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National Coal Corp. (NCOC)
Q1 2009 Earnings Call Transcript
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Executives

Christine Pietryla – Director, Communications
Daniel Roling – President & Chief Executive Officer
Mike Castle – Chief Financial Officer

Analysts

Brett Levy – Jeffries and Company
Al Shams – MidSouth Capital
Michael Gaugler - Brean Murray

Presentation

Operator

Welcome to the first quarter 2009 earnings conference call. At this time, all participants are in a listen only mode. Later there will be an opportunity for questions and comments, instructions will be given at that time. I would now like to turn the conference call over to our host, Director of Communications, Christine Pietryla.

Christine Pietryla

Good morning. Thank you everyone for joining us. Today, we're going to discuss National Coal's first quarter 2009 results. Management's statements will be followed by a question and answer period.

Before we begin, I want to remind everyone that we will be discussing forward-looking information on this call. Examples of forward-looking statements include, anticipated benefits of capital improvements and new mines and anticipated strengthening or weakening within the coal market. Forward-looking statements should not be read as a guarantee of future performance or results and are based on information currently available. Forward-looking statements made on this call are based on management's good faith belief at this time with respect to future events and are subject to risks and uncertainties that could cause actual performance or results to differ materially from those expressed in or suggested by the forward looking statements. These conditions are more fully described in the company's filings with the Securities and Exchange Commission, including our most recently filed annual report on Form 10-K and quarterly reports on Form 10-Q.

Further, we will also be referring to non-GAAP financial measures, which are reconciled in all of our quarterly earnings releases, all of which are located on our website.

With that, I would like to introduce Daniel Rolling, our President and CEO.

Daniel Roling

Thank you everyone for joining us on the first quarter conference call for National Coal Corporation.

Our first quarter as a difficult quarter but we think we made some major achievements. First and foremost, we finished delivery on the majority of our coal for 2008 that we had fallen behind on last year due to production problems that we addressed at year end, most notably the drag line that was down in Alabama and some of our operating problems in Tennessee.

So now that we have caught up on those, we were able to realize somewhat higher prices in the first quarter and we anticipate our prices to continue to increase marginally as we go through the year, along with increasing volumes as we go through the year.

Clearly, the first quarter not only was impacted by that, it was also impacted by the closure of two mines as we finished removing the assets from those mines and reclaiming them and moving into new mines which got up and full-running by the end of the first quarter.

So the first quarter was somewhat difficult. Also the coal market has deteriorated dramatically in the last two months. So far we are continuing to ship on all our committed tons and we anticipate continuing to do that.

At this point I would like to turn it over to Mike Castle, our Chief Financial Officer. He can walk through the financials and then he'll turn it back over to me for a couple of more comments and then we will go to Q&A.

Mike Castle

I will discuss the first quarter 2009 results as compared to the same quarter 2008 and certain noteworthy changes since December 2008 in our operating results, balance sheet, and overall liquidity.

In the first quarter of 2009 we sold 469,000 tons at an average sales price of \$72.68 for total sales revenue of \$34.1 million. That's compared to 612,000 tons sold at an average sales price of \$57.96 per ton for total sales revenues of \$35.5 million in the first quarter of 2008. That represents an increase of 25.4% on our average sales price per ton with a decrease of about 3.9% on total revenues for coal sales.

The decline in coal sales revenue and total sales tons is due primarily to the sale of our Kentucky operations in the first quarter of 2008 and an increase of approximately 25% sales price per ton since that period.

We sold approximately 101,000 tons of coal from the Kentucky operations in the first quarter of 2008 at an average sales price of \$48.12.

Our cost of sales was \$31.5 million and was \$67.13 per ton in the first quarter of 2009 compared to \$34.5 million on \$56.31 per ton in the same quarter of 2008, which is an increase of approximately 19.2%.

The increase in cost of sales for Q1 2009 versus Q1 2008 can be attributed mainly to increases in major cost components across the board, including fuel, labor, explosives, related items and royalties. However, I will note that our cost of sales has declined from \$71.00 per ton in the fourth quarter of 2008. We should continue to see these reductions in our cost of sales if we are able to maintain normalized production and sales going forward, which should increase our margins.

We were also transitioning into two new mines in the first quarter of 2009, both of which are now operating at lower costs than the mines they replaced.

And going to the balance sheet and the statement of cash flows, while we generated \$4.5 million in cash from operations, our cash on hand at March 31, 2009, was \$2.9 million, a decrease of \$1.7 million from the December 31, 2008, balance of \$4.6 million.

Also, we experienced a \$5.8 million increase in accounts payable since December 2008. Without getting into too much detail, the cash decrease was nearly offset by the increase in our receivables, while the AP increase is mainly attributable to third-party purchases of coal in late February and March. These coal purchases were paid during the first week of April.

We purchased 84,000 tons of coal during the quarter ended March 31, 2009, mainly to supplement lower than expected production during the transition into the two new mines.

Now, we also incurred just over \$4.0 million in capex during the quarter. Most of this was for minor development costs associated with the two new mines we've opened and for maintenance and capex. So we took the opportunity to do more than usual capex during the transition of equipment to these new mines.

Also it should be noted we put in place a revolving credit facility in early April 2009 which provides additional liquidity if needed for National Coal Corporation, our Tennessee operations.

Dan, I would like to turn it back over to you and you can add anything and then we can open up to questions.

Daniel Roling

The last comments I will make is just about the market in general. The market has pulled back from very strong levels of last year where we set record prices but not necessarily record volumes. Coal production last year was up only 0.6% from the prior record in 2006.

I think the message clearly being sent was that the ability to produce significantly increased amounts of coal, even at significantly is extremely limited in this market. Thus as we move forward, it's my belief that when electricity demand comes back, which will be in line with an economic recovery, the ability to increase coal production will be quite limited. In fact, coal production is already declining this year.

Some of that coal reduction will be permanent, some will be temporary, but I do believe as we move through the year and demand recovers we will see a significant in the price of coal and in the demand for coal as we move out through the next year.

As we have said, both prices and volumes for our coal should increase gradually as we progress through the year as we transition into our new higher priced contracts. We also believe that if we're able to continue producing in line with our plans, that our costs will continue to come down as they did come down in the first quarter versus the fourth quarter.

So the key to our success looking forward will continue to be the strong demand for coal, our ability to produce coal, and a continued good market.

With that, we will open it up for Q&A.

Question-and-Answer Session

Christine Pietryla

Our first question comes from Brett Levy – Jeffries & Company.

Brett Levy – Jeffries and Company

I notice you have got a \$200,000 bad debt expense. I know that's not a big number but I'm just wondering if it's indicative or more things to come.

Mike Castle

That was sales to a broker, quite honestly, quite some time ago. We had been receiving some pay downs on that and that ceased here recently. And we do anticipate collecting that but it was quite old and we actually had continuing discussions with that individual and it looks like we may end up having a good opportunity to collect that going forward on some additional business.

Brett Levy – Jeffries and Company

And can you quantify, you said you had the closure of two mines. Anytime of the one-time stuff during the quarter, is there any way of quantifying what that effect was?

Daniel Roling

We have not quantified it. It was meaningful but it's not a number that we're comfortable—well I shouldn't it's not a number we're comfortable putting out, we would be but it's we think that what is more important is that as we move forward and are able to show our costs on an ongoing basis that that will continue to show the progress we are making. But clearly our \$67.00 per ton cost would be significantly lower if in fact we had not incurred those costs for mine closure, the transitioning cost into the new mines.

Mike Castle

One thing I will add, about half of that capex was simply due to development costs to get those mines open, so I do consider those a one-time cost, if you will, and it looks like one of the new mines, the [inaudible] mine, the new mine has significantly lower over-burden ratios that what we had been experiencing so cost should be significantly lower down there.

Brett Levy – Jeffries and Company

You said things have slowed down, at this point does it look like shifts will be lower in the second quarter than the first quarter?

Daniel Roling

No, we believe they will be higher as we progress through the year. The comment that I made refers to what we said at the fourth quarter. What we anticipate that the capability to produce versus our contracted tonnage. So as we move forward we will still hit our contracted tonnage but we won't be selling incremental tons onto the spot market because the spot market is not strong enough to justify doing that.

Brett Levy – Jeffries and Company

What is your target cost of goods sold, as you kind of look all your inputs and that kind of thing? What would it be for this year, the target?

Daniel Roling

Lower. We have not put out a number and we don't anticipate putting out a number but we do believe the trend will continue to move downward.

Brett Levy – Jeffries and Company

And you just put in place a new bank facility. I think initially the sense was that this is a facility that would be put in place as kind of a backstop or a just-in-case kind of line. At this point, based on the slowdown in the coal market, do you think you'll draw on that line during 2009?

Daniel Roling

Our intention all along was to use it opportunistically, where we would draw and then pay it back. It is not a line that we anticipate drawing down fully and then leaving outstanding. We do plan to use it opportunistically, where appropriate, to draw down and then pay it back and continue that pattern.

Christine Pietryla

Our next question is going to come from Al Shams – MidSouth Capital.

Al Shams – MidSouth Capital

Dan, so it's your thinking that with the bank line you've got kind of as a standby back up that we've got sufficient sources of liquidity to carry us through this year?

Daniel Roling

Yes, we believe that is true. And this will be helpful to achieving it and allowing us to be a bit more opportunistic where appropriate.

Al Shams – MidSouth Capital

Just one comment. I thought you did a real good job on the annual report. You know, I've really taken the time to talk to shareholders about the overall environment in the coal industry and then about particular circumstances affecting National Coal. So I think that was a good informative report when many times people just send out a 10-K with nothing else, so thanks for that.

Daniel Roling

Thank you, Al.

Christine Pietryla

Our final question will come from the line of Michael Gaugler - Brean Murray.

Michael Gaugler - Brean Murray

I just noticed one thing off the balance sheet, looks like restricted cash was essentially flat quarter-over-quarter. Any opportunities to free some more of that up in the coming quarters?

Mike Castle

Possibly. We are continuing to determine our bonding needs beyond the fourth quarter here. Of this year. So there is a chance that we will free some of that up.

Christine Pietryla

That was our last question.

Daniel Roling

Well, thank you all for participating in our conference call. We will look forward to talking to you at the end of the second quarter. If there are any further questions or follow-up please do not hesitate to either email or call us directly. We are always happy and look forward to speaking to our investors.

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