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HudBay Minerals' (HBM) Alan Hair on Q4 2016 Results - Earnings Call Transcript

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HudBay Minerals Inc., (NYSE:HBM)

Q4 2016 Earnings Conference Call

February 23, 2017 10:00 AM ET

Executives

Candace Brule - Director, IR

Alan Hair - President and CEO

Cashel Meagher - SVP, COO

Analysts

Matt Murphy - Macquarie Capital Markets Canada Ltd.

Orest Wowkodaw - Scotiabank

Alex Terentiew - BMO Capital Markets

Stefan Ioannou - Haywood Securities

Ralph Profiti - Credit Suisse

Operator

Good morning, ladies and gentlemen. Thank you for standing by. Welcome to the HudBay Minerals, Incorporated Fourth Quarter 2016 Conference Call. At this time all participants are in listen-only mode. Following the presentation, we will conduct a question-and-answer session. Instructions will be provided at that time for you to queue for a question. [Operator Instructions]

I would like to remind everyone that this conference call is being recorded today, Thursday, February 23, 2016, at 10 AM Eastern time.

I will now turn the conference over to Ms. Candace Brule.

Candace Brule

Thank you. Good morning and welcome to HudBay's 2016 fourth quarter results conference call. HudBay's financial results were issued yesterday and are available on our Web site at www.hudbay.com. A corresponding PowerPoint presentation is also available and we encourage you to refer to it during this call.

Our presenter today is Alan Hair, HudBay's President and Chief Executive Officer. Accompanying Alan for the Q&A portion of the call will be David Bryson, our Senior Vice President and Chief Financial Officer; Cashel Meagher, our Senior Vice President and Chief Operating Officer; Eric Caba, our Vice President of the South America business unit; Andre Lauzon, our Vice President of the Manitoba business unit; and Pat Merrin, our Vice President of the Arizona business unit.

Please note that comments made on today's call may contain forward-looking information. And this information by its nature is subject to risks and uncertainties, and as such, actual results may differ materially from the views expressed today. For further information on these risks and uncertainties, please consult the company's relevant filings on SEDAR and EDGAR. These documents are also available on our Web site. As a reminder, all amounts discussed on today's call are in U.S. dollars unless otherwise noted.

And now, I'll pass the call over to Alan Hair. Alan?

Alan Hair

Thanks Candace. Good morning everyone.

This time last year having started my role as CEO in a period of [cyclic lower] [ph] commodity prices, I laid out a clear plan for the company to adapt to the volatile metal price environment, while sustaining our pipeline of growth opportunities.

We proudly achieved our objectives, but the year was not without its challenges. In early 2016, we were focused on strengthening our liquidity position through cost reduction initiatives and credit facility renegotiations. Based on the detailed review of our operations, we identified over $100 million of operating and capital cost savings and we achieved this target as seen through our lower unit operating cost in both Peru and Manitoba with nearly 1/3rd reduction in total saving capital expenditures year-over-year.

In March, we amended our credit facilities plus extended maturities to 2019. With that principle amortization payments and introduced more flexible financial governance. In December, we refinanced 9.5% senior unsecured notes through the issuance of two separate longer dated tranches as a blended interest rate of just under 7.5%.

As a result of our efficiency in cost reduction efforts, we delivered low cost production growth in copper, zinc and precious metals maximizing the free cash flow generation of the business in 2016. We successfully maintained our pipeline of organic growth opportunities and positioned HudBay to advance high return in-house brownfield projects such as Pampacancha and Lalor expansion.

We also used excess free cash flow to readjust our debt position including $64 million repayment to our credit facilities in the fourth quarter. We achieved all of our annual guidance levels provided in February 24, 2016. Production of copper and precious metals improved exceeded the higher end guidance ranges, while unit operating costs were well within guidance and expectations.

In Manitoba, production of all metals and unit operating costs were within guidance range. Sustaining capital expenditures for the year were lower in both Peru and Manitoba resulting in approximately a 20% reduction in total sustaining capital compared to guidance. This was mainly as a result of cost savings at both business units and lower deferred stripping in Peru reflecting the updated mine plans of Constancia released in November.

There was also a small amount of capital deferred into 2017 primarily related to the construction of the last [indiscernible] road interconnect, which is expected to be constructed by the end of 2017.

In summary, 2016 was the year of volatile metal prices. But, our efforts to adapt the business to responsive environment paid-off as we achieved our guidance levels generated positive free cash flow [through just] [ph] that while positioning the business to be ready to refocus and growth when marketing conditions improved.

Taking a closer look at the fourth quarter results, our operations continued to achieve strong quarterly consolidated copper equivalent production and low cash costs in both of our Peru and Manitoba business units resulting in positive free cash flow generation.

Consolidated cash costs net of byproduct credits was $0.85 per pound of copper produced, a 7% decrease from $0.91 in the third quarter of 2016 reflecting higher byproduct credits and ongoing cost reduction initiatives.

Consolidated all and sustaining cash costs, net of byproducts was $1.46 per pound of copper produced unchanged quarter-over-quarter. Net loss and loss per share in the fourth quarter were $47 million and $0.20 respectively. Gross profit increased compared to the third quarter 2016, but net earnings were impacted by approximately $50 million in cost relating to fees and the call premium paid in connection with the bond refinancing in December along with the Fed tax adjustments and mark-to-market losses in various items.

Operating cash flow before change in non-cash working capital was $122 million or $0.52 per share relatively unchanged quarter-over-quarter. While copper sales volumes will lower this was offset by lower operating costs, higher zinc sales volumes and higher realized prices.

Cash and cash equivalents increased $29 million during the quarter. This increase was mainly the results of operating cash flow of $140 million partly offset by $44 million of capital investments and $64 million in principal repayments under the revolving credit facilities in the fourth quarter.

Net debt declined by $20 million as the $80 million increase in the outstanding senior unsecured notes was more than offset by high cash balance and credit facility repayments in the quarter. Our total available liquidity of $391 million increased by $114 million during the quarter due to the increase in cash and cash equivalents an additional $20 million in commitments under the credit facility and the repayments under the credit facility I mentioned earlier.

During the fourth quarter, the Peru operations were just approximately 34000 tons of copper, a slight decrease in the third quarter resulting in full year 2016 production above the top end of the guidance range.

Our mine during the fourth quarter of 2016 decreased quarter-over-quarter as our production rates were aligned to mill throughput rates. Mine and mill copper grades were lower than the third quarter as the mine plant continues to advance to low levels in the pit.

Total copper recovery was 81.6% in the fourth quarter compared to 83.6% in the third quarter as mining began in phase 2 of the consensus open pit were the initial near surface ore contains the greater amount of altered and oxidized mineralization.

Combined mine, mill and G&A unit operating costs were $7.98 per ton in the fourth quarter compared to $8.71 per ton in the previous quarter. Unit operating cost benefit from lower mining cost due to ongoing improvement initiatives combined unit operating costs were within guidance expectations.

Cash cost net of byproduct credits was $1.11 per pound of copper purchased, a slight decrease in the third quarter as a result of continued cost optimization and maintenance timing.

Sustaining cash cost, net of byproduct credits was $1.54 per pound of copper purchased, lower than the third quarter result of lower capital cost from tailings impoundment construction.

During the fourth quarter, Manitoba operations produced just approximately 10,000 tons of copper, 29,000 tons of zinc and 26,000 ounces of precious metals. While copper and precious metal production was inline with the third quarter, zinc production and concentrate was 8% lower due to lower zinc rates at 777.

Oil production at our Manitoba mine during the fourth quarter was inline with the previous quarter. Overall, copper and zinc grades were lower due to lower grades at 777 and Reed. However, in 2017 higher zinc grades were expected at 777 as a result of the resequencing of the mine plan to prioritize stopes containing higher zinc grades is just expected to result in an improved overall economics per ton at 777.

Combined mine, mill and G&A unit operating cost in the fourth quarter at $96.38 Canadian per ton were 4% higher than the third quarter as a result of unplanned maintenance expenditures. Combined unit operating costs were within guidance expectations.

Cash costs, net of byproduct credits in the fourth quarter was negative $0.06 per pound of copper produced, lower than the previous quarter due to higher realized zinc prices and the decrease in general support cost as a result of cost reduction initiatives.

Generally, for saving cash cost net of byproduct credits in the fourth quarter was $0.58 per pound of copper produced lower than the previous quarter affected by the same price impacting cash cost described above as well as for just capital expenditures.

Looking ahead in 2017, we will continue to focus on operating efficiency improvements in order to sustain the cost reductions we achieved last year and to generate incremental free cash flow from the business.

From a growth perspective, we remain committed to advancing the high return opportunities in our pipeline such as the Lalor throughput expansion and the Pampacancha deposits.

At Lalor technical work is underway in a new mine plan, which increased throughput from the mine and associated milling facilities while incrementally adding zinc and gold production in the near and medium term respectively. We expect to release the results in an updated technical report in Lalor before the end of the first quarter.

Construction of the Lalor paste backfill plant is underway and we expect to complete the majority of the work before the end of this year. Having paste backfill was intended to reduce operating costs, increased mining rates and maximize oil recovery.

At Constancia, we recently published an updated 43-101 technical report which incorporates the Pampacancha satellite deposit into the mine plan with first production expected in late 2018. We have allocated $25 million of capital to spend on Pampacancha in 2017 to advance the development of the deposit.

At Rosemont, we continue to advance permitting activities. We expect to publish a new technical report on Rosemont by the end of March outlining the feasibility work was completed since we have acquired the asset as well as new mineral [indiscernible] resource estimates.

We are also continuing to advance early stage exploration opportunities in the countries where we operate providing long-term organic growth potential in the pipeline. Given the improved metal price environment and HudBay's increasing free cash flow generation, we are reevaluating our exploration plans for 2017 with a focus in high priority exploration targets in Canada, Peru and Chile, which may result in an increase in funds allocated to exploration.

Lastly, we also expect to allocate free cash flow generation from the business to further adjust debt and lower our cost of capital. We are pleased with the position HudBay is in today as we enter 2017, but we will remain focused on sustained positive free cash flow generation while continuing to advance the return growth opportunities in our pipeline.

With that, we are pleased to take your questions.

Question-and-Answer Session

Operator

[Operator Instructions] And we have Matt Murphy [Macquarie Capital Markets Canada Ltd.] with our first question.

Matt Murphy

Good morning. Just wondering if you can provide some thoughts on how you look at Rosemont with the copper price maybe looking a little bit better than some people had expected and maybe the market asking more about growth projects then capital conservation as you are thinking on Rosemont changed at all, are you -- what thought are you giving as to how you'd finance it, how is that changed at all?

Alan Hair

Well, the first thing that points out obviously the Rosemont, we're still waiting for the permits. But we've also indicated that we believe for us to how about credit and financing plan we need to see copper prices with -- a three in front of them and that remains our view.

Matt Murphy

And any update in terms of permitting?

Alan Hair

I think it's fair to say that we've always viewed permitting as a scientific and technical process and we believe the good signs will prevail and we've got no reason to believe that we won't achieve our permits in due course.

Matt Murphy

Has there been any dialog since the transition of the political regime since New Year or is it just still awaiting a decision from the Army Corp?

Alan Hair

We're waiting both -- we're waiting on two federal permits, one from the Army Corp and one from the forest service. As we say we view this as a scientific and technical process, not a political process and we believe that good signs should prevail shortly.

Matt Murphy

Okay. Thanks.

Operator

And we have our next question from Orest Wowkodaw [Scotiabank]. Please go ahead sir.

Orest Wowkodaw

Hi, good morning. I was wondering, if we could to get a little bit more detail on plans in Manitoba moving forward. In 2017, you've up those end guidance fair amount in terms of resequencing 777 in terms of zinc production relative to 2016. How should we think about kind of 2018 and 2019, what the paste backfill plan, I guess on track to be finished this year. Is the 2017 number kind of a good run rate before you think about doing any mill expansions, say for 2018 and 2019 or any color you could provide would be helpful? Thank you.

Cashel Meagher

Hi, Orest. It's Cashel here. As you pointed out here we intend them producing more zinc. The motivation there is to take advantage of these higher zinc prices and so what we did as we relooked at optimizing the mine and the life mine, so that work is still underway. So we've done the 2017 work as per our guidance. We're still working out 2018 and 2019.

As an overall view of what we will produce going forward, we're going to provide some more detail on Lalor; we believe there is some more opportunity at Lalor to produce more zinc from there also. So we'll give better guidance on that closer to the end of the quarter.

Orest Wowkodaw

Okay. So at this point, how long where 777, how long can you kind of focus on the zinc before you have to normalize the mine plan again, given this not much…

Cashel Meagher

If you look at the previous technical report, I think the previous technical report has us running out of reserves sometime in 2020. So the question is, what is the sustained zinc price, what are we finding as we're heading towards the margins, the deposit as you know any mine that gets along in age, sometimes the stopes themselves are more difficult to recover. So what we're doing is we're taking a detailed look at what's available to us within the 777 mine to really understand going forward, but we're quite confident of what we're going to deliver in 2017 as you know in the past we've been unsuccessful at expanding those ore zones underground with underground exploration. So we have a limited resource there and we're trying to optimize that to get the best value for the community and for the shareholders.

Orest Wowkodaw

Okay. In terms of just the Lalor kind of study that will be coming out in March, will that include -- will that only look at expanding the Snow Lake mill potentially or would also include a review of refurbishing or restarting the New Britt mill?

Cashel Meagher

I think what we'll be able to do is, with respect to the New Britt and the gold zone is provide our plan going forward, what we intend on doing there, what we're working on. As far as the detail goes that will have to come sometime after as you can imagine reopening an older assets has many components to it, of which are tailings impoundment, condition of equipment and et cetera. So I think shortly after getting out some guidance on the base metal zone with this 43-101 at the end of the quarter, we will be able to produce and provide more detail in the gold zone soon thereafter.

Orest Wowkodaw

Okay. Thanks very much for the color, Cashel.

Cashel Meagher

Yes.

Operator

And we'll take our next question from Alex Terentiew [BMO Capital Markets]. Please go ahead.

Alex Terentiew

Hi, guys, good morning. I just want to circle back to Manitoba here, so, in 777 you guys have been mentioning lately, the mine is getting older obviously it's kind of approaching end of it's life and it's getting a little bit more challenging. So just on this throughput number, should the current rate be, we talked about Manitoba in general, but should the current throughput rate for 777 is that the kind of rate we should look at for the mine going forward? And on the cost side, the cost that we've seen over the past quarter or two are those the same sort of cost we should expect, cost per ton?

Cashel Meagher

Yes. It's right. Cashel again. I think like I sort of explained with Orest, I believe that we have 2017 well understood. I would be surprised to expect any higher throughput as we move along the margins of the ore and the areas of the mine become more distal to our hosting facility. So I think what we would try and do is maintain the current throughput with respect to having a certain base load requirement to optimize our milling cost. So as a per ton basis, mines or mills you could probably expect a similar sort of cost you've seen in the past few quarters.

Alex Terentiew

Okay. Great, thanks. And just wanted to clarify one of your last comments as well, so this update on Lalor next month it would be primarily just the base metal zone and the gold zone and it really incorporating the New Brittania mill that will come later on this year, did I hear that right?

Cashel Meagher

Yes. I wouldn't say later this year, but shortly thereafter maybe in the following quarter, we would be able to give reserve detail around the gold zone. At the end of this quarter, it would still be conceptual in nature because we're still working out some detail to support the reserve; it's not so much the underground mine ability and dilution that we're concerned about. It's about the detail around the costing of the capital of refurbishing New Britt and the tailings facility we may use which is [indiscernible] Lake, though it's just about getting some more detail around those areas. However, the gold zone itself and the recovery of the gold zone remains robust.

Alex Terentiew

Okay. Sorry, just one quick question here on Constancia, you noted Alan that a $25 million allocated in 2017 for public conscious, can I just read from that you are still on target to get your surface rights by year-end and begin pre-stripping at the deposit?

Alan Hair

Yes. That's still a plan as to having negotiation across surface right this year of the view to advancing the pre-strip next year.

Alex Terentiew

Okay, great. Thank you.

Operator

And we'll take our next call from Stefan Ioannou [Haywood Securities]. Please go ahead.

Stefan Ioannou

Thanks guys. Just back in Manitoba, obviously 777, as you mentioned, it's sort of starting to get fairly older here. Just wondering at Reed, is there any plans there to specifically to do exploration this year or is mostly that exploration in Manitoba are going to be focused in Lalor?

Cashel Meagher

Hi, Stefan. It's Cashel again. So Reed itself, we believe we sort of evaluated the extents of the deposit proper or drilling off the bottom of the zone, the copper areas, they are turning out more or less as expected. So we believe we found the extent of the ore zones at Reed and basically what's going on is infill drilling.

The exploration currently yes. We will be concentrated on some infill at Lalor. However, much of our exploration were going through we're seeing a rebirth with it and we'll start looking for other opportunities within the camp itself and in due course we'll talk about those as they become more material to this.

Stefan Ioannou

Okay. Would it be fair to say that these are sort of very grassroots stage targets or once you've done work on in the past that have seen drilling with or without JV partners?

Cashel Meagher

It's a combination of both, there will be some brownfields and there will be some greenfields within the camp.

Stefan Ioannou

Okay, great. Thanks very much guys.

Operator

[Operator Instructions] And we'll take our next question from Ralph Profiti [Credit Suisse]. Please go ahead.

Ralph Profiti

Thanks operator. I'm just looking at the old technical report, I understand as it dated for Lalor, but it show that waste in development tons fall off pretty significantly. And I was wondering is it possible that we'll see Lalor moving to sort of a waste neutral or waste deficit position in the next couple of years, is that still in the plan?

Cashel Meagher

Yes. So, Ralph, it's Cashel here again. Basically the balance of this year will see the construction of our paste backfield plant. And what has happened up until it's commissioning and continuing this year is we've had a need for rock underground to backfill various voids such that we're able to continue mining. So with that we have in front of us quite a bit a predevelopment or a majority of ore zones. So other than the gold zone itself which requires and the copper gold zone which require future and more development, the base metal zone is by and large developed and so we could see a drop off certainly in the base metal components in our required capital development.

Ralph Profiti

Got it, okay. And let me switch gears a little bit and talk a little bit about Rosemont and maybe a question for Alan. Do you still consider core is in the minority partner a long-term invested shareholder there or could we see a change in the ownership structure going forward or is it kind of too early to tell?

Alan Hair

Well, obviously, it's Korea Resources and LG that the -- our joint venture partners then we get no reasons to believe that they will not -- what we believe, they remain committed to the project.

Ralph Profiti

Okay. Thanks, Alan.

Operator

And we have a follow-up question from Alex Terentiew [BMO Capital Markets]. Please go ahead.

Alex Terentiew

Hi guys, just a quick question, Constancia, I haven't seen the moly numbers, moly production numbers just closed there, is the mine producing any moly at the moment? And then also the lower recoveries that you noted, I recall that back in 2015 and 2016 when you are ramping up Constancia, you have some of the transition oxidized material when we went through that, you saw your recoveries go up, so is this kind of a Q4 and maybe a Q1 issue and you expect to see recoveries improve back into Q2?

Cashel Meagher

Hi, Alex. I think you're right on with the latter. Basically, yes, we're going through what we call our phase 2 pushback and it's from surface down and so we have been going through mixed transition. And so we have seen elevated oxide and as you know the plant itself for copper sulfide, copper minerals and so the copper total against copper total our recovery has gone down, although the ratio remains solid that the percentage of sulfide material recovered still remains in the high 80s. So it's just we report against copper total which includes some of the copper oxide or copper soluble component.

And as for the moly, we do we are getting more confidence in the moly plant. We've made some sales in moly. We expect this year with the variability and throughput as the like of mixed transitions and some current material and some supergene material that we find the moly plant becomes more stable and more predictable when we're milling less of variable throughput. So we believe it's still a material impactful for the majority of the reserve, the hypergene. And as we go further into the year, we expect to be able to improve our recovery and production of moly and then in further years even better as we get more stable and more stable or more singular feet.

Alex Terentiew

Okay. That's great. Thank you.

Operator

And it appears there are no further questions at this time. Ms. Candace Brule, I would like to turn the conference back to you for any additional or closing remarks.

Candace Brule

Thank you, operator, and thank you, everyone, for participating. Please feel free to reach out to our Investor Relations department if you have any additional questions.

Operator

And this concludes today's call. Thank you for your participation. You may now disconnect.

Comments (0)