Final Transcript

Q2 2021 Ramaco Resources, Inc. Earnings Call

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Corporate Participants

Randall Atkins *Ramaco Resources, Inc. – Founder, Chief Executive Officer, Executive Chairman, and Director*

Chris Blanchard *Ramaco Resources, Inc. – Chief Operations Officer*

Jeremy Sussman *Ramaco Resources, Inc. – Chief Financial Officer*

Conference Call Participants

Nathan Martin *Benchmark Company — Analyst*

Lucas Pipes *B. Riley — Analyst*

Presentation

Operator

Good day, and thank you for standing by. Welcome to the Ramaco Resources, Incorporated Second Quarter 2021 Earnings Conference Call.

[Operator instructions]

I would now like to hand the conference over to your speaker today, Mr. Jeremy Sussman, Chief Financial Officer. Please go ahead.

Jeremy R. Sussman — Chief Financial Officer

Thank you. On behalf of Ramaco Resources, I'd like to welcome all of you to our second quarter 2021 earnings conference call. With me this morning is Randy Atkins, our Chairman and CEO; and Chris Blanchard, our COO. Before we start, I'd like to share our normal cautionary statement.

Certain items discussed on today's call constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements represent Ramaco's expectations concerning future events. These statements are subject to risks, uncertainties and other factors, many of which are outside of Ramaco's control, which could cause actual results to differ materially from the results discussed in the forward-looking statements. Any forward-looking statements speak only as of the date on which it is made, and except as required by law, Ramaco does not undertake any obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Lastly, I'd encourage everyone on this call to go on to our website, ramacoresources.com, and download today's investor presentation under the events calendar.

With that said, let me introduce our Chairman and CEO, Randy Atkins.

Randall W. Atkins — Founder, Executive Chairman, and Director

Thanks, Jeremy. As always, I want to thank everyone for joining us today to discuss our second quarter results.

There is a line in an old song by Paul Simon, which says, when something goes right, it's apt to confuse me. And in the 3 months since our last call, we have gone through a pleasant series of things going right. I'd like to provide a few highlights.

First, we have now printed two very strong quarter to a row, driven by some terrific cost metrics and an improving overall met coal market. We concluded our first half with $30 million of EBITDA, which is frankly higher than we had internally budgeted for the entire year back in last December. The balance of 2021 seems on track for more strength and hopefully, a record performance.

Our second quarter production of 550,000 tons at our Elk Creek complex was also a record. The first half production of almost 1.1 million tons puts us on track to perhaps exceed even nameplate capacity at Elk Creek of 2.1 million tons, and that's even allowing for Q3 and Q4 vacations.

Sales have certainly been strong. The U.S. low-vol benchmark pricing has rather dramatically increased by over $50 since Q1. We have continued to see the general world economy improve. Steel companies, both domestically and abroad, are enjoying record pricing and the highest capacity utilization since 2008.

In the second quarter, we sold almost 700,000 tons, making it a quarterly record by almost 30%. This puts us at about 1.1 million tons sold through the first half, which is about 40% ahead of last year. At Elk Creek, we have held first half costs at $61 a ton, and for all our operations at $65 a ton. As a result of these outstanding operational and marketing results, for the second time this year we are again increasing guidance on production and sales, and reducing guidance on cost and CapEx, both as is set forth in our release. Our margins on our most recent sales are now running in excess of $70 a ton. We still have over 400,000 tons of dry powder remaining to place in the second half of the year, hopefully with these same strong margins or above.

As we feel, the met markets will still have more room to run. Iron ore and copper made their moves early in the cycle. We think met coal is now playing catch up and may indeed turn out to have longer legs. This is especially given the unique supply constraints in the coal sector from lack of capital. So bottom line, if the met markets continue with their current strength, which we expect, then we anticipate having our strongest year of free cash flow.

As we have said repeatedly, we try to manage for cash and, of course, for liquidity. Indeed, as you know, we have one of the cleanest balance sheets and liability profiles in our industry as well as a very strong liquidity position. After the end of the second quarter, we took some additional steps to improve that liquidity, by floating an unsecured bond offering, where we raised almost $35 million. We are proud that this was the first unsecured debt deal in the coal space in over 4 years, and we'd like to give a tip of the cap to all of our underwriters. This additional liquidity gives us some optionality to explore ideas to add near-term production, either organically or through outside development projects.

As I said, we see the met markets as having some legs. We think you may see a strong multiyear market, and we would like to be able to take advantage of that with some additional near-term low-cost production. Having said that, we intend to exercise a good deal of discipline in how we approach looking at both the market and any new production opportunities.

Our industry, unfortunately, has a long reputation of when the market shows in strength, we throw money at indiscriminately adding more tons even when that might not be particularly prudent. We intend not to do that at Ramaco. Further, I think the capital markets will keep too much production exuberance in check this cycle. We always will try to keep liabilities, our balance sheet, and liquidity in the forefront as we analyze any options, and we hope to be able to discuss some ideas further with you over the coming months.

I also want to mention two matters which occurred post-quarter end. While they were both not entirely unexpected, they do add a sense of additional positive momentum as we continue to build out the year. First, we won a very decisive $33 million plus costs jury victory in litigation against Chubb Insurance. This grew from Chubb's denial of coverage for damages stemming from the collapse of a coal storage silo at Elk Creek in late 2018. Although court decisions are always subject to possible appeal, we feel very confident in our position. We look forward to having this decision finalized.

Additionally, late last week, we heard from the SBA that our Paycheck Protection Program loan of $8.4 million, which we secured last year, had been formally forgiven. Although we had treated the loan in this manner since last year, it is comforting to also have this finalized as well.

To close, I want to touch briefly on matters near and dear to our shareholders, of which Ramaco's management team is certainly in that camp. We have seen our stock rise by 200% over the last 12 months and by about 130% year-to-date. This is certainly very gratifying, and we hope for continued strength in price over the coming months. But also, as we grow and begin to reach or are close to our production goals, we will begin later this year to explore with our Board what may become our dividend policy.

A growth company such as Ramaco always has a rather tricky balancing act. We need to fund growth in production, and we also need to balance that growth against making sure we have enough sustainable free cash flow to fund a reliable and growing dividend. As a company, we hope we are at a point later this year to explore this, again, not in the not-too-distant future.

Now before I turn the floor over to Jeremy and Chris to delve into finances and operations in more detail, I would just like to reiterate how proud I am to our whole Ramaco family on what has been a very strong first half that's been produced. With some continued operational execution and a bit of wind in our sails from the market, I hope we will continue, as that song goes, to have some things go right for the balance of what I hope will be our strongest year.

And with that, I'd like to now turn the floor back to Jeremy to discuss our financial results.

Jeremy R. Sussman — Chief Financial Officer

Thank you, Randy. I'll start by going over our second quarter 2021 financial highlights. We had another stellar quarter, both operationally and financially. Second quarter 2021 EPS of $0.23 was up more than 250% from a year ago, while second quarter adjusted EBITDA of $18.1 million was up 67% from a year ago. This was the second-best overall quarter of adjusted EBITDA in our history, with only Q2 of 2019 beating these results, when domestic met coal contracts were 30% higher than in 2021. The first half of 2021 adjusted EBITDA was $30 million, which was materially higher than our adjusted EBITDA for all of 2020.

Turning to our forward outlook, for the second straight quarter we are increasing our 2021 production and sales guidance, while decreasing our 2021 cost and capital expenditure guidance. We now anticipate overall 2021 production of 2.2 million to 2.4 million tons, up from 2.1 million tons to 2.4 million tons previously and compared to 1.7 million tons in 2020. We have increased 2021 sales guidance by a like amount.

We now anticipate 2021 cash costs of $61 to $65 per ton at our Elk Creek complex, down from $61 to $66 per ton previously, and down from $70 per ton in 2020. We now expect total 2021 capital expenditures of $23 - $26 million, down from $25 - $28 million previously. We continue to anticipate paying minimal cash taxes for the foreseeable future.

In terms of what we are seeing in the market, metallurgical coal pricing has continued to improve throughout 2021 as both the U.S. and global economies have benefited from massive global fiscal stimulus packages aimed at consumption and infrastructure. We expect these positive conditions in the steel and met coal markets to continue to provide strong tailwinds for Ramaco.

On the demand side, U.S. low-vol met coal price indices have more than doubled from their COVID-19 induced lows. Domestic hot-rolled coil steel prices are at record levels above $1,850 per ton. U.S. steel capacity utilization recently hit 85% for the first time since 2008. At the same time, the supply of high-quality, low-sulfur met coal that we produce remains scarce. We see nothing on the horizon to change our view that the met coal supply response will continue to be muted for a variety of factors. This positive supply demand market positioning is occurring as we head into negotiations for 2022 annual contracts with domestic steel mills.

Now, moving on to our balance sheet, I am pleased to note that we have shifted from having a small net debt position previously, to a net cash position of $6 million as of June 30. We believe we are the only U.S. publicly traded coal company to be in a net cash position. We ended the quarter with a record of almost $50 million of liquidity. After quarter end, we completed a $34.5 million, 9% senior unsecured note offering.

Looking ahead, both Berwind and Big Creek are on time and on budget, with Big Creek recently having uncovered coal in its first work area. We continue to expect to be producing at a 5 million ton per annum run rate by mid-2022. Simply stated, we are very excited about what the future holds for Ramaco. With that said, I would now like to turn the call over to our Chief Operating Officer, Chris Blanchard. Chris?

Chris Blanchard —Chief Operating Officer

Thanks, Jeremy. Before turning to the update on operational issues, I did want to briefly thank the entire in-house team and outside counsel who worked with Ramaco throughout the Chubb litigation. This was a long process and a complex and technical case. We thank the court for their attention, and of course, the jury for their time and care in rendering what we believe was a wise and fair decision.

Switching back to our operations, safety and compliance remain our primary focus. Our safety statistics for the first half of 2021 continue to track ahead of our performance for the same period in 2020. This is despite the fact that we are now growing our workforce and running our existing operations at near capacity as opposed to the throttle back production we experienced in the early months of the pandemic last year. We now have just under 400 employees and hope to grow by year-end to near 450. Similarly, on the environmental side, we are happy to report that water quality compliance within Ramaco has reached 99.9% for the first half of the year.

All that said, we have seen COVID-19 related impacts to our workforce move up slightly at the end of the second quarter and continued into July, in line with increased positivity rates throughout the country. We have kept all of our preventative measures in place across our operations and plan to do so until the pandemic is clearly behind us. We are also tracking and monitoring the increased stress in the local labor market on finding experienced coal miners.

While we have been able to successfully grow our workforce in the second quarter to accommodate the Big Creek start-up and fill vacancies at our existing Elk Creek operations, we have started to see turnover rates modestly increasing as well. To date, we have not experienced any adverse impact in our productivity rates at our operations, but continue to monitor the situation closely.

Turning now to the existing operations at Elk Creek. We ended the second quarter of 2021 with all of our Elk Creek mines operating in areas where we anticipate that productivity should continue at approximately the same levels for the third quarter and into the fourth quarter. I would remind everyone on the call that the third quarter does contain one of our traditional vacation weeks for the mines, although the preparation plants continue to operate throughout.

While we did see a modest increase in mine cash costs in the second quarter, this was only to our anticipated levels, and of course, included the welcome increase in cash costs due to higher realization for our spot and our index-based coal sales. We have seen modest raw material cost increases from our suppliers and anticipate these to continue as long as the commodity prices remain strong. However, we believe that the projected cash cost ranges that we have provided will cover these inflationary pressures.

Moving to our new operations, as both Randy and Jeremy noted, these projects are moving forward at full speed. Our Big Creek surface mine worked through the majority of the second quarter on pre-mining construction and sediment control. As Jeremy mentioned, we did uncap our first coal in July, and we have moved the mine into producing status, although only one ship per day currently as we start August. We anticipate having the surface mine fully staffed and operating two shifts per day in September.

Our high-vol mining system at Big Creek should begin operation at the end of the quarter or very early in October, bringing this mine to its anticipated full run rate of approximately 200,000 clean tons, clean annual tons by the end of this year. We will process the first coal from this mine in the coming days and look forward to first shipments potentially in September.

At our Berwind mine, the slope project continues and excavation of the 3 slope tunnels is approximately 2/3 complete. At our current construction rates, we anticipate we will reach the Pocahontas #4 Seam in the final days of next month or early in October. Equipment and infrastructure will be moved in, and we expect to begin the production ramp at Berwind at that time. Assuming the fourth quarter of 2021 start-up in the Berwind P4 mine, we expect to have this mine fully operational as currently budgeted and producing at up to a 750,000 annual clean ton pace by the end of the second quarter of 2022. At that point, the combined Ramaco run rate from Elk Creek, Big Creek and Berwind should exceed the 3 million annual clean ton production rate, which we have previously discussed.

It is indeed a promising time in the metallurgical coal markets, and it is an exciting time for Ramaco. With that, this concludes management's prepared remarks. And I would now like to return the call to the operator for the Q&A portion of the call. Operator?

Questions and Answers

Operator

[Operator instructions]

Your first question comes from the line of Lucas Pipes from B. Riley Securities.

Lucas Pipes — Analyst, B.Riley

Thank you very much, and good morning everyone, and congratulations on a really strong first half.

Jeremy R. Sussman — Chief Financial Officer

Thanks Lucas.

Lucas Pipes — Analyst, B.Riley

My first question is on the growth projects and I wondered if you could remind us, in terms of the quality of the additional coal, roughly what you'd be thinking about in terms of production costs? And then the commercial strategy? Should we anticipate test shipments for customers or are you establishing the market sufficiently with Elk that you'll delay in kind of, with no kind of test shipments ahead of time? Thank you very much for your perspective on that.

Randall W. Atkins — Founder, Executive Chairman, and Director

So Lucas, your question relates to our current production?

Lucas Pipes — Analyst, B.Riley

No, on the growth projects.

Randall W. Atkins — Founder, Executive Chairman, and Director

The growth projects. Chris, you want to talk about Big Creek and…

Chris Blanchard —Chief Operating Officer

So Lucas, start with Big Creek. It's the 200,000 or so annual clean tons, and that's a mid-vol project or a mid-vol product primarily. We expect costs to be in the upper 50s in that range. Then turning to Berwind, that's more of an established product for us, say, low-sulfur, low-ash, low/mid-vol that we expect costs, once it's at full run rate, to be in the low $70 range.

Jeremy R. Sussman — Chief Financial Officer

And Lucas, it's Jeremy here, so in terms of the commercial strategy, Chris said, Berwind, it's an established low-vol in the market. So needless to say, we've had more inquiries than tons on the ground that we could sell. So I don't think, certainly, that's not going to be a challenge. Obviously, we'll be ramping up, so you will want to get test shipments in here and there, but needless to say, low-vol is in very tight supply and while we don't have an established mid-vol, obviously, Big Creek will be the first of that product. Clearly, that's also a type of coal that's in short supply. So we've been receiving in-bounds on that. Obviously, having uncovered first coal is a good first step. So I think we'll start to get samples in the hands of customers shortly and needless to say, we want to get these mines up and running as quick as possible.

Randall W. Atkins — Founder, Executive Chairman, and Director

And Lucas, one other thing, just in terms of strategy. So I think this is — as we look out at our overall portfolio, we started like with a pretty heavy sort of high-vol B component, and we're now moving, so probably by next year, certainly into 2023, we're going to be probably 2/3 in terms of low-vol A's and mid-vol. I think that's probably the direction we will start to look as we examine some of our production options.

Lucas Pipes — Analyst, B.Riley

Very helpful. Thank you very much for all that detail. And then, Randy, in your prepared remarks, you mentioned capital returns and certainly very exciting discussion to be turning to that topic in the coal space, and wondered if you could maybe elaborate on what you're looking at today, what sort of metrics, either from the industry or from your balance sheet? What would influence your decision on the capital return question?

Randall W. Atkins — Founder, Executive Chairman, and Director

I don't want to get too far over my skis because, as I said, we're going to talk about this with the board later on as we progress through the year. We're in a very good position right now. We've got record liquidity. We hope to end the year even in a stronger position than we sit right now. There are a few things that are still obviously out there in the space that need to be nailed down. We have to understand how the 2022 business is going to look from a domestic standpoint. We have to get some visibility really on the market, a little bit further into the second half. And we've got some ideas, obviously, to increase production that we're just now beginning to explore both organically, we've got a couple of projects in our pipeline, and externally, we've got a couple of projects that we're looking at as well.

So I think what I wanted to telegraph is that we are not unmindful that a dividend would be something that is very high in our priority, assuming we're able to balance the requirements of getting our growth profile to a level of production that we feel comfortable we can make sort of a sustained generation of free cash flow that would support a decent dividend and a sustainable dividend. So that's probably not nailing it down with the specificity that you'd like, but again, I don't think we're in a position as we sit here just over the lip of the second quarter to really nail that down for the year, but we will be discussing it later as the year evolves.

Lucas Pipes — Analyst, B.Riley
Randy, this is super helpful. Really appreciate all the detail and continued best of luck.

Randall W. Atkins — Founder, Executive Chairman, and Director

Thanks, Lucas. And thanks to B. Riley for the placement efforts that they did in helping us underwrite the baby bonds.

Lucas Pipes — Analyst, B.Riley

That's very much appreciated, thank you.

Operator

[Operator instructions]

Your next question comes from the line of Nathan Martin from The Benchmark Company.

Nathan Martin — Analyst, The Benchmark Company

Hey good morning guys, and congratulations on the performance. Maybe I'll start with pricing. It looks like you guys have committed about 0.5 million tons of export sales now, at a price of $98. I think that was versus about 200,000 tons at $89 at end of 1Q. If I do that math, you come up at an incremental pricing around $105, but obviously, that can include some tons you guys have already shipped. I think Randy, you made the comment that what you're seeing out there right now is maybe over a margin of close to $70 or better. So I was just hoping you could talk maybe a little bit more about the export pricing environment you're seeing today going into the back half and give us some idea where your products are pricing relative to the published U.S. East Coast indices.

Jeremy R. Sussman — Chief Financial Officer

Nate, it's Jeremy. I'll start off and then turn it to Randy. So yes, that, your math certainly is correct. I would note a couple of things. One, Randy, in his comments on where pricing is today is, as you said, low-vol is up $50 a ton since we last reported Q2. So clearly, we're seeing higher prices today than anything that we have previously shipped. I think the second thing is, of the, call it, 300,000 tons or so, there were some semi-soft in there. We gave a good breakout of the semi-soft and everything on Slide 13, low-vol, high-vol A/B, et cetera., so any time you get a little bit of lumpiness in there that that can kind of skew the average a little bit. So that speaks to the kind of quarter-to-quarter cadence and Randy, I don't know if you have any other comments on pricing?

Randall W. Atkins — Founder, Executive Chairman, and Director

No. I think the only thing I was really referenced is, Nate, we've got sales that we've done that have netted us back probably in the $150 plus range at the mine. And if you take a look at where our cost structure is, that's pretty, you can figure out what kind of margins we're looking at. We think the market, as I said, it's got some legs. I would not be surprised to see further strengthening in the market as we go into the second half and perhaps even into 2022 because I think the thesis is that met coal has somewhat lagged some of the other steel supplies or really feedstocks like iron ore, because, frankly, you've had a situation politically with China and Australia, which I think has dampened a lot of the met coal pricing structures.

So I think is that, I'm not sure I would espouse that we're going to see any change in the Australia-Chinese puzzle over the next few months, but I do think that met coal will begin to catch up to what's happened earlier in the year on copper and iron ore.

Nathan Martin — Analyst, The Benchmark Company

Great, appreciate your thoughts there, guys. Just to kind of drill down on the last part of my question, any thoughts on discount or if you're getting roughly in line with U.S. East Coast indices, high-vol A, high-vol B, et cetera?

Randall W. Atkins — Founder, Executive Chairman, and Director

I don't like discounts, Nate. I think it would be a lot better if you talk about premiums.

Nathan Martin — Analyst, The Benchmark Company

Okay, that's great, thanks for those thoughts. Maybe if I could get your thoughts, guys, on how the domestic contracting season is progressing given, again, the extremely tight market we're seeing. Could you give us an idea how much you think pricing could possibly be up year-over-year given what we just talked about with export pricing, where it is today, that much higher than where it was a year ago during this time?

Randall W. Atkins — Founder, Executive Chairman, and Director

Well, I think the best guidance I could give you is that we, at least as we sit here today, expect that the dance will start sometime in September, when in September, it's not quite clear, but at some point. And I think to sort of handicap pricing sitting here in August is a little difficult. I don't see anything out there on the horizon that is going to impede sort of what continued upward trend in pricing. And as I said in my remarks, I guess, for the earnings release, I expect the pricing this year to be much more robust than the 2021 pricing, and we'll just have to see as we get closer to it.

Nathan Martin — Analyst, The Benchmark Company

Got it. Makes sense. I had to ask, obviously. I mean Lucas, touched on my bigger picture question. Obviously, you guys are now in that cash position. You've got some more cash, hopefully coming in the door related to the positive verdict on the Elk Creek silo failure. Again substantial amount of money, especially related to your current cash balance of about $19 million. And again, you lowered CapEx guidance for the second quarter in a row. So again, maybe just ask a little bit differently, what would be your first use, you think, for some of this extra cash that you guys are going to have on hand? Just any other thoughts there?

Randall W. Atkins — Founder, Executive Chairman, and Director

Yes. Well, the first thing, we're a relatively conservative bunch. So we certainly don't want to cash, count cash before we receive it. So we haven't cashed the check yet on the judgment that we just received against Chubb. And of course, we did borrow some money, and I'm fond of not having too much debt hanging around. So repayment of liabilities is certainly high on my priority list. And when we look at talking about dividends and things of that nature, of course, it's going to be paid out of free cash, not from borrowed money, at least from our vantage point. So we'll take a look at where we are a little later in the year. We'll take a look at what our forward thoughts are into 2022. We'll have a better visibility, as I said, on what 2022 may look like once we're beyond the domestic sales season. And we'll also, I think, have some visibility on how the steel industry is itself looking into 2022, which from all indications right now is that the steel industry is going to have an extremely strong 2022, which we think is great. And I think the other interesting dynamic is that typically, you've seen our coal industry rush into producing a lot of tons quickly whenever they saw a market rise. And I think this time, it's going to be a little bit different because in this cycle, we're seeing some real constraints on adding new production from the capital market side of the equation. And probably, there's a lot of people who would like to produce more coal, but just can't find the money to do so. We're fortunately in a position that we have that luxury to try to add some new tons, which we think we would try to add for near-term production. We don't want to have mines that they're going to take 3 or 4 years to build-out. We would like to see mines that would be in a position to be in production well inside of a year, and so we can take advantage of the market strength.

Nathan Martin — Analyst, The Benchmark Company

Got it, I appreciate those thoughts Randy. I think that’s it from me, thanks again for the time, and best of luck in the second half.

Jeremy R. Sussman — Chief Financial Officer

Thanks Nate.

Operator

[Operator instructions]

I am showing no further questions at this time. I would now like to turn the conference back to Mr. Randall Atkins. Please go ahead, sir.

Randall W. Atkins — Founder, Executive Chairman, and Director

Okay, thank you. And again, we, as always appreciate everyone's time and attention this morning. We hope we've addressed most of the questions that you've had, and we certainly are looking forward to a strong second half, and we'll look forward to speaking to you sometime in October or November. Take care.

Operator

This concludes today's conference call. Thank you for participating. You may now disconnect.