

# **Ardmore Shipping Corporation (ASC) Q1 2024 Earnings Call Transcript**

Seeking Alpha - Earnings Call Transcripts

May 8, 2024 Wednesday

Copyright 2024 Seeking Alpha Provided by Syndigate Media Inc. All Rights Reserved

**Length:** 3553 words

**Byline:** SA Transcripts

**Body**

Ardmore Shipping Corporation (ASC)

Q1 2024 Earnings Conference Call

May 8, 2024 10:00 ET

Company Participants

Anthony Gurnee - Chief Executive Officer

Bart Kelleher - Chief Financial Officer

Conference Call Participants

Omar Nokta - Jefferies

Jon Chappell - Evercore

Climent Molins - Value Investor's Edge

Presentation

Operator

Good morning, ladies and gentlemen and welcome to Ardmore Shipping's First Quarter 2024 Earnings Conference Call. Today's call is being recorded and an audio webcast and presentation are available in the Investor Relations section of the company's website, ardmoreshipping.com. [Operator Instructions] A replay of the conference will be available any time during the next 2 weeks by dialing 1-888-660-6345 or 1-646-517-4150 and entering the passcode 95017.

At this time, I will turn the call over to Anthony Gurnee, Chief Executive Officer of Ardmore Shipping.

Anthony Gurnee

Good morning, and welcome to Ardmore Shipping's first quarter 2024 earnings call. First, let me ask our CFO, Bart Kelleher, to discuss forward-looking statements.

Bart Kelleher

Thanks, Tony. Turning to Slide 2. Please allow me to remind you that our discussion today contains forward-looking statements. Actual results may differ materially from those projected in the forward-looking statements. Additional information concerning factors that could cause the actual results to differ materially from those in the forward-looking statements is contained in the first quarter 2024 earnings release, which is available on our website.

And now, I will turn the call back over to Tony.

Anthony Gurnee

Thanks, Bart. So first, let me outline the format for today's call. To begin with, I'll discuss highlights, the near-term market outlook and our capital allocation policy. After which, Bart will provide an update on product and chemical tanker fundamentals and our financial performance, and then I'll conclude the presentation and open up the call for questions.

So, turning first to Slide 4 for highlights. We are seeing strong momentum continuing well into 2024, reflecting positive fundamentals, along with ongoing geopolitical impacts. Our first quarter performance reflects robust market conditions, with adjusted earnings of $38 million or $0.92 per share and with further strength building into the second quarter. Our MRs earned $38,400 per day for the first quarter and $40,500 per day so far in the second quarter with 60% booked. And our chemical tankers on a capital-adjusted basis, earned $29,100 per day for the first quarter and are now up to $39,000 per day for the second quarter with 60% booked so far.

As you can see from the chart on the upper right, the strength of the market is evident. TCE rates are showing a sequential increase, which is notable given that we are coming out of the stronger winter period. Meanwhile, we continue to execute on our longstanding capital allocation policy. Today, we are declaring another quarterly cash dividend of $0.31 per share, consistent with our policy of paying out one-third of adjusted earnings. And we also continue to invest in the fleet to improve performance and reduce carbon emissions while also taking a gradual and opportunistic approach to fleet modernization. And as a final point on this slide, it's important to note that our scheduled drydockings and upgrades are already largely complete for this year. This means that we will have increased revenue days and a more productive fleet, which will boost earnings and allow us to fully capture these strong market conditions.

Moving to Slide 5. The near-term outlook continues to be very positive as a result of geopolitical events and other disruptions. But of course, it's underpinned by very strong supply/demand fundamentals. The EU refined products embargo responsible for splitting the global tanker fleet continues to drive higher ton-mile demand. In addition, the routing of vessels away from the Red Sea and around the Cape of Good Hope is significantly extending those voyage lengths. But it's worth noting that for product tankers, the Red Sea is largely an LR story. Prior to the Red Sea disruption, 20% of the LR fleet transited the Suez Canal and contrast to just 5% of the MR fleet. So while this is positive from a demand standpoint overall, it's not nearly significant a factor for MRs as it is for LRs.

Furthermore, while Panama Canal congestion showed some signs of easing, daily product tanker transits remained 20% below the prior year, further contributing to ton mile demand. But similar to the Red Sea impact, this is not the major driver for MRs, Russia-Ukraine is. Meanwhile, underlying oil consumption continues to grow. The global economy remains resilient and with potential for further upside in the second half. As you can see from the chart on the lower right, global refinery runs are projected to increase by 5% in 2024 to an all-time high of 85 million barrels a day, driven by activity in Asia and Middle East and increases in Chinese refined product export quotas as compared to the prior year adds to this constructive outlook.

Moving now to Slide 6 where we highlight our longstanding capital allocation policy. Given our strong financial position, we're now able to pursue all of our priorities simultaneously as shown on this slide. To this end, we're pleased to declare another dividend of $0.31 per share. And it's also worth noting that since the resumption of our quarterly dividend in the fourth quarter of 2022, we've now paid $70 million in total dividends, representing about 10% of our market cap, a substantial return of capital in just over 1 year.

Subscribe to Seeking Alpha for more content like this

At the same time, we continue to invest in our fleet to improve performance and reduce emissions while also gradually modernizing over time. As already reported, but now executed, in April, we completed the sale of our 2010-built Ardmore Seafarer and the acquisition of the Ardmore Gibraltar, a 2017 Korean-built Eco-Design MR, which has much better fuel efficiency and also greater cargo flexibility than the outcoming Seafarer. But I'm also pleased to say that we more than doubled our money on the Seafarer, which we have purchased at a low point in the market in September 2020.

And with that, I'm happy to hand the call back over to Bart.

Bart Kelleher

Thanks, Tony. Building upon Tony's comments on the market outlook, we'll further examine the industry fundamentals. As we have been discussing, the supply/demand dynamics remain highly favorable. On Slide 8, we'll highlight the significant supply/demand gap, and I'll address each component in more detail on subsequent slides. We can see from the green bars in this chart, the strong forecasted ton-mile growth which is a result of the positive underlying demand fundamentals and ongoing market dislocation. In contrast, we can see the limited net fleet growth across both product and chemical tankers, and in particular, MRs as indicated in the gray and blue bars. So overall, we believe the limited net fleet growth across these sectors, combined with increasing ton miles supports ongoing market strength.

Moving to Slide 9, where we highlight how the low MR tanker order book contrast sharply with a rapidly aging fleet. The chart on the left provides a visual representation of the changes in the MR fleet. 15 years ago, as highlighted in the red quadrant, we observed a modern fleet with a large order book. However, over time, the order book has declined while the fleet has aged. Currently, as highlighted in the green quadrant, we have a low order book and the oldest fleet in two decades with an average age of greater than 13 years.

Looking at the graph on the right side, the current MR order book is at 9% of the existing fleet. And as we have previously mentioned, it is important to point out the impact that Aframax crude tankers have on the overall product tank order book, which stands at 14%. Currently, the Aframax crude tanker fleet is shrinking while still experiencing demand growth. This implies that an increasing proportion of LR2s, most likely older vessels will naturally transition to the crude trades to cover the shortfall in the Aframax fleet.

In addition, as vessels reach 15 to 18 years of age, their trading capabilities typically become restricted, further contributing to the supply tightness in the younger modern global fleet where Ardmore's vessels operate. In fact, within the next 5 years, close to half of the MR fleet will surpass the 20-year age mark and enter the scrapping zone. The current order book at 9 million deadweight tons is just a fraction of the 50 million deadweight tons that will fall within the scrapping age profile in the next 5 years. Slide 22 in the appendix highlights this phenomenon.

Turning to Slide 10, where we address demand drivers in greater detail. As we have discussed earlier, the Russia-Ukraine conflict and the EU refined products embargo has led to a persistent reordering of global product trades, boosting overall ton miles. Concurrently, the energy transition is being tempered by energy reality and market projections continue to show year-on-year growth in oil demands. Meanwhile, the long-term trend in refinery dislocation between East and West, supported by forecast for increasing consumption, will continue to drive incremental ton miles. Please reference Slide 21 in the appendix for additional details. In summary, these robust long-term demand drivers point to continued strength in the product and chemical tankers market.

Moving to Slide 12. Ardmore continues to build upon its financial strength. As a reminder, the chart on the bottom left highlights our achievement of reducing our cash breakeven levels by over $3,000 per day in an elevated interest rate environment. This accomplishment is a result of our effective cost control, lower debt levels and access to revolving credit facilities. Looking ahead, we see a potential pathway to further reduce our breakeven to a level below $11,500 per day. With this aim, we provided notice to execute purchase options on 2 leased vessels for a total of $41 million and expect to close this transaction in June and further reduce our debt cost. And as always, Ardmore is focused on optimizing performance, closely managing costs and preserving a strong balance sheet.

Turning to Slide 13 for financial highlights. As noted, we are very pleased with our performance as we report results of $0.92 per share for the first quarter. We are correspondingly reporting strong EBITDAR for the quarter and continue to frame EBITDAR as an important comparable valuation metric against our IFRS reporting peers. While I won't go into the detail here, there is a full reconciliation of this presented in the appendix on Slide 25. Also, please refer to Slide 26 in the appendix for our second quarter guidance numbers.

Moving to Slide 14. As Tony mentioned earlier, our drydocking schedule for this year is largely complete. And as highlighted by the chart in the upper right, this will lead to increased revenue days and enhanced earnings power for the rest of the year. In accordance with our energy transition plan, we have made some significant investments in our fleet during the recent drydockings to further improve operating performance, reduce emissions and enhance earnings. Total CapEx for 2024 is anticipated to be $17 million, including $11 million related to scrubber installations and other efficiency upgrades as well as ballast water treatment systems. It's worth noting that we now have more than half of our MR fleet outfitted with second-generation carbon capture-ready scrubbers, which are set to further enhance our earnings power.

Moving to Slide 15. Here, we're highlighting our significant operating leverage. As you can see in the chart, for every $10,000 per day increase in TCE rates, earnings per share would increase by approximately $2.30 annually, with free cash flow generation increasing by nearly $100 million over the same time period. This is why the current market outlook is so exciting, and Ardmore's position is very compelling.

Subscribe to Seeking Alpha for more content like this

With that, I'm happy to hand the call back to Tony and look forward to answering questions at the end.

Anthony Gurnee

Thank you, Bart. So to summarize, first, regarding the market. TCE rates remained elevated through the first quarter and have strengthened further into the second quarter, boding well for the full year. These rates are being supported by the geopolitical events we've discussed, most notably for MRs being the persistent reordering of the product tanker trade as a result of the EU refined products embargo. And of course, underlying supply/demand fundamentals remain highly supportive.

And regarding the company, we're continuing to achieve strong TCE performance and effective cost control, generating excellent returns and continuing to bolster our financial position. This enables us to pursue all of our capital allocation priorities simultaneously. In particular, returning capital to shareholders in the form of our quarterly dividend now accumulated to 10% of market cap in just over 1 year while also gradually and opportunistically investing in fleet modernization.

And with that, we're pleased to open up the call for questions.

Question-and-Answer Session

Operator

[Operator Instructions] Your first question comes from the line of Omar Nokta from Jefferies. Please go ahead.

Omar Nokta

Thank you, operator. Hey, guys, good afternoon. Bart, Tony. I mean, it looks like a lot of good stuff happening here. Congrats on a really good quarter and kind of getting the company to where it's at today. I just – I had a couple of questions for you. Maybe just first on the Handys in particular. It looks like there's a pretty good step up here and your averages thus far into the second quarter. You've got 60% book now at 32.5%. I believe that would be a record for you if it holds. What's sort of driving that, if you don't mind giving us some color on what's driving the chemical market there? And any color you can give on how that spot market is looking today?

Anthony Gurnee

Yes. Omar, thanks for that. Yes, the chemicals are doing well at the moment. It's not a big fleet. We do trade them in and out of products and into chemicals. And I think it's just reflective of just good charter in practice and good market conditions. And sometimes, things go really well. It seems like we're hitting our stride now with those ships.

Omar Nokta

Okay. Yes. Alright. Thanks for that. And then just maybe on – Bart, you mentioned the leaseback financing. You're going to – you're exercising the options on the two, the Seahawk and Seawolf, $41 million outlay. Is the plan to use cash or you plan to draw bank debt against those?

Bart Kelleher

Yes. Thanks, Omar. Good question. So plan to draw on our revolvers for that. I mean, certainly, incremental cash generation could be used, but kind of the default going in is that we draw down on the revolvers and we've been able to actually expand the revolving capacity so that we have 100% capacity with all of our banks now. So we've got tremendous flexibility.

Omar Nokta

Okay. Yes. And makes sense. And maybe just kind of on that and final question for me is, clearly, you guys have had a balanced capital allocation policy for several years. You're now at this point where the balance sheet's evolving into potentially a net cash position here in the next few months. Does that in any way change how you're viewing big picture capital allocation?

Bart Kelleher

Thanks, Omar. I think the way we think about it is that it's situational. I mean we know we're in a cyclical business, it is dynamic. Today, we still see that we have some additional runway on the debt reduction. We still have $100 million of debt and really chipping away at that breakeven has been the key thing in terms of our earnings quality and incremental cash flow and then incremental capacity for the dividend. So just to put it into perspective, at the $13,250 level today, if we hadn't delevered, we will be north of $17,000 per day cash breakeven. So that delta represents $35 million more in cash flow generation per year or approximately $0.83. And then we also see runway to continue investing in our fleet and the energy transition projects. And they're typically short payback periods, significant return levels and we certainly don't have a problem returning additional capital to shareholders at the right time. I think we just see that like right now in the immediate future, where we have opportunities to deploy the capital internally, that's what's in focus.

Subscribe to Seeking Alpha for more content like this

Omar Nokta

Okay. Thanks, Bart, that's very helpful. And good points, and it's interesting. Here we are, you're obviously earning very strong rates, but yet you're keeping a very close focus on that breakeven and lowering it. So good to see that and well done again, guys. Thank you.

Anthony Gurnee

Thanks, Omar.

Operator

[Operator Instructions] Your next question comes from the line of Jon Chappell from Evercore. Please go ahead.

Jon Chappell

Thank you. Good afternoon. Bart, I'm going to stick with you for a second. This path to $11,500 on the cash breakeven. Is that strictly the sale and leasebacks on these two vessels in the $41 million or are there other either sale and leasebacks or other cost initiatives that takes you from that just over $13,000 to sub $11,500 over time?

Bart Kelleher

Sure, Jon. No, thanks. The sale leasebacks is a component of it. But we're always actually looking at additional cost reductions and have achieved some through this year already on the expense side. And then also further reduction of debt, reducing the interest expense beyond the sale leaseback. So kind of multifaceted but something that we just see as really boosting the quality of earnings and then really setting up Ardmore kind of for any market scenario well into the future.

Jon Chappell

Okay. And then over 50% of the MRs with scrubbers now or planned for scrubbers is the ultimate target to get the entire fleet there? Are there a couple maybe older vessels that you'd be holding back and I want to put that capital into?

Bart Kelleher

Yes. Thanks, Jon. We're really happy with the scrubbers thus far in getting half of the fleet installed on the MR side has been great. We've done it during the regular drydocking period, so we don't incur an incremental cost to do so. So really looking ahead, it will be more – our 2015-built vessels next year for drydocking something that we likely continue to roll out and they have good returns. We like the scrubber 2.0 technology and also the carbon capture readiness for potential future applications.

Jon Chappell

Okay. Just finally, is there any way to quantify the – either returns or the rate differential of the ships that have had the scrubbers put in? I'm not sure if this is coincidental or it's something to read into, but the Eco-Design versus the Eco-Mod, there was a $6,500 spread in the first quarter of '23, and they're basically right on top of each other in the first quarter of '24. Was that more just kind of the market strength? Or are there some of the Eco-Mods given the scrubbers and that's really narrowed the gap?

Anthony Gurnee

Well, the Eco-Mods at this point, we just see the charters in and the ones that we sold in charter back as well as another market charter in. So if you strip away everything – essentially, these scrubbers will generate the same benefit as any other scrubber – on any other companies MRs.

Jon Chappell

Yes. Got it. thanks, guys.

Operator

Your next question comes from the line of Climent Molins from Value Investor's Edge. Please go ahead.

Climent Molins

Good morning. Thank you for taking my questions. Omar and Jon have already hammered some of the key points, but I was wondering, could you provide an update on your investment in E1 Marine?

Subscribe to Seeking Alpha for more content like this

Bart Kelleher

Sure. And as a reminder for the listeners. A few years ago, in 2021, the company made an investment in Element 1, which has proprietary technology to take methanol and produce pure hydrogen, and that can be used in a wide range of fuel cell applications and I think also important to remind that it was a multifaceted deal. So that was also when we put $40 million of preferred on our balance sheet at a time when the company really needed the capital. And so now today, Element 1, like other industrial companies when you have this proprietary technology and you're looking to monetize it, they're expanding their global scale in terms of license agreements across geographies and across verticals. So marine included, but really other verticals, off-highway, on-highway charging stations, aerospace. So significant momentum with licensing revenue. And I think just also important to note though, like for us, that's a $10 million investment. So a small portion of our overall asset base and the one that's outside of our own fleet of actual vessels, but certainly part of our energy transition plan and team today.

Climent Molins

Thank you, that's all for me.

Operator

There are no further questions. Ladies and gentlemen, this concludes today's conference call. Thank you very much for your participation. You may now disconnect.

**Load-Date:** May 8, 2024

**End of Document**