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UAN - Q4 2019 CVR Partners LP Earnings Call

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CORPORATE PARTICIPANTS

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CONFERENCE CALL PARTICIPANTS

Adam L. Samuelson *Goldman Sachs Group Inc., Research Division - Equity Analyst*

PRESENTATION

Operator

Greetings and welcome to the CVR Partners, LP Fourth Quarter 2019 Earnings call. (Operator Instructions) As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, Jay Finks, Vice President of Finance and Treasurer. Thank you. You may begin.

Jay Finks - *CVR Energy, Inc. - VP of Finance & Treasurer*

Thank you, Michelle. Good morning, everyone. We appreciate your participation in today's call. With me today are Mark Pytosh, our Chief Executive Officer; Tracy Jackson, our Chief Financial Officer; and other members of management.

Prior to discussing our 2019 full year and fourth quarter results, let me remind you that this conference call may contain forward-looking statements as that term is defined under federal securities laws. For this purpose, any statements made during this call that are not statements of historical facts may be deemed to be forward-looking statements. Without limiting the foregoing, the words outlook, believes, anticipates, plans, expects and similar expressions are intended to identify forward-looking statements. You are cautioned that these statements may be affected by important factors set forth in our filings with the Securities and Exchange Commission and in our latest earnings release. As a result, actual operations or results may differ materially from the results discussed in the forward-looking statements. We undertake no obligation to publicly to update any forward-looking statements, whether as a result of new information, future events or otherwise, except to the extent required by law.

This call also includes various non-GAAP financial measures. The disclosures related to such non-GAAP measures, including reconciliation to the most directly comparable GAAP financial measures are included in our 2019 fourth quarter earnings release that we filed with the SEC yesterday after the close of the market.

With that said, I'll turn the call over to Mark Pytosh, our Chief Executive Officer. Mark?

Mark A. Pytosh - *CVR Partners, LP - CEO, President & Director of CVR GP LLC*

Thank you, Jay. Good morning, everyone, and thank you for joining us for today's call. Before I go through the highlights, I wanted to thank our employees for great environmental health and safety performance this year, as process safety events declined by 75% and environmental events declined by 64% in 2019 versus 2018.

The summarized financial highlights for the 2019 full year included: net sales of \$404 million, a net loss of \$35 million and EBITDA of \$107 million. Looking more specifically at the 2019 fourth quarter, we reported net sales of \$86 million, a net loss of \$25 million and EBITDA of \$11 million. There is no cash available for distribution this quarter.

During the fourth quarter of 2019, we completed the planned turnaround at East Dubuque in mid-October and finished the quarter with strong operating performance at both facilities. Following the completion of the turnaround at East Dubuque, we hit a new record for ammonia production at that facility in December.

At Coffeyville, the ammonia plant operated at 90% utilization for the quarter compared to 96% for the fourth quarter 2018. At East Dubuque, the ammonia plant operated at 88% utilization adjusted for the planned turnaround compared to 95% for the fourth quarter of 2018. Our combined operations produced approximately 180,000 gross tons of ammonia, 286,000 tons of UAN and 55,000 tons of ammonia available for sale in the fourth quarter 2019. This compares to production of 209,000 gross tons of ammonia, 357,000 tons of UAN and 59,000 tons of ammonia available for sale in the fourth quarter of 2018.

We sold a total of approximately 293,000 tons of UAN during the fourth quarter of 2019 at an average netback price of \$176 per ton, which was a 2% price decrease from the fourth quarter of 2018. In addition, we sold a total of approximately 62,000 tons of ammonia during the fourth quarter 2019 at an average netback price of \$324 per ton, which was consistent with the fourth quarter 2018 price.

The extreme wet conditions in the spring of 2019 caused the late planting season, which in turn led to a delayed grain harvest in the fall. Continued wet weather in the fall made the environment for nitrogen application less than optimal, which led to a weak price environment in the fourth quarter 2019, similar to what we saw in the fourth quarter 2018. However, our outlook for 2020 remains optimistic as we expect an increase in planted corn acreage, which I will discuss further in my closing remarks.

I will now turn the call over to Tracy to discuss our financial results.

Tracy D. Jackson - CVR Partners, LP - Executive VP & CFO of CVR GP LLC

Thank you, Mark. Turning to our results for the full year 2019, we reported net sales of \$404 million and operating income of \$27 million compared to net sales of \$351 million and operating income of \$6 million for the full year 2018. Net losses for the full year of 2019 were \$35 million or \$0.31 per common unit and EBITDA was \$107 million. This is compared to a net loss of \$50 million or \$0.44 per common unit and EBITDA of \$84 million for the full year 2018. The approximate 27% increase in EBITDA year-over-year was primarily due to the improved netback pricing of 20% and 15% for both ammonia and UAN, respectively, along with a 19% increase in ammonia sales volumes.

For the fourth quarter of 2019, we reported net sales for the period of \$86 million and an operating loss of \$9 million compared to net sales of \$98 million and operating income of \$8 million in the fourth quarter 2018. Net losses for the fourth quarter 2019 were \$25 million or \$0.22 per common unit and EBITDA was \$11 million. This compares to a net loss of \$1 million or \$0.01 per common unit and EBITDA of \$33 million for the fourth quarter 2018. The decrease in EBITDA was driven primarily by turnaround expenses incurred in the fourth quarter of 2019, along with a 20% reduction in UAN sales volumes and a 2% decline in UAN pricing as a result of the late fall harvest and challenging weather conditions in the quarter.

Direct operating expenses for the fourth quarter of 2019 increased to \$46 million from \$38 million in the prior year period. Excluding inventory impacts, direct operating expenses increased by approximately \$2 million year-over-year primarily related to turnaround expenses and higher personnel costs, partially offset by benefits from utility cost improvements.

During the fourth quarter 2019, we spent \$9 million on primarily maintenance capital. For the full year 2019, we spent approximately \$20 million, of which \$18 million was for maintenance capital at our 2 facilities. Total capital spending for the year came in at the low end of our expected range of \$20 million to \$25 million as a result of a shift in timing of certain capital projects into subsequent years. We currently estimate total capital spending for 2020 to be \$23 million to \$27 million, of which \$19 million to \$21 million is expected to be maintenance capital. This excludes turnaround spending, which we expect will be approximately \$8 million.

Looking at the balance sheet. As of December 31, we had approximately \$62 million of liquidity, which was comprised of \$37 million in cash, full availability under the ABL facility of \$50 million less \$25 million of cash included in our borrowing base. Within our cash balance of \$37 million, we had approximately \$9 million related to customer prepayments for the future delivery of product. Our long-term gross debt and finance lease obligations of \$647 million, including current portion, remains unchanged.

In assessing our cash available for distribution, we generated EBITDA of \$11 million for the quarter, had total cash needs of \$15 million for debt service, \$7 million for environmental and maintenance capital expenditures, and the Board of Directors of our general partner authorized a release of previously established cash reserves of \$7 million, leaving no cash available for distribution. We are a variable distribution MLP. We will review our previously established reserves, evaluate future anticipated cash needs and may reserve amounts for other future cash needs as determined by our general partner's Board.

As a result, our distributions, if any, will vary from quarter-to-quarter due to several factors, including, but not limited to, operating performance, fluctuations in the prices received for finished products, capital expenditures and cash reserves deemed necessary or appropriate by the Board of Directors of our general partner.

With that, I will turn the call back over to Mark.

Mark A. Pytosh - CVR Partners, LP - CEO, President & Director of CVR GP LLC

Thanks, Tracy. As I've mentioned on the past several calls, we are focused over the next 5 years on improving the reliability of our plants and debottlenecking in incremental ways to gain added production for low capital investment. Since coming out of the turnaround at East Dubuque in October, the plant has had record production levels of ammonia due to the work we did on the reformer. The Board has approved a re-expansion project at our Coffeyville plant, which is expected to be completed during the turnaround scheduled for the fall of this year. This project will focus on improved reliability and debottlenecking of our urea plant that should allow for improved utilization rates and higher UAN production.

There was a confluence of weather factors that impacted the transition period from fall to spring and weighed on our fourth quarter results. Grain harvest was delayed as a result of the late planting season due to extreme wet conditions in the spring of 2019. Wet weather in the fall then slowed the ammonia application in the Northern Plains and farmers were not able to apply the desired amounts of ammonia. Like last year, we expect a portion of the normal fall nitrogen demand to be shifted to the spring of 2020. The late harvest and poor fall ammonia application also slowed the timing of farmers' purchases of nitrogen fertilizer for spring application. Similar to last year, ammonia orders that were not fulfilled during the fourth quarter were shifted to our spring order book.

Additionally, in the UAN market, we are in the first planting season after the EU confirmed tariffs in October on UAN imported from Russia, Trinidad and the U.S. This has created a resetting of the trade flows with more UAN tons exported to or remaining in the U.S. This shifting of trade flows commenced while the market was contending with the excessive moisture that led to poor application conditions in the spring and fall of 2019.

While we expect the market to continue to have some near-term volatility, we expect the trade flows to normalize over time as they have with new capacity additions in the past. Offsetting some of the pricing issues has been lower natural gas cost. Natural gas prices were significantly lower in the fourth quarter of 2019 compared to 2018, and they have fallen further since the beginning of this year. East Dubuque benefits directly from lower natural gas costs of production and Coffeyville benefits through lower electricity cost. We consider our overall production cost to be competitive with the other domestic producers.

Looking to the spring, normal weather should allow inventory levels to become balanced after 3 consecutive application periods with poor weather. We expect corn planting to increase to 92 million to 95 million acres and with slower purchasing by customers this year in advance of planting, we expect to see strong in-season purchases of nitrogen fertilizer.

I want to reiterate that the partnership will continue to focus on maximizing free cash flow by safely operating our plants reliably and at high utilization rates, prudently managing our cost, being judicious with our capital, but selectively investing in reliability projects and incremental additions to production capacity and maximizing our marketing and logistics activities.

In closing, I would like to thank all of our employees for their contributions in 2019 to significantly improve our environmental health and safety metrics and safely completing the planned turnaround at East Dubuque.

With that, Michelle, we're ready to answer any questions.



QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Adam Samuelson with Goldman Sachs.

Adam L. Samuelson - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

Yes. So I guess, first, just on the market side. I mean you had a pretty sharp fall in UAN values from summer fill, and I'm just trying to think about how to -- you can characterize it, especially at NOLA how far it's fallen? How to think about kind of in the book of business in the first half of the year? How much was done? If any is carrying over from summer fill price levels versus kind of at the new lower levels? And does the changing in trade flows impact kind of your plant level realizations? Or should we be thinking about something approximating kind of the Midwest benchmark?

Mark A. Pytosh - *CVR Partners, LP - CEO, President & Director of CVR GP LLC*

Okay. There were several questions in that question. I'll try to take -- let's take it in sequence, I think, from the events. If you think about in past markets, Adam, we typically are trying to sell, I wouldn't call, perfectly ratably. But we typically sell on a regular basis. So we don't sell in peaks and valleys. And so we like what we did last year. Coming into this year, we had already sold a decent part of the first quarter tonnage back in the fourth quarter. That's typical and that's when customers are coming in, and that was after the fill. And there's -- prices have really fallen more at the -- since the beginning of the year as producers were trying to sell first quarter tonnage to clear inventory to manage and wait for spring. And so we had already sold a good chunk of our first quarter tonnage.

I think the NOLA -- let's talk about that. And so I think that the first quarter, we feel very comfortable with our position, and we're just waiting for spring at this point. And we've been very selective at participating when we sell tonnage. The NOLA price that's quoted a lot, which is for UAN in particular, is not a particularly liquid point in the market. And I would say it's kind of an extreme measure compared to, if you looked at the inland pricing in the Midwest or in the Northern Plains, it's -- the spread there has been much wider than historically what's posted in NOLA, and obviously, there's been some tonnage coming into NOLA. So I think that's been a little distorted in terms of what the pricing appears to be.

But clearly, the buyers were slower to purchase this year, as I mentioned in my comments, and so producers have been selling here in the first quarter to clear -- to keep our inventory levels comfortable to get to the spring. We're all waiting for the spring, including the buyers, to a degree, so I feel very good about our position. I feel good about the spring. I think there's pent-up demand in the spring for nitrogen because it didn't get on in the fall, and the buyers have been kind of slow to come in. I'm actually a little more concerned about the logistical parts. Whenever we have these events where people wait and then everybody wants tonnage at the same time, the logistical network in the United States isn't set up for just-in-time delivery, particularly either rail or barge.

And so -- and there's high water on the Mississippi. So between our rail system in the United States and the water in the Mississippi, the logistics aren't super easy. So long-winded answer, but I do expect conditions to get better here in the spring as demand starts to come in for application.

Adam L. Samuelson - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

That's a -- it's a lot of very helpful color. And then just a little bit of clarity on the urea debottlenecking. I mean is there any way to frame the capital, just any income -- meaningful incremental capital expenditure with the turnaround? And how much incremental kind of urea you'd actually be producing to improve your UAN output?

Mark A. Pytosh - CVR Partners, LP - CEO, President & Director of CVR GP LLC

Well, I'll start with the back end of that question. We're not ready to sort of post what we think the incremental production. But Tracy quoted our expectations for capital this year, which should be pretty -- it might be a few million higher than 2019. But we're trying to fit that urea project inside our kind of, what I call, our normal spending rate of \$20 million to \$25 million for capital. So it's not -- it's -- the turnaround is going to be steered towards that project as a bigger part of the turnaround, but we're not going to be spending really outside of our normal boundary of total capital, if that makes sense.

Adam L. Samuelson - Goldman Sachs Group Inc., Research Division - Equity Analyst

No. That's super helpful. I appreciate the color. I'll pass it on.

Operator

Thank you. We have reached the end of our question-and-answer session. I'd like to turn the call back over to management for any closing remarks.

Mark A. Pytosh - CVR Partners, LP - CEO, President & Director of CVR GP LLC

Again, I'd like to thank everybody for joining the call today and your interest in CVR Partners. And we look forward to talking to you next quarter for the first quarter results. Thank you.

Operator

Thank you. This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation, and have a wonderful day.

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