind of you got it in a bad condition or something came up unexpected. And I ask that because again, you could have finished out your buyback program I think during the quarter if you wanted to, but you didn't and maybe it's the rate at which you buy back stock. Was the third quarter, kind of a good example of what a maximum rate might be?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

I think it's a bit of mute point. I mean, whether we bought it back by the end of October, the end of September, it still precludes us from doing anything else on a normal course until March of last next year. And like I said earlier in my opening comments, we'll want to build the cash on the balance sheet before we execute a substantial issuer bid. So there's a lot of experts predicting very low pricing in Q4, just a few months ago. So why blow all of our cash if it didn't make any difference to how we're going to redistribute cash to shareholders. So we've demonstrated again at low methanol pricing our ability to generate excess cash and return it to shareholders.

As far as our minimum cash balances, we've set $100 million to run the company and about $100 million to execute on the Chile projects. So that's where the $200 million comes from. If you look at the net cash, we weren't too much higher than that as we ended Q3 because I'll remind you that the cash in Egypt is trapped. So you have to exclude that cash, and if you look at our cash just on our equity basis, you're not much north of $200 million when you go through the math. So we're exactly where we said we'd be.

And I think now you're going to see cash balances start to increase because we don't have the ability to return it through the NCIB after we complete the bit that we're currently in. I think I've said before that a substantial issuer bid, we'll want to do significant, so $200 million, $300 million. So we'll have to build that kind of cash on the balance sheet before we execute on a substantial issuer bid. So you should expect us to increase our cash balances in the current methanol price environment until we execute on our normal course – sorry, substantial issuer bid or re-launch a normal course issuer bid. Right in line with.

John Roberts
Analyst, UBS Securities LLC

Q

Okay. And then on U.S. Gulf Coast natural gas prices, any changes to your thinking on how you'll be hedged as we go across the winter months here? I think you are 40% hedged, is that correct? And just remind me if I'm wrong there.

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Yes, John, so no change. We're 100% contracted on Geismar I, 40% hedged on Geismar II, and 60% spot. You should expect any change to that. Why that rate? Well at 140 – sorry, that gives us the ability to run both plants at minimum rates if the gas was to blowout in the U.S., which we're anticipating, but I think it allows us flexibility to run both plants, and benefit from low spot gas that we're experiencing today. So I wouldn't expect any change to our strategy there in Geismar.

John Roberts
Analyst, UBS Securities LLC

Q

Great. Thank you.

Operator: Thank you. The following question is from Matthew Blair of Tudor, Pickering, Holt. Please go ahead.

Matthew Blair
Analyst, Tudor, Pickering, Holt & Co. Securities, Inc.

Q

Hey, John. Good morning.

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Hey, Matthew.

Matthew Blair
Analyst, Tudor, Pickering, Holt & Co. Securities, Inc.

Q

I had a question on methanol supply and I guess specifically, the potential of seeing mothballed methanol capacity restarting. So you're looking into this in Chile. I think one of your competitors was planning to restart the mothballed plants in the Netherlands later in 2018. What's your outlook going forward? Do you think this is going to become a theme in the industry? It looks like there is quite a bit of mothballed methanol capacity just sitting out there. So any thoughts on this would be helpful.

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

A

Yes. I would disagree with you. There's quite a bit on methanol mothballed capacity out there. I think you've mentioned the ones that we're aware of, the second plant in Holland. It's mothballed, but it's also been cannibalized. So it will require significant amount of capital to get it restarted. So we have that in our plant, about 100,000 tonnes, I think give or take. There's a couple of plants being relocated, one from Brazil, one from I think it's somewhere in Eastern -- in Middle Asia, I think Slovenia, but don't quote me on that, to West Virginia, a couple of hundred thousand tonnes. But in the big scheme of things, all the plants that can run are running today because we're well above the cost curve. So anybody that wants to run and make cash can run today and we're still seeing pricing above the cost curve. So that tells me that the supply demand balance is quite healthy and inventories continue to go down in China.

So I think these are all great signs and we're going to see additional demand like I said, the -- one of the three MTO plans are starting up as we speak, and the other two by sometime mid next year, and really, not a lot of supply coming on in that similar period. So we think we're in a really good spot from a supply demand fundamental point of view, which should lead to pretty good pricing and excellent results in cash flow generation. So I don't think -- I wouldn't agree with you. There's a lot of file capacity around the world that's looking to start up.

Matthew Blair
Analyst, Tudor, Pickering, Holt & Co. Securities, Inc.
Q

Okay, okay. Thanks. And then just on turnaround, so you had New Zealand and Egypt so far this year. Is it safe to say that we're pretty much done for 2017 turnarounds considering that we're already in November?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.
A

Well, I never guide to turnarounds. What I say is we have 10 operating plants today and you should expect, on a given turnaround cycle of three to four years, that we'll have two to three turnarounds in any given year. Some years, it'll be two. Some years it'll be three. So we tend to like to do these in the months where it's warm, and not cool. So I think we've executed on two like you said, but I'll keep you guessing on three, but I did guide in my previous remarks that we expect very healthy production in Q4 and sales of produced methanol.

Matthew Blair
Analyst, Tudor, Pickering, Holt & Co. Securities, Inc.
Q

Got it. Thank you.

Operator: Thank you. The following question is from Christopher Shaw of Monness Crespi. Please go ahead.

Chris L. Shaw
Analyst, Monness, Crespi, Hardt & Co., Inc.
Q

Hello. How are you doing.

John Floren
President, Chief Executive Officer & Director, Methanex Corp.
A

Hey Chris.

Chris L. Shaw
Analyst, Monness, Crespi, Hardt & Co., Inc.
Q

Just a quick one on the swap transactions. Are those just purely sort of neutral beside the costs you save? Is there any other sort of financial arrangement that happens?

John Floren
President, Chief Executive Officer & Director, Methanex Corp.
A

Well, they're not neutral. There's a sharing of the savings. So there can't be significant savings. So let's take an example. Supplier A is in the Middle East in selling in North America. Their freight might be $60, $70. We might be taking product from Trinidad to Asia. So – and that freight might be $80. So by just saying to that supplier A, deliver to us in Asia, we'll deliver to you and the U.S., let's say, that's a $30, $40 saving per tonne. We'll just share that, just as an example. So it can be quite significant on the saving side. And that just goes into net logistic costs. So you never really see it, but I'll point out, as we've grown our production, our net logistics cost per tonne has come down quite nice. And it's as a result of more production and the great job our supply chain and marketing team is doing on increasing and executing on these swaps.

Chris L. Shaw Q
Analyst, Monness, Crespi, Hardt & Co., Inc.

Okay. And the Geismar facility, now it's been running for a year or so; a year or two. What's the sort of – I remember you were suggesting [indiscernible] (42:45) pipeline distribution across the fence and access to rail, how much – can you quantify how much more net logistic savings per tonne or something that you guys have over an average plant at that facility?

John Floren A
President, Chief Executive Officer & Director, Methanex Corp.

Yes, we don't specify logistics by plant. I think I just mentioned, if you look at our net logistics cost per tonne, it's gone down. And you know, as we add more tonnes in Chile, you should expect our net logistics costs per tonne to go down.

Chris L. Shaw Q
Analyst, Monness, Crespi, Hardt & Co., Inc.

Got it. Thank you.

John Floren A
President, Chief Executive Officer & Director, Methanex Corp.

Assuming the fuel remains kind of where it is today. If fuel was to spike, that would impact our logistics cost.

Chris L. Shaw Q
Analyst, Monness, Crespi, Hardt & Co., Inc.

Great. Thanks.

Operator: Thank you. There are no further questions registered at this time. I'd like to turn the meeting back over to Mr. Floren.

John Floren
President, Chief Executive Officer & Director, Methanex Corp.

Okay. Thank you. So we believe that the methanol industry fundamentals remain strong, and I'm very pleased with the record sales result we achieved in the third quarter. Our plants continue to run well, and I'm also encouraged by the improvement we have seen regarding gas availability in Egypt. Our assets are in excellent shape and in the current methanol price environment, we are well-positioned to generate significant cash flows. Our priority for capital allocation are to meet our financial commitments, meet our near-term growth objectives in Chile and return excess cash to shareholders.

Thank you for the interest in our company. Have a good day.

Operator: Thank you. The conference has now ended. Please disconnect your lines at this time. We thank you for your participation