

03-Nov-2022

MPC Energy Solutions NV (MPCES.NO)

Q3 2022 Earnings Call

CORPORATE PARTICIPANTS

Martin Vogt

Chief Executive Officer, MPC Energy Solutions NV

Stefan Meichsner

Chief Financial Officer, MPC Energy Solutions NV

MANAGEMENT DISCUSSION SECTION

Unverified Participant

Good morning to all and welcome to the Q3 2022 Webcast of MDC Energy Solutions. My name is [indiscernible] and I have the pleasure of guiding you through the presentation and the Q&A session later on. This morning at 7 o'clock MPC Energy Solutions published its financial statements for the nine months ended September 30, 2022. We would therefore like to take the opportunity to walk you through some of the highlights of the financial statements and also share some insights into project updates over the last few weeks with you. After our presentation, we will as usual hold a Q&A session in which we would be happy to answer any questions you might have. You can send in your questions via the text function in the webcast at any time during the presentation, and we will answer them at the end. This webcast is being recorded and will be published later together with the transcripts. Before we get started, let me remind everyone that certain statements made on this call, including financial estimates and comments about our plans, expectations, beliefs or business prospects and other statements that are not historical in nature may constitute forward-looking statements under the securities law. We make these statements on the basis of our views and assumptions regarding future events and business performance at the time we make them. And we do not undertake any obligation to update these statements in the future.

And we do not undertake any obligation to update these statements in the future. Forward-looking statements are subject to a number of risks and uncertainties, and actual results may differ materially from the results expressed or implied in light of a variety of factors, including factors contained in our financial statements, filings, and other releases.

Okay. Let me now move on and introduce you to the management team of MPC Energy Solutions. I have with me Martin Vogt, the CEO; and Stefan Meichsner, the CFO of the company. Please go ahead, Martin and Stefan.

Martin Vogt

Chief Executive Officer, MPC Energy Solutions NV

Thank you, [indiscernible] (00:02:33). Good morning also to everyone from my side. I'm very excited to present today our Q3 results and go into some of the most recent development in our projects and also the last time that we have the opportunity to speak to this audience. This year, we also wanted to recap on MPC Energy Solutions as an organization.

And if you may move forward to the slide, the next one, please. So as you all know, we started last year only with a very small group of management colleagues and have grown the company to about 20 full-time employees

during the last 18 months and since the IPO. So the management and our colleagues from the supervisory board, as well as from the team in Amsterdam, Panama and Colombia, we took the time to develop a joint vision, mission and purpose statement.

We believe this is very critical for an organization that is culturally and geographically fully diversified, like MPC Energy Solutions, and really serves in the future as a focal point that helps to align everyone with the organization, ensuring everyone is working towards a single purpose and as an effective guide also for decision making. So you see here on this slide the results of our vision and mission, I think [indiscernible] very important for us of course its sustainability aspects in our business, first of all to preserve the risk – the resources also for future generations in the way how we conduct our business also to work with respect to the local communities that we are affecting heavily with our activities. And in the next step, what we will present also to the public shortly is the sustainable value strategy that we have developed based on our vision, mission and purpose statement. We have also adopted accordingly our environmental social management system so that all these management tools are fully aligned with these statements. Now focusing on the business model itself. And to recap for everyone – go to the next slide. Thank you. The comprehensive value chain that MPC energy solution is part of applying, I would really like to highlight here again from our perspective, one of the main key differentiators in our value chain also compared to our peers is really the true and sole focus on the needs of our clients. We are truly technology agnostic and try to implement a technical and commercial solution that meets the requirements of our clients when it comes to renewable energy penetration, affordability, reliability as well as source of – of energy. So I do believe it is a key differentiator to some of our peers. And of course, we remain a long-term partner throughout the project cycle from the development of the financing into the operations until these assets are reaching [indiscernible] (00:06:12) of lifetime.

Going into our market characteristics and why we have chosen once again to be active in Latin America and the Caribbean islands. And why we keep our focus on these core markets for the moment is really that we – that we find very attractive local conditions to invest. First of all, we have the very strong ambition of the governments that have all set binding goals and – and NDCs next week we'll receive COP 27 starting in Egypt. And we believe also from that perspective, there will be a new push in the region for a faster energy transition, especially for the small island development states, as well as for the remaining developing markets that we have exited.

So from that side and the policymakers and the regulators with the continuous support, when we approach with our projects, the private and public sector. Furthermore, we still see that there is a limited renewable energy base, meaning strong growth prospects for companies like us in the – in the markets. And the rationales will all remain the same. We have a high abundance of solar and wind resources. We have a very strong dependency on fossil fuels, still on – on diesel and HFO in some countries there was a shift towards natural gas massively in the last three to five years. However, as we experience at the moment in global energy crisis, the reference prices on Henry Hub tests materially increased and that have led to a moment also for the Government to recognize that only a true diversification away from fossil fuels can be the key to independence, considering the price movements for natural gas lately.

On the other side, we remain to see high local generation costs, given the outdated technology that is being active since 30 years, 40 years, and replacing this with state-of-the-art technology, renewable energy remains truly the cheapest – cheapest source of generation. And another benefit that we clearly see that is not listed here is that all of these markets are given its size are relatively high entry barriers that for us as an established player creates some level of protection, but also that the contracts that we are signing are in US dollars, meaning we have limited exposure to FX movements except for Colombia, where we do seem TPAs and local Colombian face off.

Moving over to our regional footprint. And I think we can say by now that MPC Energy Solutions at the broadest asset base across the region for us, diversification remains a key risk mitigator and our strategy. So there is a reason why we are targeting the entire region, despite in itself each of these markets being fragmented. In the niche markets of this marketing fragmented. And the niche markets, we do not want to assume any [indiscernible] when it comes to our off-take or in counterparty strategy and risks, as well as protection from regulation and policy changes. Therefore, we believe that our current strategy provides very attractive risk adjusted returns for our shareholders. And at the moment, we can clearly say that we are the only player with such a broad footprint across the region compared to many of the other European IPPs that are also active. Looking at the growth path. On the next slide, we wanted to show where we see the growth opportunities. We have highlighted here today in particular the solar growth because for the region, solar energy will be the key technology. 70% to 80% of the energy transition will be fueled by solar technology. Of course, [indiscernible] also played a role combined with other technologies such as biomass and geothermal, but by far the vast majority is being created through solar which you can also see already in our existing portfolio. So our growth for the next three years is to create a proprietary project development backlog of around 800 megawatts of ready-to-build assets. So assets of that are fully permitted reaching financial goals and are ready for construction that is doubling our current capacity of about 400 megawatt that we do have already in the region, focusing on four key areas we have, two – what we would consider the most developed markets, which are also OECD members that is Mexico and Colombia that are currently seeing major growth in – in renewables, but also the Central American region, as well as the Caribbean, Central America will look particular, will look at Panama, Guatemala and El Salvador and in the Caribbean, on the larger islands like the Dominican Republic, Jamaica, as well as the Eastern Caribbean islands that all have very ambitious plans to decarbonize their energy metrics. So we have shifted clearly our focus more towards own project development in the region. I think it's a – it's a very good moment to do so and compared to our this year focus that was primarily on the construction of the first series of assets that we have brought through the IPO and capitalized.

When we look at the current projects, please go to the next slide. Thank you. So when we look at the current project and this is really just to – to give once again a transparent overview of the projects that are under ownership and in the development backlog in the – in the moment where we see here a significant growth also in the – in the factory projects and backlog, we will also – we will also see more and selected partial and full farm zones of this project to lift the value that we have created through the early stage of own project development so that clearly also four us an attractive opportunity to capture early on the value in this project and to recycle some of the invested capital and convert such equity premium or promote into construction equity. So with that, we come from the future plan to the present situation, and that relates primarily to the construction of our ongoing projects. In the region, you see our portfolio of assets in El Salvador, Colombia, Puerto Rico and St. Kitts that are with 100 megawatts of currently under construction. Capital expenditures, fully secured and fully funded with debt and equity and these projects that are now nearing its completion. So if we go to the next slide we have, we wanted to give you also a bit of a visual impression where some of the projects are. I think our statements are very clear that the projects are on track to achieve now COD in early 2023. Overall, Santa Rosa and [indiscernible] has made significant progress with 88% of modular installation. We are very close to complete the construction with some transmission line and substation upgrades as the remaining activities that should be completed by the end of the year. You then see [indiscernible] the project in Colombia that we brought also into the in Colombia that we – that we brought also into the IPO from – from the legacy MPC Capital portfolio. We are here at 72%. We have single access tracker installations in Colombia and also there now after the top of the extended range in Colombia. We do see very good progress in the piling and modular installations locally from our subcontractor, EPC contractor supporting.

The projects that we have in a joint venture with – with [indiscernible] (00:16:23) the French IPP Planetarica follows with an overall progress of 65%. At the moment, it has a total capacity of around 26 megawatts peak. So

this will, in the time be completed after Santa Rosa and [indiscernible] (00:16:40). And last but not least, we have the – we have the – we have the CHP plant in Puerto Rico, where we have now confirmed that the remaining seven day test will start on November 7th. And after the successful completion, we will be able to deliver the power to our offtaker Noel Pharma.

And with that, I'm happy to hand over to my colleague Stefan, who will invite you through the remaining slides for today. Thank you.

Stefan Meichsner

Chief Financial Officer, MPC Energy Solutions NV

Thank you, Martin. To put the progress on construction that Martin just elaborated on into numbers. You can see how it will change the pace of our company as our capacity grows one operational effort in Mexico today to a proportionate value of 66 megawatts of installed capacity that means we factor in the states of the project owned by co-investors and 66 megawatt of installed capacity might not sound like much, but we're talking about 144 gigawatt hours of annual energy output for the full year for these assets, which is quite significant. And we should also not forget in what kind of environment and market these milestones were achieved. There was a lot of talk about COVID, about supply chain disruptions, about material price increases, about higher interest rate inflation, and they certainly left their mark. And these are very real world challenges that we had to navigate through. And yet we were able to take these projects from the development phase through construction to successful operation. And we did so while maintaining our recurring targets for the investment. So, I would say that from our view, our team here in the region and also here at home has done an absolutely excellent job. And we consider once these projects are online, this can be the proof of concept that we believe we needed to deliver to make sure that everybody understands what our strategy is, what it entails, and that we are successfully executing on. We would also like to share some data points that we previously have not presented, and this is a look at our current portfolio. So, we're speaking about the six project that might be shown on the slide before. And what we see here are in my view very substantial numbers. We see an average PPA lifetime over 50 years. These are PPAs that are majorly US dollar denominated during the IPO and in the months after we always elaborated that we will see exposure to what you could call software currencies like the COVID vessels, further we would see, the overwhelming majority of US dollar exposure. And our portfolio as of today is structured in exactly that way.

And looking at the average lifetime, looking at the different revenues we can expect from the portfolio, we also see that we contracted revenues under these PPAs from a 100% view are over \$310 million. So what we see here is a high predictability on cash flows that yield double-digit returns and this really also in a strong currency mix. And this really also underscores what Martin mentioned that MPC Energy Solutions seems to be a long-term partner in the region. And well, what we've done today really, really underlines that [indiscernible] (00:20:39).

Speaking about double-digit returns, we have deployed a significant portion of the funds we raised in the IPO, but we are also still in a comfortable position to have ample cash reserves to invest in new projects and to fund our development activities. Now, part of the reason why we haven't invested all of the funds since the IPO yet. It's not a lack of opportunity, further we remain very committed and strict with our investment criteria. And we are very much focused on creating shareholder value and we understand that creating shareholder value comes from investing in the right project to deliver the better rate that we've set for the individual – individual offtaker in regions and technologies. And we don't want to compromise on that. Neither the time nor the market environment to do that opportunity do exists.

and we are actually in the process of targeting an additional FID shortly for another project in the Caribbean. So, at the moment we don't see why we should compromise. We are executing on our strategy and we continue to deploy capital in the project that we believe will add shareholder value and are the right ones in line with our

strategy. We look at the financial performance of our project in the first nine months. There is one operational asset as we go at the moment. It's the Los Santos effort in Mexico, which we acquired in February of this year. And this project really continues to perform in line with our expectations. The plant generated 22.3 gigawatt hours and delivered that energy to the offtakers in February. This corresponds to a \$2.2 million revenues generated from the project at a stable 74% EBITDA margin. And in addition as we mentioned in our previous market update, we are conducting energy trading activities related to a PPA in Colombia and in Q3, which is the first period that we have to conduct these activities we managed to secure a very small profit from – from trading, but we did not see immediate impact, which is mainly caused by fairly low stock prices in the past period in Colombia, something that we expect to – to turn in the fourth quarter. But overall our projection on the overall energy trading outcome remains very positive that we will not incur a major loss from this, and we might and the details will come out with a big [indiscernible]. Following the progress that we've made we're happy to confirm the outlook that we previously shared of \$3.5 million from our project corresponding to \$2.2 billion EBITDA on project level. We also expect our group EBITDA on a consolidated basis to end up in the previously shared range. And as we expect, certain effects to help it come down from the numbers that we shared this morning. We are not very aggressive when it comes to, let's say, capitalizing – capitalizable expenses, for example, during the year, we assessed it very, very carefully. So what you might see in the interim is always a bit of a bigger P&L impact as what we will ultimately display for the end of the year. At least that is our expectation to date.

And before handing the call back to [indiscernible] (00:24:31) for the Q&A session, I would really like to highlight one thing. We are very actively seeking ways at the moment to recycling part of the capital that we invested, meaning that we want to attempt to return capital sooner to us other than just waiting for the operational performance of the fund. This can happen, for example, by financing currently unlevered projects and then returning the cash to the shareholders of the projects up in our co-investors, and also partial form downs of our development backlog and operation that is always possible. If we manage this and I think there is a good chance that we will, we would continue to bolster our free cash position even further, which would then of course help us to invest these additional funds into additional projects in the region that meet our investment criteria. And with that, I will hand the call back over to [indiscernible]. Thank you very much. And [indiscernible] (00:25:32) we're ready for any questions that might have come in. Thanks.

QUESTION AND ANSWER SECTION

Operator: Great.

Thanks a lot Martin and Stefan for the presentation. We will now continue with our Q&A session. We'll pause for a couple of seconds to give you some time to send your questions in the text function, if you've not done so yet. Okay, then we can get started. And we have received a question from [indiscernible] (00:26:05) and the question is what is your view on raising fresh money for the next great project, perhaps a convertible or perhaps from MPC Capital or are we foreseeing any problems in this difficult market to raise fresh money?

A

Yeah. Of course. This is the question that is frequently raised, I think, by – by the market. And most importantly, what Stefan just elaborated. The – the projects that we have currently under construction and that are nearing construction are fully funded with the capital available. And Stefan also indicated there will be a major capital fund flow back to the company through the envisaged refinancing of the unlevered assets that we have. So at the moment, we feel well-prepared for our next opportunities. And we see, of course, that the market and the capital market environment is currently fairly challenging. And we see all the major markets being down, so that is not necessarily the most attractive environment for a company like ours to raise new capital.

for a company unlike ours to raise the new capital. So, the management and the supervisory board will consider such activities once we are there and cross that bridge.

Q

The next question that came in is from Christopher [indiscernible] . And his question is in August, you mentioned that there were issues with the new CHP project. So, could you please explain the following briefly, considering there is only some additional equipment required to get the plant up and running? How come the lead time for receiving this equipment is more than twice a month? Is there a shortage of the equipment in question, which makes it impossible to obtain it sooner?

A

Yeah. Unfortunately, it is indeed a pity how disrupted the global supply chains are. The equipment value that we were talking about was around \$50,000 only which – which is of course very hard for us. However, we are relying on the global suppliers and indeed it takes 22 weeks to supply this equipment. What we've mentioned today however is that we have come to a resolution with Lima. Lima is the grid operator in Puerto Rico that will allow us to start with the testing already next Monday and working on – on a temporary solution. So, the equipment will indeed only arrive I assume around January, February. However, considering the power outages in Puerto Rico and the supply of – of energy to residential and industrial off takers.

[indiscernible] is taking a very practical approach. They understand the needs of their clients as well. So therefore, we came to a practical solution where we have a temporary equipment installed that needs the regulatory requirements from [ph] LUMA in the next few months, however, we will install the long term equipments as soon

as it arrives. So I think on that perspective, again, a practical view and our active approach allowed us to come to a solution in this environment.

Q

Okay. Christopher sent on a follow up question for this. With regards to the Neol CHP project, do you assume it's likely that MPC Energy Solutions will receive full financial compensation for the project delay, or is there uncertainty whether or not you are covered by the contractual agreements with the project partner?

A

Yeah. So there are two things to consider. First of all, there is the clock and the power purchase agreement that basically keeps the full term of the PPA active. So there is no – when not eating so to say into our PPA lifetime, so we have the full PPA starting with the what is start of production. And as in any EPC contract, there are of course clauses with regards to the liquidated damages that are applicable in case of project delays. And those are covering our losses and MPC energy solutions and the project by us will obviously make sure of these claims. And in this respect I also wanted to re-highlight which might not be clear to everyone, we have also positive impacts from recent developments in this project. The Inflation Reduction Act made the tax credits, the tax equity credits for the CHP plans tradeable. So, previously at MPC Energy Solutions and its project partner have no taxable base in the US. These tax credits were of no value and couldn't be consumed by us. Now, where they are tradable we believe that at face value of around 80% these can be monetized, which Stefan correct me if I'm wrong, but is around a value of around \$400,000 US dollars to the company that has only been recently made – being made available sort of thing.

A

I would like to add that in our previous outlook, we said that we expect this plant to become operational early next year. What we see now with Martin mentioning that the final testing is supposed to start next week and completed within a week. This present additional upside on let's say starting revenues, production delivery energy sooner which – which also I would consider [indiscernible] the previously very careful timeline early and that will be met in [indiscernible] .

Q

Let's move on to the next question and that came in from [indiscernible] . And this question is, will you hedge the Colombian peso FX exposure and then also an undertaking US dollar versus NOK.

A

The second question first, we don't hedge US dollar versus NOK because we don't have any exposure to Norwegian Kroner and our day-to-day operations in US dollars are functioning currently and we trade seriously in US dollar except for the Colombian peso. And in terms of securing forward rates for money flowing back to us from Colombia, yes we intend to hedge that provided hedging is not only possible at good terms, it depends on when money will flow back to us from the project from the various shareholder loans that we have or dividends

that we will see – we will certainly very actively look into securing X rate rather than waiting for – for an appreciation of the Colombian pesos, which at the moment we [indiscernible]

A

I would like to add that given our development activities in Colombia, it is an important consideration that we are re-employed in Colombian pesos in the Colombian market for our local expenditures, not just of – of team Banco, but also all our project development activities are being conducted in local contracts. So, this is – this is an additional, let's say indirect hedge of our activities and how we are managing our foreign currency exposures.

Q

The next question that came in is from Christopher Carson again. And this question is one of the potential focus areas for MPC Energy Solutions is wind power, which we are yet to see an investment in, but will you primarily be focusing on onshore wind or offshore wind?

A

I think that's a very easy answer for us at the moment, it will be onshore wind. The region is in very, very very early stages of The region is in very, very, very early states of accessing their offshore wind potential. There is clearly some but in the largest offshore players globally are not yet really active in the region for except for maybe some very initial assessments in Colombia. Offshore technology will certainly make its way also into the region in the next decade. But at the moment, if you look at our financial capacity, at our balance sheet, at the maturity of the technology in the region, it is nothing that that we – that we seek investments in for the foreseeable future.

A

Okay. I think we've covered the incoming question. So if there are no further questions, this will conclude the Q&A session and the webcast. Let me just remind you, of course, as usual, if there are any further questions that we haven't covered today or any further questions, you think after the webcast, feel free or that was a bit tough. That was actually another question that just came in. So let's just take maybe a minute to consider that question. Came in from [indiscernible] (00:36:38). And the question is, do you consider to repurchase some of your own shares at the current price to increase EPS?

A

No, not at the moment. While we may have the flexibility to do so, our focus is very much on investing money into projects that meet our investment criteria to build and grow our company. We think it would be sending the wrong signal, and we also believe that the intrinsic value of the company is of course much higher than the current share price, and that the good news that we share today is the proof of concept that we will continue to deliver should be enough to bring the course the stock price back to where it belongs, which is certainly significant above the current level.

A

Okay, great. Then I think we can now conclude the Q&A session as I just started to say, if there are any further questions that we haven't covered or anything else you would like to clarify, please feel free to send us your questions via email. Our contact details are on screen now and yeah, let's take the opportunity for joining us and have a great rest of the day. Thank you.

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