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Methanex Corp. (MEOH)

Q2 2021 Earnings Call

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Analyst, UBS Securities LLC

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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to the Methanex Corporation Conference Call hosted by Ms. Kim Campbell held on Thursday, July 29, 2021 at 11:00 AM Eastern Time. [Operator Instructions]

Ladies and gentlemen, thank you for standing by. Welcome to the Methanex Corporation Q2 2021 Earnings Call. I would now like to turn the conference call over to Ms. Kim Campbell. Please go ahead, Ms. Campbell.

Kim Campbell

Director-Investor Relations, Methanex Corp.

Good morning, everyone. Welcome to our Second Quarter 2021 Results Conference Call. Our 2021 second 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 stated outcome to differ materially from the actual outcome. Certain material factors or assumptions were applied in drawing the conclusions or making the forecasts or projections which are included in the forward-looking information. Please refer to our second quarter 2021 MD&A and to our 2020 Annual Report for more information.

I would also like to caution our listeners that any projections provided today regarding Methanex's future financial performance are effective as of today's date. It is our policy not to comment on or update this guidance between quarters. For clarification, any references to revenue, EBITDA, adjusted EBITDA, cash flow 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 event. These items are non-GAAP measures that do not have any standardized meaning prescribed by GAAP and are therefore unlikely to be comparable to similar measures presented by other companies. 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.

Thanks, Kim. Good morning, everyone. Today, I'm pleased to discuss our excellent second quarter 2021 financial results. In addition, we'll share our view of the methanol markets, review our operational results, and discuss our outlook entering the third quarter. We'll also make a few remarks regarding our decision to restart construction on our Geismar 3 project, our strategic shipping partnership and our priorities around capital allocation, including the recent announcement to increase the quarterly dividend, then we will open up the call for your questions.

So turning to our financial results, we increased our average realized price in the second quarter to \$376 per tonne, a \$13 increase compared to the first quarter. Adjusted EBITDA increased to \$262 million in the second quarter, an increase of \$20 million compared to the first quarter. We also recorded higher adjusted net income of \$95 million or \$1.24 per share in the second quarter, an increase of \$13 million or \$0.17 per share compared to the first quarter. These results illustrate the significant leverage that our earnings have to methanol prices.

Now, turning to the methanol market, over the last 12 months methanol prices have rebounded as the global economic recovery continues and vaccines roll out worldwide. Current methanol industry dynamics are favorable, supported by strong methanol demand, low global inventory levels, ongoing industry supply challenges, and a constructive energy price environment. We estimate that the global demand – methanol demand increased by approximately 3% in the second quarter compared to the first quarter. We anticipate that global methanol demand will surpass pre-pandemic levels later this year.

Strong methanol demand combined with ongoing industry supply challenges around the world, and the delayed startup of new industry capacity additions supported higher prices in the second quarter, with tight market conditions continuing into the third quarter. We estimate that the industry cost curve set in China has increased to approximately \$300 to \$320 per tonne supported by rising coal and natural gas prices.

We recently posted our August prices, which remained at \$542 per tonne in North America and \$420 per tonne for Asia Pacific. We set our European contract price quarterly and our third quarter posted price is €410 or approximately \$485 per tonne. As we mentioned on our call in mid-July, over the last few months we completed a comprehensive review of the medium- to long-term industry outlook.

We reviewed our expectations for demand growth and timing for new industry capacity additions and industry operating rates for new and existing methanol plants over the coming years. Based on that work, we believe that the methanol industry medium-term outlook is positive and new industry supply will be needed to meet growing methanol demand over the next five years.

Now turning to our operational results, our second quarter 2021 production of 1.5 million tonnes was lower than the first quarter, primarily due to the lower gas availability in New Zealand and Chile. In New Zealand, our production was lower in the second quarter compared to the first quarter due to ongoing lower gas deliveries. In addition, we agreed to a short-term commercial arrangement with Genesis Energy to make natural gas available to support a tight New Zealand electric – electricity market.

As a result, we temporarily idled one of our Motunui plants for approximately three months. We expect the margin from the sale of gas will be – offset the margin loss from the lower forecasted production line of 85,000 tonnes. We estimate that – production in New Zealand for 2021 of 1.4 million tonnes. The upstream gas sector is completing several field development projects that could improve gas availability over the coming years.

In Geismar, our production in the second quarter was higher than the first quarter as we completed a planned turnaround at our Geismar 2 facility in the first quarter. We finished the debottlenecking project at our Geismar 2 plant in the second quarter of 2021 following the work completed at our Geismar 1 plant late in 2020. As a result, our operating capacity for our Geismar facilities is now 2.2 million tonnes on an annual basis, an increase of 10%. Completed for our capital costs were approximately \$125 per tonne for the addition of 200,000 tonnes of capacity.

In Trinidad, our production in the second quarter was higher than the first quarter as we received full gas deliveries. Based on current gas deliveries, we estimate that production in Trinidad for 2021 to be 1.1 million tonnes, reflecting Methanex's equity interest.

In Chile, as expected, our production in the second quarter was lower than the first quarter. We typically experience lower gas deliveries in the Southern hemisphere winter months, impacting our second and third quarters. We should receive higher gas deliveries in the fourth quarter and we estimate production in Chile for 2021 to be 800,000 to 900,000 tonnes.

In Egypt, our production in the second quarter was slightly lower than the first quarter due to minor technical issues that have been resolved.

In Medicine Hat, our production in the second quarter was similar to the first quarter as the plant ran at nearly full operating rates.

Now turning to our balance sheet, we have a strong financial position with over \$750 million in cash on our balance sheet at the end of the second quarter. This amount reflects our strong adjusted EBITDA results in the second quarter and the repayment of \$173 million drawn on our G3 construction facility. We've previously announced a strategic shipping partnership with Mitsui O.S.K. Limited (sic) [Lines] or MOL with the proceeds of \$145 million expected by the end of 2021. This transaction will not have a material impact on our earnings.

Our Waterfront Shipping subsidiary generates revenue from shipping methanol to Methanex customers and third-party backhaul arrangements. As a result of the partnership, MOL will be entitled to a proportional share of Waterfront's net earnings, which fluctuate based on ship volume and tanker market rates.

However, in terms of our financial statements, our ownership of Waterfront Shipping now and after this transaction is complete is accounted for on a consolidated basis, resulting in 100% of the revenue and expenses being included in our financial statements. We continue to generate meaningful cash flow across a wide range of methanol prices and have an undrawn backup liquidity, including our \$600 million G3 construction facility and our \$300 million revolving credit facility.

Now turning to our Geismar 3 project, we were pleased to announce that our board unanimously approved the restart of the construction of our Geismar 3 project, a unique project with significant capital and operating cost advantages that enhance project's returns. An abundant low-cost natural gas supply in the US underpins production for this project.

In addition, we estimate that G3 will have one of the lowest CO2 emission intensity profiles in the industry. Ultimately, Geismar 3 will strengthen our asset portfolio and substantially improve our future cash generation capability. We believe that Geismar 3 will deliver significant long-term value to our shareholders.

Our capital cost estimate for the project is \$1.25 billion to \$1.35 billion. We expect that approximately \$435 million will be committed to the project as of the end of Q3 2021 through the care and maintenance period. We expect approximately \$800 million to \$900 million of the remaining capital cost after resuming construction in October 2021.

We are confident in our ability to complete this project on time and on budget. We have substantially reduced the project execution risk profile over the last 24 months. We are well positioned from a labor perspective as construction on our project is ahead of other major capital projects in the region. We have also secured prices for the majority of our bulk material costs. Our remaining budget includes allowances and contingencies for both escalation and the remaining risks on the project.

Then lastly turning to our capital allocation priorities. Our capital allocation priorities remain the same. We use the cash that we generate to maintain our business, pursue value-accretive growth opportunities, and continue our strong record of returning excess cash to shareholders.

Going forward, we will increase our emphasis on financial flexibility in three ways. We plan to hold more cash, targeting a minimum of \$300 million of cash on hand plus our remaining G3 capital cost during construction. We plan to target lower leverage and reduce our debt levels over time to a target of approximately 3 times debt-to-EBITDA as methanol price is between \$275 to \$300 per tonne, and we will increase our weighting on flexible vehicles for distributions, such as share buybacks combined with sustainable dividend to return capital to shareholders.

We recently announced that we've reset our quarterly dividend to \$0.125 per share. We anticipate that we'll have the ability to further delever and increase shareholder distributions such as share buybacks in a few quarters at methanol prices of approximately \$325 a tonne or higher.

Geismar 3 is the only significant growth capital in our plans over the next few years. We expect that G3 will substantially increase our cash generation capability and support a significant increase in our future shareholder distribution potential.

Now turning to the outlook for the third quarter. We expect realized methanol prices in the third quarter of 2021 will be similar to the second quarter based on our posted prices so far. We forecast that our third quarter production will be similar to the second quarter. We anticipate our adjusted EBITDA results in the third quarter to be similar to the second quarter.

Finally, I want to mention that we recently published our annual Sustainability Report. We have publicly reported on our sustainability performance since 1997 and continue to enhance our sustainability and ESG-related disclosure to align with evolving best practice and to support greater transparency and comparability.

This year, our disclosure is aligned with the Sustainability Accounting Standards Board or SASB reporting standards for the chemical and marine transportation sectors. Also, our disclosures reference some aspects of the Task Force on Climate-related Financial Disclosures or TCFD and some requirements of the Global Reporting Initiative or GRI. We will continue to look at ways that we can improve our sustainability performance and reporting over the coming years.

I would now be happy to answer any questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Thank you for your patience. And the first question is from Steve Hansen from Raymond James. Please go ahead. Your line is now open.

Steve Hansen

Analyst, Raymond James Ltd.

Yeah. Good morning, guys. John...

Q

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

Good morning.

A

Steve Hansen

Analyst, Raymond James Ltd.

...just thinking about Chile specifically for a minute. In the past, you've gone through the effort of refurbishing Chile I and then starting Chile IV, and this is all pre-COVID. But just give us a sense for where the gas availability might lie there in the region right now and any plans you might have over time to think about the two-plant operation. I understand that COVID required some reshuffling of the production asset profile, but just getting a sense for now that we're into recovery mode here, where do you think about that complex going forward?

Q

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

Yeah. I think the gas profile in Argentina has improved a lot in the last 12 months. We're running our plant right now on Chile gas and that profile has also improved in the last 12 months. So our expectation, Steve, today is by the late third quarter, early fourth quarter, that we'll be running both plants in Chile.

A

Steve Hansen

Analyst, Raymond James Ltd.

Okay. Great. That's very helpful. And just can you clarify, I missed the number, but the metric that you cited on the cost per tonne to complete the G1, G2 bottlenecking. And just now that those two projects are now complete, any other bottlenecking projects that you might be contemplating across the portfolio? Thanks.

Q

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

Yeah. We're always looking to get more methanol out of our existing kits. So we're always – have lots of ideas that we look at and execute if they make sense. So we are continuing to look for other debottlenecking opportunities, but nothing to report today, Steve. The costs for completing the 200,000 additional debottleneck in Geismar was \$125 per tonne.

A

Steve Hansen

Analyst, Raymond James Ltd.

Very helpful. Thanks, guys. I'll jump in the queue.

Q

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Thanks, Steve.

Operator: Thank you. The next question is from Ben Isaacson from Scotiabank. Please go ahead. Your line is now open.

Ben Isaacson

Analyst, Scotiabank

Q

Thank you very much. First question is given the changing operating rates in your portfolio over the past year or so, can you update us as to what percentage of your sales go into each of the three or four major methanol markets depending on whether you break China out of Asia or not? And based on the review that you conducted at the methanol market to restart G3, do you see G3 impacting your regional sales allocation in the future? How do you see that changing?

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Yeah. So we've earmarked 100% of G3 to go to Asia in the modeling that we've done for the economics and the IRR calculations that we've shared. So that hasn't changed. So if we're able to do better than that and place some in the Atlantic Basin, obviously, that makes the economics even more attractive than what we've already published, really attractive economics.

We don't disclose, Ben, where our product goes around the world. It's a very fluid supply chain and we move product to optimize our netbacks as well as to take advantage of certain spot situations that may arise in different parts of the world and to balance out our supply chain and inventories. So we don't really disclose what product goes where.

Ben Isaacson

Analyst, Scotiabank

Q

Thank you. And my follow-up is can you just talk about how the freight market is impacting the company? Maybe discuss the magnitude of freight rates versus normal. Who's bearing additional cost? Is it Methanex or is it built into prices? And I guess you being an active shipper and an owner of Waterfront, do you have an outlook in terms of how freight rates will evolve?

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Well, we wish they're a lot higher. I mean, despite what we're seeing in container markets and dry bulk, liquid tankers for chemicals are still not that great, below what I'd call average prices. So, we'd like to see higher prices because, obviously, we make more money with higher prices and we think we have a competitive advantage on our shipping. So, there seems to be still lots of tanker capacity in the world and we're not seeing the same thing that the world is seeing on dry bulk and containers.

Ben Isaacson

Analyst, Scotiabank

Q

Great. Thank you.

Operator: Thank you. The next question is from John Roberts from UBS. Please go ahead. Your line is now open.

John Roberts

Analyst, UBS Securities LLC

Q

Thank you. LyondellBasell had an unfortunate incident yesterday with their acetic acid plant. Is that methanol unit running, do you know? And will that come into the merchant market here until they can get the acetic acid plant back up again?

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Yeah. I don't have any more information about that site than what's been reported in the press. And I haven't seen anything reported regarding operations. My understanding, based on what I've read, they were in planned turnaround for the acetic acid unit. So it was a planned – they were just starting the turnaround is what I understand and that's why the contractors were entering the unit. I don't know any more than that, John.

John Roberts

Analyst, UBS Securities LLC

Q

Okay.

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Yeah. I agree it's a really tragic event and I think it really illustrates all the attention that we've put on safety and process safety. And you can never take your eye off the ball because there was another event in Germany this week as well in Leverkusen where two other people were killed. So, really tragic events.

John Roberts

Analyst, UBS Securities LLC

Q

And then, since you just updated your longer term industry outlook, what did you assume longer term for your gas-constrained plants? Do you assume an eventual restart at Titan or an eventual restart at Waitara Valley in the longer term outlook or how long do you wait before you think about other options for the equipment that's there?

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Yeah. We're optimistic that, over time, we'll get those plants restarted. We've put a little bit in our five-year outlook, but certainly not full rates for those two sites.

John Roberts

Analyst, UBS Securities LLC

Q

Thank you.

Operator: Thank you. The next question is from Joel Jackson from BMO Capital Markets. Please go ahead. Your line is now open.

Joel Jackson

Analyst, BMO Capital Markets Corp. (Canada)

Hi. Good morning, John.

Q

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

Good morning, Joel.

A

Joel Jackson

Analyst, BMO Capital Markets Corp. (Canada)

A couple of questions. I'll go one by one. John, thanks for giving the guidance for Q3. It looks like your guiding to a 19% discount rate again in the third quarter, so third quarter in a row aback. Is it fair to say that based on your contracts and what's going on here, that we should be modeling as a placeholder now 19% discount rate, not 17%? Last quarter, you had said that the 19% discount rate, a little bit higher than 17%, was because of some weak Chinese spot prices. The Chinese spot prices rose a fair bit in the third quarter. Can you help us reconcile all that?

Q

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

Yeah. So I'm not changing my guidance, Joel, on the discount rate at this time. If we think it's a permanent structural change, we'll certainly change the guidance so I'm comfortable on 17%. And I would look at the overall netback price. That's what we'd look at. [ph] \$375 (00:20:59) for the quarter was an excellent quarter and generated over a \$1 billion run rate. So, we're very happy with the realized price in the quarter and we're expecting strong pricing to continue in the second half of this year.

A

Joel Jackson

Analyst, BMO Capital Markets Corp. (Canada)

Thank you for that. So my other question is obviously different investors want different things. You know that being in this role for a long time. And you've laid out, and thank you for this, couple of weeks ago what your strategy is will be around buybacks. You want to make sure on your balance sheet, you have your cash buffer. I think you said \$300 million, and then you would have enough cash on the balance sheet build up to finish G3.

Q

[ph] So, the other question (00:21:38) for you is looking at what the share price is doing, there's a clear valuation disconnect I think between the stock price and where your earnings and free cash flow power are, where commodity price levels are. Typically, the finance book says you should be doing share buybacks, right? You should be going in the market, buying your stock, and reducing that disconnect. You have G3; it makes sense why you're doing it. But does this all make you think about maybe changing some of the thoughts that maybe you should take out a bit more risk and buy back stock a bit earlier before having all the cash for G3 on the balance sheet?

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

Yeah. So our financial strategy has not changed. I mean, we fine-tune it, as you pointed out, a couple weeks ago, but use this for cash that's generated from the business or to maintain the business, grow the business with value-accretive projects like G3 and then return excess cash to shareholders. But the slight tweak is to have a

A

little bit less on a fixed return to shareholders. So we've reset the dividend at \$0.125 and had more flexibility to return cash in a flexible way to shareholders.

So that \$325 per tonne in higher methanol realized prices we think in a few quarters as we delever a little bit and increase a little bit of cash on the balance sheet for G3 that we'll be able to enter into a share buyback. But our policy of borrowing money is not to buy back shares. So any kind of money that we borrow is for the project, G3.

And I'll remind you, we did change our strategy there during COVID where our plan was to use the construction loan and to draw on it as we continued on the project. And with COVID, we decided and then replaced that, sorry, the construction loan with bonds over time. And we decided to, because the markets were open last September, to just go out and get all the bonds at that time. So that's why we have quite a bit of cash on our balance sheet, but it's allocated for G3, and we're not going to use it to buy back shares.

Joel Jackson

Analyst, BMO Capital Markets Corp. (Canada)

Q

Thank you.

Operator: Thank you. The next question is from Eric Petrie from Citi. Please go ahead. Your line is now open.

Eric B. Petrie

Analyst, Citigroup Global Markets, Inc.

Q

Hey. Good morning, John.

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Good morning.

Eric B. Petrie

Analyst, Citigroup Global Markets, Inc.

Q

Methanex's posted methanol price spread between Asia and North America is kind of at a record of roughly \$100 a tonne. So how do you think about it? Is it sustainable? And going forward, how do you see that level trending?

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Yeah. We've said for a number of years, despite lots of analysts writing to the contrary, that we think the basin balances and price differentials will continue and they are higher than we would have even assumed and that's based on production issues in the Atlantic Basin. So, how long this record – I don't know if it's a record, but it is on the higher end of the differential goes, it really depends on what we and our competitors do with product that we're producing in the Atlantic Basin.

So I can't predict what our competitors are going to do. We know what we're going to do and we would expect that the basin differentials to continue, maybe not at their current levels, but they will continue.

Eric B. Petrie

Analyst, Citigroup Global Markets, Inc.

Q

Okay, helpful. And as my follow-up question, you mentioned the higher China coal prices and natural gas prices. I think coal was trading around RMB 1,000 per metric tonne, double that from recent lows. So how do you see prices of coal going forward and the cost curve evolving into 2022?

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Yeah. There's – coal remains quite, we understand, not readily available in China. They're consuming a lot for our generation. So, if the economic activity continues, we would expect coal to continue to be priced higher than what we were thinking.

There's two markets in China for coal, as you remember. There's the power generation market, which is really set by the government and that's not anywhere near RMB 1,000 per tonne. And then there's the spot market or the other traded market, which where chemicals and others get their coal. And the reason it's RMB 1,000 is because of supply-demand fundamentals.

You're right to point out gas has really shot up not only in North America. It's almost close to \$4 an mmbtu now. But in Europe, it's at \$12 and nobody was predicting that a year ago, and that's really impacted methanol production in Europe.

There's two plants in Holland. One is shut down and the other one is operating at minimal rates because of the high gas prices. And it's hard to see at this point that those gas prices coming down in the near future based on the inventories that we see in the United States, but these things have a way of changing quickly and nobody predicted \$12 gas. But I think it's a function of a couple years of \$150 gas with no investments.

So, I always say the cure for high prices is high prices and the cure for low prices is low prices, and that's what we see in commodities.

Eric B. Petrie

Analyst, Citigroup Global Markets, Inc.

Q

Great. Thank you.

Operator: Thank you. The next question is from Hassan Ahmed from Alembic Global Advisors. Please go ahead. Your line is now open.

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 I. Ahmed

Analyst, Alembic Global Advisors LLC

Q

John, a question on demand. You mentioned sequentially global demand was up according to your estimates by, I believe, 3%. And if I remember correctly, sequentially in Q1, demand was down. So the question is, what are

you guys seeing or what are you forecasting in terms of demand growth for the remainder of the year? And I guess where I'm going with this question is that again and again, you mentioned it, a bunch of other chemical companies mentioned it about obviously supply chain disruptions that have happened over the last couple of months, inventories being lean, people sort of backfilling sort of orders probably a function of winter storm Uri as well. So just trying to get a sense of where you feel underlying demand is and could we even expect a further bump-up from this 3% that we saw in Q2.

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Like I said in my remarks, we expect to get back to pre-pandemic levels later this year. So that has increased demand. In Q3, there are some MTO plants that are taking some planned maintenance. The MTO industry has been operating at really high rates for a couple of years. In Q2, they operated at 92%, which is above our even estimate. So, we expect them to have some maintenance, which could impact demand, but we expect demand to continue to grow through the second half of this year.

A couple of applications that are still lagging are the fuels applications, MTBE, biodiesel, those kinds of applications because we're still not seeing globally a return to normal driving habits because of the pandemic. So, we expect those to improve as we get back to more normal habits as people are vaccinated and the pandemic is brought under somewhat of a control.

Hassan I. Ahmed

Analyst, Alembic Global Advisors LLC

Q

Understood. And the other side of the equation on the supply side, obviously, a healthy pricing environment and pricing continues to tick up. Obviously, you guys announced the restart of – or work on Geismar 3, but what are you guys seeing broadly speaking in terms of the broader industry supply response? And are you seeing any sort of project delays or maybe even people sort of ratcheting up their plans in terms of bringing online new supply?

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Yeah. I think having the price environment that we just come through for almost two years, a lot of projects that were being thought about were shelved or canceled altogether, we expect the coke plant to run at some point. We understand they ran for a bit in July, but they'll get lined up and run at some point during this year is our current expectation. Beyond that, we have a bit of supply coming on in Iran. How it runs is anybody's guess. Certainly, the track record has not been great.

And then China will add a bit of capacity in the Inner Mongolia, backward-integrate a couple of MTO plants and some other plants will come out as more and more restrictions on the east coast of China. So net-net, we're not expecting much new supply beyond what's coming in from coke in Iran over the coming three to five years.

Hassan I. Ahmed

Analyst, Alembic Global Advisors LLC

Q

Understood. Very helpful, John. Thanks so much.

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Thank you.

Operator: Thank you. The next question is from Nelson Ng from RBC Capital Markets. Please go ahead. Your line is now open.

Nelson Ng

Analyst, RBC Capital Markets

Great. Thanks. Good morning, John.

Q

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

Morning.

A

Nelson Ng

Analyst, RBC Capital Markets

Just a quick question for you. So, you mentioned earlier that you were optimistic on gas availability in the various regions going forward. In New Zealand, in particular, I think gas production has been pretty low this year. Do you have any color on production levels going forward in terms of like production issues, drilling activity, and whether current prices are like incentivizing more exploration?

Q

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

Yes. I'll remind you, the gas in New Zealand is very wet gas, so there are lots of barrels of liquids with – and oil prices haven't really helped the economics and they're really going after the liquids. So a higher energy complex in general is positive for our business, and that's one of the reasons it incentivizes more exploration and development.

A

The situation in New Zealand really was – the [ph] focal here or field (00:31:53) failed and that lost 30% of its production late last year, and nobody was expecting that and that's caused the gas market to tighten up quite substantially. The current situation in there, winter, as well, they had a lack of rainfall which is leading to lower than expected hydropower. It's rained again in New Zealand so that situation is behind us now, and there's drilling going on.

I think that's the positive thing for us, is that the upstream owners of the field, Maui and Pohokura, are drilling and planning to drill more. So we'll know a little bit more in the next 12 months the results of those drilling and, like I said, we're certainly contracted for two plants really into the end of the decade and we're optimistic that drilling will be successful and we'll see a third plant have a reasonable opportunity to start up as well.

This is not new in New Zealand. We've seen this before and they pretty well-developed the reserves as the country needs them. So yeah, we're optimistic, but really I think we'd be modeling a two-plant operation at this point until we see the results of what's happening in the upstream.

Nelson Ng

Analyst, RBC Capital Markets

Great. Thanks for the additional color. I'll leave it there.

Q

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

[ph] Thanks (00:33:12).

Operator: Thank you. The next question is from Laurence Alexander from Jefferies. Please go ahead. Your line is now open.

Laurence Alexander

Analyst, Jefferies LLC

Q

Hi there. Could you give a update on what line of sight you have to the amount of global shipping capacity that is ordered or under construction that would use methanol as a flex fuel and what that could mean for methanol demand over the next four, five years; and similarly, what you're seeing in the Chinese industrial boiler market development?

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Yeah. So, we have eight of our own ships on order. Proman, our competitor out of Trinidad, has six and Maersk has one. That's what's on order at this time but lots of other interest. So takes about two years to build a ship, Laurence, so I don't know how many more orders are going to be placed in the next few years, but we would expect more. Each ship around a 50,000 deadweight vessel running on methanol a 100% of the time would consume between 10,000 tonnes and 12,000 tonnes. So you can do the math there.

As far as boilers, yeah, we continue to see that market replacing coal, but there's other potential natural gas as well and diesel. So that market continues to be a couple of million to 3 billion tonnes of methanol demand and we would expect it to grow.

Laurence Alexander

Analyst, Jefferies LLC

Q

And do you have a sense in your more industrial or formaldehyde application and so forth what's the kind of level of pent-up demand is? I mean, downstream companies are talking about having lost 1% to 2% of volume because of supply chain issues, but there's probably some kind of multiplier effect when we get back up to the commodity that you supply or...

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Yeah, I'd be guessing, Laurence, so I probably don't have a good guess, but I would agree with the assumptions there's pent-up demand.

Laurence Alexander

Analyst, Jefferies LLC

Q

Yeah. Thanks.

Operator: Thank you. The next question is from Matthew Blair from Tudor Pickering Holt. Please go ahead. Your line is now open.

Matthew Blair

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

Q

Hey. Good morning, John. It looks like Trinidad natural gas production is down about 21% year-to-date versus the same period last year. You raised your Trinidad volume guidance pretty meaningfully, so is that just good work from your procurement team or is there anything else going on there?

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

No, we've been – being supplied 100% of our gas allocation for Atlas for most of the year, and that's what we've been told to expect for the balance of the year and that's the guidance we provided.

Matthew Blair

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

Q

Great, sounds good. And then on our modeling, your implied costs seemed to drift up a little bit in Q2. Would you agree and were there any factors that you can point to? And then as we look at Q3 and just thinking about the higher [ph] nat (00:36:10) gas environment in the US, I know you're hedged, but could you talk about whether this would be something we should be thinking about for Q3 modeling?

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Yeah. Nothing abnormal in our cost structure. Quarter-to-quarter, some – there could be a few things here and there but nothing really – our cost structure is actually quite a bit lower than it was last year as we've taken a lot of steps to reduce it. And as far as – yeah, you're right, we hedged about 70% of our requirements for G1 and G2 so we're exposed about 30% to the spot market. So depending on what price you're using for Q3 versus what you're – have in your model, that it would impact us by about 30% of our gas requirements.

Matthew Blair

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

Q

Great. Thanks for the color.

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

You're welcome.

Operator: Thank you. The next question is from [ph] Roland Roesch (00:37:05) from Crown Extra Investments. Please go ahead. Your line is now open.

Q

Hey. Good morning, John. How are you?

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Good morning. Good, thanks.

Q

Well, congratulations on another good quarter. I would like to ask a two-pronged question around liquidity and capital returns, also coming back to one of your comments previously around there is quite a bit of cash on your balance sheet. So, I round the updated numbers, I see that the company has paid down \$200 million in debt for this year, sit on a over \$750 million in cash. If I pro forma the shipping transaction, that's around \$900 million in cash, plus there's a \$900 million in lines of credits with the \$300 million in undrawn RCF and the \$600 million unutilized construction loan.

So that gets me to a total of \$1.8 billion of liquidity. And then you just guided for another Q3 in line so I assume we are looking at \$2 billion in cash and lines of credits by the end of September versus a total G3 that's only kicking in next year of \$800 million to \$900 million. So why do you and your board do not think the shareholders deserve a larger dividend or a clear share buyback program?

And I want to come back to one comment you made on your recent announcement on the call where – at what prices you would start, buy back the shares. Obviously, we're on year-to-date lows, so do you consider the current share price level as attractive to buy back shares? Thank you.

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Yeah, it's attractive to buy back shares at the current price level, I would agree with that. We stated pretty clearly our financial strategy around what we want to do with our balance sheet and returning cash to shareholders, that hasn't changed. So we want to maintain \$300 million in cash plus the additional whatever G3 spend is left on the balance sheet. And once we've achieved that, we will start to return more cash to shareholders flexibly, like we've described, and that include buybacks.

We reset the dividend and fixed dividend at \$0.125. And our plan hasn't changed, that we'll grow the company, and we, over the last 10 years, grown the company [ph] and doubled (00:39:28), spending about \$3 billion, and we've returned over \$2 billion to shareholders in the same period through dividends and buybacks. So our balanced approach is the same. Right now, we're having cash generation going towards the G3 project in addition to what's on our balance sheet. And once that is achieved, then we will look to return cash to shareholders. So nothing's really changed.

Q

Okay.

Operator: Thank you. The next question is from Cherilyn Radbourne from TD Securities. Please go ahead. Your line is now open.

Cherilyn Radbourne

Analyst, TD Securities, Inc.

Q

Thanks very much and good morning. In terms of the outlook for methanol supply, I was hoping you could give some perspective on what you think the current environment is like to contemplate a new methanol plant as far as being able to lock in a fixed cost with an E&C partner in light of inflationary pressure, and what sort of price deck financial institutions might be prepared to lend on.

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Yeah, it's a good question. Obviously, that's going to impact us as well post-G3 so it's something we look at all the time. We may have some other brownfield opportunities, but if we're assuming greenfield, there's two projects that have been recently completed there's public information around, and that's the Koch Methanol plant that's in the process of starting up and the OCI Natgasoline plant.

Both of them are around 1.7 million tonnes or 1.8 million tonnes, give or take, and they are well north of \$2 billion to complete based on public information that we saw. So if you use those numbers that's public, that's over \$1,100 a tonne. And assuming gas pricing in the \$3 to \$3.50 range and a double-digit return of around 10% to 11%, you would need \$400 methanol to get – or higher to get that return.

So we certainly like and we love \$400 methanol for 20 years to get a payback on a project like that, but we've seen quite a bit of volatility in the last 12 years in our commodity and I think that would – if I'm a bank looking to lend money to a potential project, with those kinds of returns and what [ph] you're doing (00:41:47) on methanol price, it seems in the hard to do category. But having said that, there's lots of – seems to be lots of money out there trying to find a home, so we'll see what happens. But those are the kind of the numbers, Cheril.

Cherilyn Radbourne

Analyst, TD Securities, Inc.

Q

And then second one is just could you speak to the company's confidence in the view that MTO demand for methanol will be stable over the coming five years?

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

A

Yeah. Well, I guess we can only look at what has happened in that industry and what's been going on in a high price and low price environment. So the industry started up four, five years ago. That was what we called the first wave which is just about being completed. Now there's a couple more plants that one is close to completion and one will probably get completed in the next couple of years. And that's what we call the first wave.

And as the first wave was being commissioned, there was a second wave. And certainly, with oil prices in the \$40 range and naphtha in the \$400 range, it made more sense to look to naphtha crackers than to empty old plants. So we never expected the second wave and we're not anticipating. So what we think will happen is what's there will run. We have 85% to 90% operating rates, and I think we can only go on to history.

When we had \$400-plus methanol pricing in 2018, they all ran in higher rates. When we had a low olefin cycle last year because of COVID, they ran at high rates and they continue to run at high rates. So it's something we watch very closely because it is a big demand driver for methanol. And like most things, it's hard to predict the future, but based on what we've seen today, we would expect that 85% to 90% operating rate.

Cherilyn Radbourne

Analyst, TD Securities, Inc.

Q

That's my cue. Thanks.

Operator: Thank you. The next question is from Chris Shaw from Monness Crespi. Please go ahead. Your line is now open.

Christopher Lawrence Shaw

Analyst, Monness, Crespi, Hardt & Co., Inc.

Good morning, John. How are you doing?

Q

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

Good morning. Good, Chris.

A

Christopher Lawrence Shaw

Analyst, Monness, Crespi, Hardt & Co., Inc.

If one were to take a really pessimistic view on, I guess, global gas availability going forward outside of, say, your Medicine Hat, Geismar, what – can you remind me what both the potential for moving any of your other plant, [ph] all of (00:44:15) the first two Geismar plants or – to another site? And like it I doesn't have to be I guess Geismar, specifically, but not only the potential but I guess the economics and, I mean, is that a possibility at all in any of those plants in the future?

Q

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

I would say very unlikely. When we looked at the kit that we have in the other locations, the way it was built, the way it's installed, pretty expensive to move. We had a unique opportunity. We had two twin plants in Chile and the way they were built, we could lift them up and move them, but I think that was unique to Chile 1 and – sorry, to Chile 2 and 3 which are now Geismar 1 and 2.

A

But in – we look at things all the time, but right now our focus is to get those plants running in – where they are. And we're not giving up any hope yet that we won't be able to achieve gas contracts to allow us to run all of our kit over time. So we've seen this in the history of our company. I mean, we didn't have any production in North America for the longest time and we're going to have \$4.5 million here pretty soon, \$4.7 million, I guess, with the debottlenecking. So, yeah, so we're – our focus is trying to get those plants running based on gas, they're – and not moving them at this time.

Christopher Lawrence Shaw

Analyst, Monness, Crespi, Hardt & Co., Inc.

Thanks. And then just a reminder, do you know – I can probably jot down the math but not off the top of my head, but the – your cost per tonne for Geismar 3 relative to what it'll be for the – when you – say, Geismar 2 when you move the – are they similar or is one lower?

Q

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

No, about the same. We've guided to a bit lower but not significantly.

A

Christopher Lawrence Shaw

Analyst, Monness, Crespi, Hardt & Co., Inc.

All right...

Q

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

And that's...

[indiscernible] (00:45:58)

A

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

..modeling it [ph] probably going to (00:45:59) Asia as I mentioned. Because it...

[indiscernible] (00:46:02)

A

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

...the gas efficiency on the Geismar 3 plant is much superior to Geismar 1 and 2.

A

Christopher Lawrence Shaw

Analyst, Monness, Crespi, Hardt & Co., Inc.

Yeah. Got it. Thanks a lot.

Q

Operator: Thank you. And the last question is from Steve Hansen from Raymond James. Please go ahead. Your line is now open.

Steve Hansen

Analyst, Raymond James Ltd.

Hey, John, just one quick follow-up, if I may. How do you feel about your human resources capabilities across the existing operating complex today? It strikes me that everywhere we look, we're hearing about strained labor resources, both skilled and unskilled. I'm not so focused on the G3 but just on your existing operating complex today. Are you well-positioned right now? Are you looking for people? How should we think about that and whether you're well-positioned going forward here?

Q

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

Yeah, one of the benefits that we've enjoyed in our company is a low turnover rate. I mean, if you compare our turnover rate on average to the industry, not just methanol but chemicals and other industry applications like that, we're very low. So we're – we – doesn't mean we don't have turnover, and retirements are becoming a bigger and bigger issue as – especially in the Western countries as we tend to the aging to retirement age.

A

So I don't have any concern today that we're at risk of not being able to run our plants efficiently because of labor, but it's something we talk about all the time. So things like diversity, inclusion are really important to our company, and to really expand our labor potential where we can look for new team members is really, really important. And each region's a little unique. In Trinidad, we have all kinds of labor today because of what's happened in – on that island. In Egypt, we're employer of choice, and certainly I'm not concerned in the short term, but it's something we think about all the time and we want to make sure that we're a great place to work. We pay good wages and we have people stay for a long, long time and we're not planning on changing that strategy and philosophy.

Steve Hansen

Analyst, Raymond James Ltd.



Okay, great. That's helpful. Thank you.

John Floren

President, Chief Executive Officer & Director, Methanex Corp.

Thanks, Steve. Okay. Well, thanks. We're very pleased to share our excellent financial results with you today. We continue to generate meaningful cash flow across a wide range of methanol prices. Our capital allocation priorities remain the same. We use the cash that we generate to maintain our business, pursue value-accretive growth opportunities, and continue our strong track record of returning excess cash to shareholders. Thank you for joining us today and we'll speak with you again in October, and 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.

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