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MPC Energy Solutions NV (MPCES.NO)

Q1 2024 Earnings Call

CORPORATE PARTICIPANTS

Stefan Meichsner
Chief Financial Officer, MPC Energy Solutions NV

MANAGEMENT DISCUSSION SECTION

Unverified Participant

Good morning, everybody. I have the pleasure to welcome you to the MPC Energy Solutions Q1 2024 Results Presentation. Our first quarter results have been published this morning and are available on our website. We would like to take the opportunity to walk you through some of the highlights of the last quarter and also give you an outlook on the coming months. Now, if you have any questions during the presentation, please feel free to type them into the text box and we will answer them at the end. Just one remark, this webcast is being recorded and will be published later together with a transcript on our website.

Now, before we get started, let me just remind you of the forward-looking statements. So as usual, certain information and statements shared in this document, including financial estimates and comments about our plans, expectations, beliefs, our business prospects and other information and statements that are not historical in nature may constitute forward-looking statements under the securities laws. We make these statements on the basis of our views and assumptions regarding future events and business performance at the time we make them. We do not undertake any obligation to update these information and 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.

Let me now hand over to Stefan Meichsner who will guide you through the presentation. Stefan?

Stefan Meichsner
Chief Financial Officer, MPC Energy Solutions NV

Thank you [indiscernible] 00:01:44 and good morning to everyone joining here today. Before we get started, I like to give a quick review about our business and what we, at MPC Energy Solutions, are all about and then we will move on to review the first quarter results.

MPC Energy Solution is what MPC Energy Solution is what we call a full cycle independent power producer. We are exclusively focused on renewable energies and we develop projects from green field all the way through construction and then remain invested long term as an owner and operator of these projects.

The focus area that we have selected to roll out our business model is Central America and the Caribbean. That means we cover the area from Colombia all the way down – up to Mexico and into the Eastern Caribbean. We've been operating now for three years and we are listed on the Oslo Stock Exchange since January 2021.

Why do we pick Central America and the Caribbean as our rollout region Well, first of all, this is an area where the energy transition is as important as it is in Europe or North America or Asia for that matter. And governments are supporting the energy transition from fossil fuels or on diversified renewable bases into a green and clean setup that we are supporting.

Secondly, in the region, countries either have a very small renewable base or a very undiversified ones where some countries like Colombia heavily depend on hydro energy, which in periods of extreme drought like what we are facing today or this year becomes an issue. Therefore, diversifying that base towards solar photovoltaics, towards wind onshore is elemental for these countries and we are supporting that transition.

A lot of countries still depend heavily on fossil fuels. Most of the islands in the Caribbean for instance, and this leads to the fact that the generation cost and the electricity costs that people pay when they consume power are actually among the highest in the world. So we believe that we will find extremely positive market frameworks in these countries, a lot of demand for renewable energy and ultimately a lot of support and a lot of factors that play in our favor and that compensate us for the risks that we take when we invest in these regions.

Since we started operations, we have put five projects on the grid, combining for a total of around 80 megawatts. These projects are currently in operation and 2024 is actually the year that they are operating as a portfolio for the very first time. So, for the very first time, we will see a full year output from these projects.

In addition, in March of this year, we started constructing our largest project to date, the 65 megawatt peak power plant in Guatemala. The teams are now ready to mobilize to the site and start the onsite works and we expect this project to be completed and connected to the grid and to start delivering energy by the middle of next year. In addition, we have a fairly strong development backlog, just a lot of solidify our future growth. And these are projects mainly focused in Guatemala, in El Salvador and in Panama among some other countries, where we believe growth and frameworks will be most beneficial for us coming, in the coming years and help us meet our return requirements and other factors.

If you look at our portfolio today, the average lifetime of the bilateral power purchase agreements that we signed, meaning the contracted revenue that we have extends to around 15 years on average. And most of our portfolio is exposed purely to US dollars, meaning the currency risks that we are facing in our portfolio is relatively low. The currency risk that we have, if you want to call it that, is associated to the Colombian projects where we generate revenues in Colombian pesos. But of course, we also pay bills in Colombian pesos. So overall, this is only a risk if we try to repatriate funds from Colombia to our US dollar based operations.

What are we looking for in projects? I've elaborated on this before, but I think it's always important to remind everyone that our target equity IR is quite substantial at 15% or higher are quite substantial at 15% or higher. We are a greenfield developer that likes to stay invested long term, and we are focused on utility-scale projects, either solar PV, wind onshore, or a combination of both, even attached to a storage facility like a battery, which we become – think will become much more important down the road.

The projects that we have need to qualify for a, what we call, co-investment case, or they need the potential to be farmed down, meaning that once we develop a greenfield project to the ready-to-build stage, we will bring in co-investors and sell a minority stake in our companies or sell the project outright. We're currently working on a partnership in Guatemala for exactly that purpose, so that a co investor will come in and be a partner in the 65 megawatt projects that we're building.

And of course the offtaker is something that we look at very, very closely. We need bankable offtakers. We need creditworthy offtakers that we can enter long-term partnerships with into. And we spend a tremendous amount of time looking for offtakers that we believe long-term partnerships work with because, ultimately, once a project is operational, you have two main risks.

You have the risk that the fan is not working properly. That's the technology risk, and we can focus on that ourselves by making sure that it's maintained and operated properly, and that we use high-quality equipment and solid EPC contractors when we build the plant in the first place. And it's then the risk that the offtaker is not going to meet its obligations. That is, pay the bills to us. So these are the two main operating risks, and that's why we spend a lot of time looking for the right offtakers and managing that exposure to the extent that we can.

To sum up our core principles, we are looking for greenfield returns. We know that developing projects from scratch has a certain risk attached to it. But once that risk is mitigated by entering the construction stage, we have created tremendous amount of value and we want to make sure that we can take that value off the table in whole or in part very early on. So that means we want to combine a steady capacity buildup without compromising our returns and by making sure that we properly balance selling down projects and ready to build, but also building our portfolio. And of course, with our offices in Colombia and Panama, we have a very lean setup that is focused and well connected in the region, and I think having feet on the ground is really the core difference that we have compared to some other IPPs we try to work exclusively with partners in the region.

Taking a look at Q1, we have good news to report across the board. Energy output is up. Project revenue on a proportionate basis, meaning accounting for the economic share that we have in project, is also up significantly by 70% and we continue to see an increase in our project operating profit's EBITDA and the corresponding margins. This is basically what we said all along that once the portfolio is operational and once we have managed the restructuring at some of our projects that we will not only see significant increase in numbers across the board, but also we would see margin improvements and get closer to the target margins in our projects where we want to be, which is significantly above 75%.

In Q1, these margins are commonly a little bit lower because in the first quarter you have some expenses that cover the whole year like insurance premiums or other expenses that you need to account for in Q1. So while margins are a little bit lower in Q1 commonly, they are also significantly higher than they were a year ago, illustrating that the portfolio now that it's up and running actually has some nice scalability effects.

The largest contributions in our portfolio still come from our project in El Salvador and in Mexico. Together they account for a little over 60% of the total output of total revenue and total profits. And the current environment of high energy markets and of inflation is of course also benefiting us, some of the power purchase agreements that we have signed are tied to either price indices or they are related to in trade at a discount to the stock market. And in times where stock market prices are very high compared to previous years, relatively high. We will also benefit from that.

So overall, we're very happy with the results that we have achieved in the first quarter. It's a record quarter for us. We've never delivered numbers like this before and I'm very proud of what we've achieved. And I think this is a testament to the work that we put in to the business model that we are pursuing.

On the cost side, a factor or an area where we've been criticized in the past that we carried along, a long and fairly large overhead compared to the small portfolio that we have, we've also done our homework. We understand that we cannot scale as quickly as we originally anticipated in the current interest rate environment, even though the projects are there finding attractive capital and making sure that we meet our return requirements is a challenge. We can still scale up, but less quickly than before, and consequently we believe we have to rightsize the organization to reflect that and no longer be as large as it was when we had more ambitious growth targets.

And the Q1 really illustrates that the work that we put in to identify cost cutting measures and to implement them late last year are already bearing fruit. And in Q1, we came up more than 30% below the previous overhead cost level and that is a clear indication that we are on the right track. And at the moment, we don't see why we shouldn't be able to continue this cost cutting of around 30% year-on-year compared to 2023, for the entire year of 2024. And this, of course will positively impact the group level profits as well, which we see when we look at our consolidated financials that we published this morning. So I'm very, very happy to report that for the very first time in our young history, group level EBITDA on a consolidated level was positive, we recorded around $625,000 of EBITDA this morning when we published our report. And also our net income and therefore earnings per share were positive for the very first time.

What you see is that revenues on a consolidated basis, as I explained on the previous slides are up significantly, overhead costs are down, margins within the projects are up and this immediately translates because of the scalability of our business into group level profit. And we have no reason to believe that towards the end of the year this trend will continue and that we will even record a positive group EBIT by the end of 2024, which is ultimately the goal that we have.

Some other key financial parameters. The total asset base of our company was a little over $124 million at the end of the first quarter, mostly still equity finance, that is, we are significantly under lever compared to some of the peers that we see in our industry, which are commonly trading at 20% to 25% equity ratio. The reason here is that we build our portfolio in times where interest rates, interest rates increased significantly and we decided to just simply finance these projects with equity only and re-lever them at a later stage when interest rates come down.

So, we see some tremendous upside here in terms of repatriating cash from our projects once we bring up leverage and debt levels in our projects, and are able to return the money to our holding companies where we can then redeploy them into new growth opportunities. Our free cash position is also still very strong, $12 million at the end of Q1, with the only commitment that we're really seeing being 00:13:45 project. So we are in a very comfortable position at the moment to react flexibly to whatever opportunities might come our way. We are well established to fund our development backlog and of course continue to pay for our now significantly reduced overhead. And as I said, for the first time, earnings per share, just as an indicator for those looking at these kinds of parameters and performance indicators were $0.02 per share positive for the very first time and we will continue to deliver this during the year 2024.

With all these good news, the outlook for 2024 that we've shared before remains unchanged. We expect our energy output to increase by nearly 50% this year compared to last year, revenue to be up by more than 30% and project EBITDA to almost double to make sure that we finally see some margins that are more clearly reflecting the potential of the solar PV assets that we have at the overall portfolio. And now that we've contained trading losses in Colombia, which weighed us down last year as we previously reported and as we've completed the restructuring of our Mexican solar PV plant project margins that we will see down the road, the gross margins will be significantly higher and get to the level where we want them to be step by step. And of course, if you account for the reduced overhead target overall, we're looking at a very good 2024 now that our portfolio is operational for the very first time.

One more comment on the San Patricio project. As I elaborated, we started construction in March of this year. We expect the project to be completed in the next 12 to 15 months that connect to the grid. This is transformational for our company. It will double our capacity, it will double our energy output, and we will see revenues on a consolidated and proportional basis to go up by $8 million with a very, very high EBITDA contribution on more than 80% margin. And we do this without having to touch our overhead, without changing our personnel structure, without implementing any or incurring any additional costs.

This is simply the scalability effect that we see.

Naturally, once we bring in a partner, these numbers that will contribute to our own top and bottom line will be a little bit lower. But in return, we are able to secure development fee and to share the equity requirement for building the project. So this would be still a very strong win for us and a significant transformational event that we're looking at.

Why be exposed to us as a shareholder? I've said this before. I think our company exposes shareholders to being part of the energy transition of the renewable energy in a very high-growth region in Central America and the Caribbean. These are developing and emerging markets.

The energy transition is as important as it is elsewhere. But we believe we can secure significantly higher returns compared to other countries. Even though we are exposing ourselves to what some people might call country risk, we often see that this country risk is overstated. You can simply look at the energy market, at the power market, and you look at the respective offtakers that we sign deals with.

As a full-cycle IPP, we cover the entire value chain, from development through construction to operation. We're able to secure greenfield returns and to create value early on, and we are still able to meet the scalability requirement that we see to cover development costs, to cover our overhead costs, and with a strong local presence we have, I think this really sets us apart from some other competitors that are active in the region.

We already have an existing asset base now with long-term cash flows, average PPA lifetimes of 15, yeah, 15 years and strongly US dollar-exposed. The cash flows are predictable. The high margins will come in now, and our target equity IRR, also make sure that future projects that we invest in meets our high-return requirements.

And of course our development backlog of more than 300 megawatts means we can solidify the growth. We have plenty of potential going forward, and bit by bit, we will exploit that potential and become a much larger IPP and an IPP that is really delivering long-term positive cash flows for its shareholders. We have created value over the past three years, we will continue to create value and I think Q1 of 2024 is proof of that and it demonstrates that the hard work that we put in is now paying off and delivering solid financial results. And we will only see those improved in the coming quarters, in the coming years.

And with that, I thank you for your attention. This concludes my prepared remarks, and I hand the call back to [indiscernible] 00:18:15 for the Q&A session. Thank you all for joining this morning.

QUESTION AND ANSWER SECTION

A

Okay. Thank you very much, Stefan. Now, as I said, we will start a quick Q&A session. And the first question that came in from Yan Martinek this morning is [indiscernible] 00:18:37 Bank wrote today that MPC Energy Solutions is too cheap to ignore. What investor activities are you planning to narrow the discount?

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The activities that we can have most control over is by delivering solid results, by making sure that the portfolio performs at it's supposed to perform and that people see the true value not only in the operating portfolio but also in the development backlog. For example, by bringing in a partner for Guatemala to show what other investors are willing to pay for a ready-to-build project or project that is under construction.

If your question refers to perhaps share purchase repurchase programs or other kinds of measures, these are currently not planned. If we would go down that road, we would have to ask the general meeting for approval anyway. So the public would know once we start discussions along that way. But I also think with the low liquidity in the stock, which has been an issue, that taking of more shares off the market by a share repurchase program is really not supportive. What we see is we deliver solid results. Investors will see the value embedded And as [indiscernible] 00:19:42 said, we are too cheap to ignore. I certainly do agree and I'm sure those investors will also see this and will more and more enter the stock and thereby increase liquidity in the stock and drive up the price much closer to the value where it should be because the intrinsic value of our portfolio and the structure that we've built is clearly much, much higher in that.

A

Okay. Thanks, Stefan. The next question that comes in is please elaborate on the reasons behind the tax effect in Q1.

Stefan Meichsner
Chief Financial Officer, MPC Energy Solutions NV

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Yeah. So we have deferred tax assets and liabilities on our balance sheet that we estimate at a regular basis, whether we use them or not use them. And here, liabilities were released and consequently had a tax impact. This was more, let's say, a correction of the year end 2023 results than any particular impact that we had in Q1. It was just something that we do on a continuous basis together with tax advisors where we make sure that our tax assets and deferred liabilities are correctly reflected, and we made a correction in Q1 and that drove up the tax result in this case. As I said, it's not operational. I think if you want to really see the operational performance and the operating profit, it's the best indicator as of right now.

A

All right. And do you also plan to partially sell existing projects in line with the co-investor strategy or are you already working on adjusting the financing structure of existing projects towards the industry's target leverage ratio of 80 to 20?

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Yes to both. We are certainly open to look at partially farming down some of the existing assets as well or fully selling them down. Of course, we have some really prime assets in our portfolio. We're selling them at the current interest rate environment. It might not yield the valuation that we believe they have but we believe we could still secure a significant uptake compared to the still secure a significant uptick compared to the money that we have invested.

So these discussions about even selling part of the operating portfolio are solely – certainly on the table. We always need to account for the fact that the less we own in our operating portfolio, the less cash flow we can actually repatriate. And this – the portfolio needs to help us cover our ongoing spending. That, at least, is the idea. So we may get a lot of cash up front, but we still want to make sure that the portfolio is big enough to cover our ongoing expenses.

And in terms of – so in terms of selling this down, that's clearly a yes. When it comes to financing some of our unlevered project, of course, we keep our eyes open. We are in constant discussion with financial institutions in the region.

Interest rates, however, still remain high, in some cases tick even higher. So, in Colombia, where this is a predominant reality that we still need to lever one of our projects, it's been very challenging, and there is no immediate pressure to do so. We just need for the market to turn for the debt market to make sure that we can secure attractive rates that do not harm our current project returns.

And as long as the projects are up and running, they are generating positive cash flows, which we benefit from. So this is just an upside that we will exploit the moment that we can. Right now, it's not the moment, but we keep vigilant, we remain vigilant, and we are in continued discussions with banks in the region.

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Okay. Thanks. A follow-on question for this, do you plan to develop all the projects in the backlog if they make economical sense, or would you also sell fully developed projects?

Stefan Meichsner
Chief Financial Officer, MPC Energy Solutions NV

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Once a project hits the ready-to-build stage, that's, of course, the latest that we will ask ourselves, do we want this project to be part of our operating portfolio because it meets our return requirements, because we have the cash to build it, etcetera, or whether we want to farm it down entirely?

So the goal is clearly to develop the development backlog as long as these projects are promising that make economic sense why wouldn't we? If they are about to meet our target returns, why wouldn't we? And if we spend money on a project it's really an exit point, when the project starts, starts construction. We sell it down entirely. We are certainly securing a multiple on our own invested money. So, that's a positive value creation factor. And if we decide to sell invested, we get part of the upside that we created during valuation, during development. But we can also stay invested and benefit from the long term cash flows and high returns.

So, I think overall our focus is to realize the backlog to the extent that we can always with an eye on spending appropriately and making sure that we prioritize the most promising projects. But when we say that we have a development backlog of 300 megawatt, we are not overexaggerating this, we're just showing you the projects that we believe actually have a high probability of being realized. Otherwise, we would have to put up a number that's much bigger, but much less certain. So, you can rest assured that we will focus on that development backlog in its entirety. But of course, we are prioritizing certain, certain projects, especially in Guatemala.

Q

Sure. Now, another question that's perhaps a slight overlaps between some of the questions here. Is there any progress on the potential farm down on the existing portfolio?

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As I've said before, we are in discussions, we are considering our top priority right now is to build Guatemala. And if there is an appropriate co-investor that wants to enter during the construction phase at terms that we find acceptable, we will make that work. And otherwise, there's no particular progress in our existing portfolio. We're focusing on Guatemala, and we're also actively trying to sell our Colombian development backlog because Colombia is no longer core country for us when it comes to future projects.

projects. And here we are actually in final discussions with potential buyers. So we hope that we can report something on that.

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All right. Now, the last question I can see for now is what is the status of the projects that were exited last year in Saint Kitts and Puerto Rico? Were the funds recovered?

Stefan Meichsner
Chief Financial Officer, MPC Energy Solutions NV

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Yes, the funds for the Saint Kitts project that we – were recovered already in November last year. And the funds from the Puerto Rico Project, which is around $2.4 million, we expect to be returned later this month.

We've been in discussions with our partner who are in the final stages of selling these projects themselves. This is the step that needs to happen before they can repay us, and we've extended the payment deadline based on the good progress that we're seeing in the process. But we should be able to secure these funds in Q2, I believe end of May, latest early June.

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Great. All right. The last question here now is what's the premium to NAV you could sell the projects for?

Stefan Meichsner
Chief Financial Officer, MPC Energy Solutions NV

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I'm not sure I fully understand what exactly you're referring to. But let me say this. The money that we invested in all of these projects, if we were to sell down the entire assets at the current fair market value, I'm sure that we could sell them at around 15% to 20% higher than what we've invested, based on our internal valuations and also based on what we've seen in the market.

So I think the minimum that you can account for is what the projects are worth in our books. I personally believe that we would secure a premium to that. But in terms of NAV or NAV per share, I would actually have to do the math. But you can rest assured that the money that we invested would be returned and then some because that's ultimately why we make these investments in the first place.

Unverified Participant

Excellent. Thanks a lot, Stefan. I think this covers the Q&A session this morning. Now of course, everybody, if there are further questions that we haven't covered today, please feel free to send them to us via email at ir.mpc-energy solutions.com and then, of course, we will answer your questions after this call. All right, then we would like to thank everybody for joining us this morning and we wish you a great rest of the day. Thanks a lot.