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Methanex Corp. (MEOH)

Q3 2019 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by. Welcome to the Methanex Corporation Q3 2019 Earnings Call. I would now like to turn the conference call over to Ms. Kim Campbell. Please go ahead, Ms. Campbell.

Kim Campbell

Manager-Investor Relations, Methanex Corp.

Thank you. Good morning, everyone. Welcome to our third quarter 2019 results conference call. Our 2019 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 conclusion, or making the forecasts or projections which are included in the forward-looking information. Please refer to our third quarter 2019 MD&A and to our 2018 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.

I would now like to 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. In the third quarter of 2019, we recorded adjusted EBITDA of $90 million and adjusted net loss of $21 million or $0.27 per share. Adjusted EBITDA was lower in the third quarter compared to the second quarter, primarily because of lower average realized price, which was only partially offset by higher sales volume of Methanex-produced methanol and improved cost compared to the second quarter. Our average realized price was $272 per tonne in the third quarter, which reflects a decline of $54 per tonne from the $326 per tonne that we realized in the second quarter, as our posted prices were lower across all regions and we recorded a discount rate of 17.5%. When prices decline, our discount rate tends to be higher than our guidance of 15%.

We estimate that the industry cost curve, which is set in China, is currently around $260 per tonne and current prices in China are slightly below this range. We recently posted our November North American price, which remains unchanged at $342 per tonne and our Asia Pacific price, which remains unchanged at $295 per tonne. Our European contract price is set on a quarterly basis and our fourth quarter posted price is €280 per tonne.

Methanol industry demand in the third quarter of 2019 increased slightly compared to the second quarter of 2019. Traditional chemical demand declined slightly as a result of planned and unplanned downstream outages, nationwide safety and environmental inspections in China, and a slowdown in manufacturing activity, particularly in the automotive and construction demand segments. Demand into energy-related applications was strong as two new methanol-to-olefins, or MTO plants, with a combined capacity to consume 3.6 million tonnes of methanol annually, started up at the end of June. This new MTO demand was partially offset by planned maintenance activities at some existing MTO plants. We continue to see steady operating rates for most MTO facilities.

Methanol industry supply outside of China operated well in the third quarter of 2019. We observed some high cost producers in China reduce operating rates in the quarter when spot prices dip below the industry cost curve. We're excited to welcome three new ocean going vessels powered by methanol-fuel technology to our Waterfront Shipping fleet during the quarter. These vessels can run on methanol, fuel oil, marine diesel or gas oil. We have one additional methanol-powered vessel joining the fleet in the coming weeks, and with this addition, approximately 40% of our fleet will be capable of running on methanol-fuel technology.

Now, turning to our operational results. In New Zealand, we produced 469,000 tonnes during the third quarter compared to 446,000 tonnes in the second quarter. Upstream natural gas producers in New Zealand are completing significant field development projects to increase production. However, we do not expect to see any impact of these activities in 2020. Based on our current contracted gas position, we are revising our guidance to approximately 80% operating rates for our New Zealand operations in 2020, or approximately 1.9 million tonnes.

In Trinidad, our plants operated well. We produced 474,000 tonnes during Q3, compared to 384,000 tonnes in Q2. Production was higher in the third quarter as our second quarter production was impacted by a turnover at the Titan plant and a short unplanned outage at our Atlas facility. We continue to guide to approximately 85% operating rates for our Trinidad operations.

In Chile, we produced 146,000 tonnes during the third quarter of 2019, compared to 290,000 tonnes during the second quarter. Production was lower in the third quarter as only the Chile IV plant operated during the quarter. Late in the second quarter, we began the first phase of the refurbishment of our Chile I plant, which was scheduled to match lower natural gas deliveries during the southern hemisphere winter months.

The Chile I restarted in early October. Both plants are operating at high rates today and we expect significantly higher production in the fourth quarter, compared to the third quarter from our Chile facilities during their summer months when we receive higher gas deliveries.

In addition, we were very pleased to announce that we reached the longer term natural gas supply agreement for our Chile operations that will underpin approximately 25% of a two-plant operation through the end of 2025. This gas agreement and the completion of the first phase of the Chile I refurbishment reflect important steps to returning our assets in Chile back to full operating rates over the coming years at very low capital costs. In the near-term, we continue to guide to annual operating rates of up to 75% of a two-plant operation or annual production of up to approximately 1.3 million tonnes per year.

In Egypt, we completed the necessary repairs at our facility and restarted our plant safely in August, following the unplanned outage that began early April. We estimate that the Egypt outage had an impact of approximately $20 million, reflecting our 50% share of Egypt on our Q3 adjusted EBITDA results. We have insurance that covers repairs and business interruption subject to deductibles, however, no insurance recoveries have been recorded to-date.

Now, turning to our approach to capital allocation. Our balanced approach to capital allocation remains unchanged. We believe we're well positioned to meet our financial commitments, execute on our growth projects in Chile and Louisiana, and deliver on our commitment to returning excess cash to shareholders through dividends and share repurchases.

In terms of our financial commitments, our expected maintenance capital expenditures for the remainder of 2019 are estimated to be $30 million, primarily related to turnarounds planned for 2020. We continue to advance two near-term growth projects to increase our production capacity for very low capital cost. In Chile, we continue to work with gas suppliers in Chile and Argentina, and they were optimistic they will be able to secure sufficient gas to underpin a full two-plant operation over the medium-term. In Louisiana, we continue to make progress on the debottlenecking opportunities at our existing Geismar 1 and Geismar 2 facilities to increase production by approximately 10% or 200,000 tonnes per year for a few tens of millions of dollars.

We are completing the necessary work required, including construction of a pipeline to bring CO2 to the site and the necessary work at the Geismar 2 plant. We expect that the incremental production capacity will be phased in over the next couple of years. We have begun construction of our third plant in Geismar, Louisiana, an advantage growth opportunity for our company, which we believe will create significant long-term value for shareholders.

Geismar 3 will be a 1.8 million tonne methanol plant, located adjacent to the Geismar 1 and Geismar 2 facilities. We expect this project will deliver outstanding returns based on a substantial capital and operating cost advantages. We believe we are well positioned to complete this project as we have a rigorous and well-defined execution plan, an experienced team in place, and a robust and flexible financing plan.

We ended the quarter with $857 million in cash on the balance sheet. In September, we issued $700 million and 10-year notes and subsequent to the quarter end, we used $350 million of the proceeds to repay the unsecured notes that were due at the end of this year. The remaining proceeds are earmarked to fund Geismar 3 construction expenditures.

In addition, we have a strong liquidity position with an $800 million construction loan facility for the Geismar 3 project that remains undrawn and a $300 million undrawn revolving credit facility to provide further financial flexibility to manage potential unforeseen business stress. As we have stated previously, we have a preference for a strategic partner for G3 project and we continue to pursue that option.

During the quarter, we paid $27 million to shareholders through our regular dividend. Up to June 30, 2019, we repurchased nearly 1.1 million shares of the approximately 3.9 million shares approved under the normal course issuer bid. We did not repurchase shares in the third quarter.

Now turning to the outlook for – our outlook for the fourth quarter. Based on posted methanol prices so far this quarter, we expect average realized prices in Q4 to be slightly lower than Q3. We expect production in the fourth quarter to be substantially higher than the third quarter, as both of our Chile plants are operating during the southern hemisphere's summer months and our Egypt plant is back on line. We expect adjusted EBITDA in the fourth quarter to be higher than the third quarter.

I would now be happy to answer any questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] The first question is from Mike Leithead with Barclays. Please go ahead.

Michael Leithead
Analyst, Barclays Capital, Inc.
Q

Thanks. Good morning, guys.

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

Good morning.

Michael Leithead
Analyst, Barclays Capital, Inc.
Q

I guess, first, if I look at the supply/demand commentary you provided in your release, it appears you saw methanol demand up a bit sequentially, yet prices were down, call it, 15%, 20% sequentially. So, I was hoping maybe you could give a little bit more color on what you're seeing on the supply side and maybe where you're seeing incremental supply that drove such a move in the quarter?

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

Yeah. So, I mentioned already, pricing is just slightly below the cost curve in China. We've seen the industry outside China operate very well in the last two quarters and better than on average over the past number of years, which has caused a little bit extra supply.

Michael Leithead
Analyst, Barclays Capital, Inc.
Q

Got it. That makes sense. And then just on Geismar 3, could you provide us with any update on your discussions for a potential partner for this project? Is that still on the table at this point, or any update there would be helpful?

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

Yeah. Our preference is to have a partner for the project and we're pursuing that option. We're in a discussion with a couple of parties about the potential partnerships. And well, you should expect us to approach couple of parties at a time to gauge interest and discussions are ongoing and our preference is still to have a partner for about 30% of the project.

Michael Leithead
Analyst, Barclays Capital, Inc.
Q

Great. Thank you.

Operator: Thank you. The next question is from Eric Petrie with Citi. Please go ahead.

Eric B. Petrie
Analyst, Citigroup Global Markets, Inc.

Q

Hi. Good morning, John.

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

A

Good morning.

Eric B. Petrie
Analyst, Citigroup Global Markets, Inc.

Q

You noted that the energy-related methanol demand increased 6% quarter-over-quarter. If I exclude the two new MTO plants, what was underlying demand growth, or was it flat?

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

A

Well, the traditional chemical, as we mentioned, was down slightly quarter-over-quarter. We saw quite a few unplanned and planned outages in the downstream. I already mentioned in my remarks that the automotive and construction sectors are a bit weak as well.

Eric B. Petrie
Analyst, Citigroup Global Markets, Inc.

Q

Okay. And secondly, China methanol inventory still look like they remain elevated around 900,000 metric tonnes, what is normalized levels and is it an important driver to getting prices higher in the region?

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

A

Yeah. We see the inventory levels at that level, but I wouldn't call that high, because remember we've got a lot more demand as a result of the additions of MTO. I think the challenge in China today is lack of storage capability, even though demand has gone up significantly over the past few years, storage has not kept pace. And yes, we are experiencing – we see situations during the quarter where ships are lined up to try and unload cargoes, because the tanks are full and that's more of a – as a result of not enough storage, which can lead to some pricing of distressed cargos. So, we think we need to see more storage built to meet the increased demand for methanol, especially on the coast in China.

Eric B. Petrie
Analyst, Citigroup Global Markets, Inc.

Q

Great. Thank you.

Operator: Thank you. The next question is from Jacob Bout with CIBC. Please go ahead.

Jacob Bout
Analyst, CIBC World Markets, Inc.

Q

Hi. Good morning.

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

A

Good morning.

Jacob Bout
Analyst, CIBC World Markets, Inc.

Q

I wanted to ask some questions around the gas contracts in Chile and maybe a bit about the structure of these gas contracts. What was the origin? Is this conventional or nonconventional? And is there any price participation with the supplier?

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

A

Yeah. So, these are for about 25% of our requirements for the two-plant operation. These are all – this – all gas is on the Chile side of the border, all unconventional. All the activity in Chile has been going after tight gas over the last five or six years. So, this is tight gas, and there is a sharing mechanism in this contract that works similar to what I've guided to before. We're about one-third. We share with the producer about $200 methanol, in that kind of ballpark.

Jacob Bout
Analyst, CIBC World Markets, Inc.

Q

And then, in Egypt, can you quantify what the losses were from the outages in the quarter and then how much are you actually expecting to be covered by insurance?

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

A

Yeah. So, in my opening remarks, I mentioned our half, about $20 million EBITDA impact in the quarter. There are some deductibles like I mentioned. And we have made an insurance claim, and we expect to be able to collect on that insurance claim, plus the deductibles.

Jacob Bout
Analyst, CIBC World Markets, Inc.

Q

And is this going to extend into fourth quarter, into 2020?

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

A

The outrage or the insurance claim?

Jacob Bout
Analyst, CIBC World Markets, Inc.

Q

These outages, losses that you're taking there.

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

A

Yeah. So, when the plant came back up in early October and has been running extremely well since then, so that issue is behind us, and we made the insurance claim. And whether we get in Q4 or Q1, it's too early to tell, but we expect to be able to collect on the insurance.

Jacob Bout
Analyst, CIBC World Markets, Inc.

Q

Okay. I'll leave it there. Thanks, John.

Operator: Thank you. The next question is from Joel Jackson with 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

Good morning.

Joel Jackson
Analyst, BMO Capital Markets (Canada)

Q

John, would you be able to give some sort of valuation metrics around what you would be looking for in a 30% stake in some of the different conditions at G3? And then, also as you've been starting to price out long lead time items, how maybe CapEx is faring – your expectations for CapEx is faring in that $1.3 billion, $1.4 billion range for G3? Thanks.

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

A

Yeah. So, just to correct something I just said. The Egypt plant came up in early August, not October. I apologize. But for G3, we're having partnership discussions, like I said, for about 30%, not just financial considerations, but strategic considerations. We're talking to potentially other producers of methanol that maybe looking to build their own facilities somewhere around the world where we can partner together, or a customer, you know, somebody that might be consuming 600,000 tonnes or so of methanol at several locations around the world where [indiscernible] (17:57) methanol and this would help them backward integrate into some equity tonnes. So, both of those kinds of conversations are ongoing, not with Chinese companies, not with American companies, but other parts of the world.

What was the second part of your question, Joel?

Joel Jackson
Analyst, BMO Capital Markets (Canada)

Q

Now that you're getting some long lead items, starting to get price, how your CapEx is fairing within that $1.3 billion, $1.4 billion range?

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

A

Yeah. So, all of the long lead items that we placed the purchase orders for have come back either what we had been indicated in a call or less. So, we're not seeing any surprises on the capital side. I'd say, I was just down there two weeks ago. Some of the other competing projects that we expected to be FID-ed over the coming months seem to be somewhat delayed. So, as far as productivity and labor availability, I'm getting way more comfortable today than I was even three months ago, about our ability to execute on this project within the range of capital we provided.

Joel Jackson
Analyst, BMO Capital Markets (Canada)
Q

Thank you.

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

Thanks, Joel.

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

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC
Q

Hi. Good morning, John.

Operator: Hassan Ahmed, your line is now open.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC
Q

Sorry, I was on mute. Good morning, John.

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

Good morning.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC
Q

John, wanted to revisit the demand side of things. It seems that the energy-related demand sort of ticked up quite nicely quarter-on-quarter in Q3 and conventional demand was down a tad bit. So, I mean, Celanese recently reported their Q3 numbers and they were talking about as much as 25% of their acetic acid capacity down in the quarter and it seems also Sipchem in Saudi had a turnaround as well. So, as I think through that and sort of think about the negative sort of conventional demand growth that you guys saw in Q3, should we expect a lot of that demand growth to come back now in Q4?

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

Yeah. We saw the same thing you mentioned. We saw some unplanned and planned downtime, especially on the chemical side of the equation. We do plan and see this part of the 55% demand for methanol, the chemical side to grow at IP and GDP growth rates. So, provided we're seeing positive GDP and IP growth rates, we would expect those to manage to grow at those amounts.

Now, having said that quarter-by-quarter, they do vary, but usually the Q4 in any given year is the strong demand quarter for methanol, especially in the chemical products and we're not seeing anything that would change our beliefs around that.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC
Q

Understood. Understood. And as a follow-up, in your earlier remarks, you talked about sort of Chinese environmental inspections again sort of popping up and the like. Are you seeing any sort of environmental sort of curtailments at all within the Chinese methanol industry?

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

Yes. We're seeing some, not only in the methanol but in the downstream products more. There have been quite a few industrial accidents in China and that is leading to these inspections and safety is a big concern for us and for the Chinese. So, I think we're probably going to continue to see these inspections both on methanol and methanol derivative plants going forward.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC
Q

Perfect. Thanks so much, John.

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

Thank you.

Operator: Thank you. The next question is from John Roberts with UBS. Please go ahead.

John Roberts
Analyst, UBS Securities LLC
Q

Thank you. The timing of the 10% debottlenecks for Geismar 1 and 2, is that being done to take advantage of any of the synergies with Geismar 3 or because of the upcoming downtime at those sites?

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

No. This has nothing to do with Geismar 3. This is totally isolated projects. Similar – John, this is similar to what we did in Medicine Hat number of years ago, where we had a CO2 source across the fence from an ammonia plant and by introducing CO2 into our production process. Because we have excess hydrogen, we can get more methanol for the same kit. So, we've contracted for CO2 in Louisiana with a supplier of CO2 and we're in the process of building a pipeline to bring that to our sites.

When we did the G1 turnaround, earlier this year, we put in the necessary equipment to be able to introduce CO2 into the system and we'll do the same when we do the Geismar 2 turnaround in the coming quarters. So, that work has been done. The CO2 pipeline has to be built. So, you should think of the first G1 sometime in the end of the next – first quarter next year and then about a year after G2. But that's just roughly guidelines for today and we still have to complete the work.

John Roberts
Analyst, UBS Securities LLC

Q

And then, are you seeing any higher shipping costs from IMO 2020? And do you expect to have to eat that or it'll just reduce the netbacks?

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

A

Yeah. So, we are in our budgeting process right now for next year and we're obviously trying to forecast what's going to happen to, well, methanol. I guess, we have a better view about the ultra-low sulfur diesel market. When you see both sides, you see some people think that that's going to spike in price and others think that there's enough refinery capacity to meet the demand. And I guess, nobody will know until we actually get the demand in Q1. But yes, we will experience higher fuel costs, which will lead to higher freight in our supply chain. And we'll continue to price methanol based on the cost curve and based on the supply/demand balances. So we and other suppliers, if nothing changes on the price side, we'll be eating that additional freight.

John Roberts
Analyst, UBS Securities LLC

Q

Okay. Thank you.

Operator: Thank you. The next question is from Steve Hansen with Raymond James. Please go ahead.

Steven Hansen
Analyst, Raymond James Ltd.

Q

Yeah. Good morning, guys. John, just a quick one here on the partnership for G3, how should we think about the timing of your [ph] perceived (24:15) partner here, given that you've now started construction? I only ask, because every month that passes now, the project arguably de-risks a little more and I'm just thinking that that's got to be a difficult or a sliding scale backdrop for ongoing negotiations. So, are you able to think about a timeline or some sort of like milestone that you would like to have a partner locked up by, given the context of current negotiations? I mean, how should we think about that?

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

A

Yeah. So, we wanted to have a partner before we FID-ed, but here we are. I'd agree with you that as time goes by, the project does get considerably de-risked. We still preference to have a partner for this project and that may impact the buy-in price as the project gets de-risked, but still our preference is to have a partner and we'll pursue that. Like I said before, we're not talking to 10 parties at the same time, we're talking to a couple. And we've put some fairly aggressive timelines as we're talking to potential partners, because if there's no interest, we'd like to go on to some other potential partners. So, we'll continue to pursue that strategy and we're optimistic we'll secure a partner, and we'll continue to work towards that.

Steven Hansen
Analyst, Raymond James Ltd.

Q

Okay. Helpful. And then just one quickly on the supply side as relates to Iran, lots of talk about potential Iranian startups at some point. What is your supply chain telling you, what have you seen in the channel, has there been any indications on shipping from either Bushehr or one of the other projects as yet? Just anything you're seeing on that front would be helpful.

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

Yeah. We don't have any special intelligence from Iran, because being a US-traded company, we obviously can't be doing any business at all with Iran. We have seen the Iranian production in the quarter operate much better than we had anticipated. So, they continue to run and they continue to be able to ship mainly to China and India. So, that was a bit of the upside on the supply side as well. I read the same things you do, Steve, about the next plant, I really don't have any special intel over and above what you read and I read.

Steven Hansen
Analyst, Raymond James Ltd.
Q

Okay, thanks. And just I'll squeeze in one last one if I may on the Chile ramp for Q4. Can you give us some better context? I know you noted that Chile has restarted, but can you just give us a sense for what kind of ramp or what kind of utilization we should expect in Q4?

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

Yeah. So, what I've guided to is 75% operating rate for the year for the two-plant operation. What I've said is, full rates for plant I and plant IV for the nine months when we're not experiencing their winter and one-plant operation during their winter. So, I would expect provided everything goes well with the operation of plants, full rates in Q4.

Steven Hansen
Analyst, Raymond James Ltd.
Q

Okay, very good. Thank you.

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

Thank you.

Operator: Thank you. And the next question is from Jonas Oxgaard with Bernstein. Please go ahead.

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

Hi. Good morning.

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

Good morning.

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

When looking at your non-US margins, historically there's been a strong correlation between the margins and the price, presumably due to the raw material formula, but that seems to broken down lately, the margins have been much lower than the pricing suggest. Has something changed in your formulas, or how should I think about this?

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

A

No, I think we've guided to this in the past. So, about 55% to 60% of our gas today is this formula-based gas and that's mainly outside North America. With inside North America, you should think a more fixed price gas in our portfolio. We do have some fixed price gas in other parts, but mainly its formula outside North America and fixed in North America.

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

Q

Yeah. But I was only looking at the non-US or non-North America margins. So, nothing has really changed. Is there a good reason for why the margin is lower than it's historically been at these methanol prices then?

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

A

I'd have to take it offline. I don't have the numbers in front of me. So, I mean, Egypt didn't run during the quarter. And we have – that's a very high margin business for us. So, we didn't have any sales – there were very few sales for me, that could have impacted, but I'd have to look at the numbers.

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

Q

Okay. Thank you.

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

Nelson Ng
Analyst, RBC Dominion Securities, Inc.

Q

Great. Thanks. So, John, just for New Zealand, could you just give a bit more color in terms of the gas market there? And I guess, I presume there isn't a spot market, so you can't really get more gas in 2020 in terms of that 80% utilization? And then, I guess the second question relates to kind of longer term for New Zealand in 2021, like do you generally expect the utilization and gas availability to improve?

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

A

Well, we've been experiencing a lot of maintenance activities in the upstream in the last number of quarters. So, I thought it would be best to guide to what we expect as opposed to disappointing each and every quarter. Just how we think about New Zealand, its 2.4 million tonnes at full capacity. That's assuming we get the high CO_2 gas, which we haven't got for 10 years. So, the actual capacity we've gotten in the last 10 years is around 2.2 million tonnes. Now, there is high CO_2 gas available and we're still actively trying to contract that, but we haven't done that yet.

So, the way I think about it without the high CO_2 gas, it's a 2.2 million tonne facility and we've been experiencing, like I've said, shortages because of maintenance and other activity. I guess, the good news is, Shell has sold their business to OMV and OMV are investing hundreds of millions of dollars, not only in the infrastructure, but in developing existing reserves as well. There's a lots of other activities from [indiscernible] (30:30), right.

There is no spot market there for gas or very little spot market. So, all the gas that we would consume in our plants is contracted. So, the country itself just re-determined the reserves in Egypt, up by 20% year-over-year, which I think is very positive. So, yeah, I think we're going to have probably similar operating rates that we had this year, next year, but 2021 and beyond we're optimistic we can get to the 2.2 million tonnes and possibly to 2.4 million tonnes, if we can get the high CO2 gas. And I know our team there is working hard towards that goal.

Nelson Ng
Analyst, RBC Dominion Securities, Inc.
Q

Okay. Got it. And then the next question relates to the NCIB. Obviously, you've taken a pause in Q3. I was just wondering what you need to see in your balance sheet or cash flow to start repurchases again?

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

Yes. So, what I said is that we've had this target of about $200 million of cash on the balance sheet. That's not borrowed money, that's actually generated excess cash to the operations. We're increasing that guidance to $300 million, as we're completing the G3 project. Beyond the $300 million, we would plan to return excess cash to shareholders through the dividend and share repurchases. The dividend is going to be – we look at it once a year around April time and make a call whether we grow it or keep it the way it is and we'll look at it again around the AGM time.

When we look at our internal numbers, above $300 methanol realized, we believe that we can complete the project on our own and have a little bit of excess cash to repurchase shares. So, it'll be a factor of methanol price. And like I said, we'll still want to build that cash balance up to $300 million before we would start to exercise the NCIB again.

Nelson Ng
Analyst, RBC Dominion Securities, Inc.
Q

Got it. Thanks, John.

Operator: Thank you. The next question is from Matthew Blair with Tudor, Pickering. Please go ahead.

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

Hey. Good morning. So, your net leverage is moving up with the debt issuance. Can you remind us of any sort of, I guess, like max targets or parameters and what are the chances that you ought to issue equity down the road here?

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

Yeah. Issuing equity is probably – I never say never, but highly unlikely. Maybe I'll ask Ian, our CFO, to comment on the leverage.

Ian P. Cameron
Chief Financial Officer & Senior Vice President, Finance, Methanex Corp.

A

Our target leverage from a balance sheet perspective is 2 times to 3 times debt-to-EBITDA. And as we've described before, we live within that range in methanol prices above $300 a tonne. So, at $300 a tonne, we achieve a leverage ratio of around 3 times and it could go higher than that. Obviously, it goes a lot lower. And that's how we've been running our balance sheet.

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

Q

Sounds good. And then just a clarification on the commentary on global methanol demand, so I think in Q2, you said that your estimates for global methanol demand was up 3% year-over-year and in the commentary talked about a slight improvement in Q3. So, I guess should we be thinking about like a 3% to 4% year-over-year growth rate for global methanol demand this past quarter?

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

A

Yeah. I think going forward, it's about 3% to 4% including the MTO. So, it depends on how the MTO runs and it's hard for us to forecast the future operating rates of our customers, whether they have problems or take downtime, but I think that's a good range of growth.

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

Q

Great. Thank you.

Operator: Thank you. The next question is from Chris Shaw with Monness, Crespi. Please go ahead.

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

Q

Yeah. Good morning, John. How are you doing?

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

A

Very good. Thanks, Chris.

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

Q

I have a question or clarification on the $20 million EBITDA impact from Egypt. Is that just cost that you guys had to spend or was that just sort of reflective of the volume you didn't produce as well or can you just give color on that?

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

A

So, I mentioned we obviously have insurance for both the equipment and business interruption with a deductible. So, that's a combination of both.

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

Q

Okay. And then I had a question about the new Trinidad plant that's coming up. I thought Trinidad was – I think you guys were always having some problems getting gas down there and I'm just curious, do you have any like color on why – how that plant was developed and I don't know for sure who is the owner down there and will they have enough gas and will that impact your gas availability at all?

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

A

Well, since that isn't my project, I'm not going to make any comments on it. I've guided to 85% operating rates for our plants, based on what we've been told to expect for gas and I'm comfortable with that guidance at this time.

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

Q

Do you know the owner of that plant is or is it...

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

A

Yeah. It's Japanese [indiscernible] (35:34) small shareholding, local Trinidad company.

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

Q

Got it. Thanks for the info. Thanks.

Operator: Thank you. [Operator Instructions] The last question is from Cherilyn Radbourne with 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

Most of my questions have been asked, so I'll just ask a couple of quick ones. I was also looking for clarification on the $20 million referenced with respect to Egypt. Would that have related just to the plant outage or would that have also included additional logistics costs that you might have incurred from a supply chain perspective?

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

A

That's just the insurable amount which is the equipment, plus some loss margin, I would say, business interruption. So, I think one of the reasons our logistics costs were higher in the quarter was because of the outage and we had to reconfigure our supply chain as a results of bringing product into the Mediterranean from farther distances which led to higher costs on our logistics. And that would be shown in our logistics cost as opposed to the insurance claim.

Cherilyn Radbourne
Analyst, TD Securities, Inc.

Q

Okay. So, that should normalize in Q4 and going forward then as well?

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

A

Yeah. But again, I'll remind you that we will be paying higher for fuel starting January, because of the new IMO regulations. So, we expect it to normalize in Q4, but to see our logistics cost go up starting next year, because of the higher fuel cost.

Cherilyn Radbourne
Analyst, TD Securities, Inc.

Q

Okay. And then just in terms of the gas supply in Chile. Can you just clarify how far out you've now contracted gas to support up to 75% of the two-plant operation?

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

A

Yes. So, we have 25% contracted out through 2025 and that's the Chile contract. The balance we're getting from Argentina, different lengths of contracts, but they're shorter term and we're in the process of renegotiating those.

Cherilyn Radbourne
Analyst, TD Securities, Inc.

Q

Great. That's helpful. That's all for me. Thank you.

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

A

Thank you.

Operator: Thank you. This concludes the question-and-answer session. I would now like to turn the meeting back over to Mr. Floren.

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

Thank you. We remain focused on strengthening our global leadership position in the methanol industry, enabling us to deliver secure, reliable methanol supply, which is our competitive advantage and makes us the preferred supplier to customers around the world. Our balanced approach to capital allocation remains unchanged. We believe we're well positioned to meet our financial commitments, execute on our growth projects in Chile and Louisiana, and deliver on our commitment to returning excess cash to shareholders through dividends and share repurchases.

Thank you for the interest in our company.

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