



Timminco bleeds more red ink, investors take flight

2008-11-14 17:14 ET - Street Wire

by Lee M. Webb

Timminco Ltd., a Toronto Stock Exchange (TSX) solar play headed by Heinz Schimmelbusch, released the financial results for its money-losing third quarter after the market closed on Nov. 11. The results were reported just a week after the Financial Post gave Mr. Schimmelbusch the nod as Canada's top-performing chief executive officer for 2008.

The once-hot solar play was a star performer on the TSX through 2007 and the first half of this year, rocketing from 30 cents per share in January of last year to a high of \$35.69 per share in June of this year as bullish analysts touted the stock and financial reporters churned out puff pieces celebrating its meteoric rise. The market and media infatuation with Timminco has waned in recent months, along with the stock price.

In the wake of Timminco's disappointing third-quarter results a number of analysts have slashed their price targets and jittery investors are giving the cold shoulder to the former market darling.

The numbers

For the third quarter ending Sept. 30, Timminco posted a loss of approximately \$13.7-million or 13 cents per share on revenue of \$69-million. The company's accumulated deficit now stands at \$102.9-million.

During the third quarter, Timminco's bank debt climbed to \$24.3-million, up \$14.3-million from the \$10-million outstanding at the end of the previous quarter. That figure is likely to grow, given that the company has since increased its line of credit with Bank of America from \$32.8-million (U.S.) to \$50-million (U.S.) to help finance the planned expansion of its solar-grade silicon facility in Becancour, Que.

The company received \$33.3-million in deposits from solar-grade silicon customers during the quarter and another \$4.2-million customer deposit subsequent to the end of the quarter. The deposits, which are earmarked to help pay for the Becancour expansion, are non-interest bearing prepayments to be credited against future deliveries of solar-grade silicon.

Even with the increased borrowing and customer deposits during the third quarter, Timminco only had \$2.5-million in cash as of Sept. 30.

During the quarter, Timminco recorded a \$13.8-million impairment charge relating to its peculiar investment in Fundo Wheels AS, a money-losing Norwegian company that makes aluminium wheels for high-end automobiles. After pouring millions of dollars into Fundo even as it was experiencing its own cash problems, Timminco has written the investment down to its fair market value: zilch.

Oddly, even after Timminco experienced its epiphany on Fundo's road to insolvency, Mr. Schimmelbusch and his management team decided to help the troubled Norwegian company out again. Subsequent to the end of the quarter, financially challenged Timminco bought \$1.7-million worth of wheels from Fundo.

Under the strange purchase agreement, Fundo is supposed to resell the wheels on behalf of Timminco and remit the proceeds by the end of December. Adding to the peculiarity of the deal, Timminco's parent AMG Advanced Metallurgical Group N.V., which is also headed by Mr. Schimmelbusch, has guaranteed to cover any shortfall in the expected proceeds of \$1.7-million.

Most of the interest in Timminco, of course, turns on the company's solar-grade silicon operation, which is based on a secret proprietary process. During the third quarter, Timminco shipped 300 metric tons of solar-grade silicon, up from the disappointing 221 metric tons shipped during the previous quarter.

While the volume of solar-grade silicon shipments increased during the third quarter, the average selling price plunged. Through the first two quarters of the year, Timminco received approximately \$65 per kilogram for the material. In the third quarter, however, the average selling price only came in at \$53 per kilogram as Timminco reported approximately \$16-million worth of solar-grade silicon sales.

Perhaps of at least passing interest, Timminco's third-quarter filings disclose that the company purchased a vacuum furnace used in the production of solar-grade silicon ingots from ALD Vacuum Technologies GmbH, for \$900,000. ALD is a wholly owned subsidiary of AMG.

In early August, Stockwatch asked Mr. Schimmelbusch about the furnace, but he did not bother to respond. During the second-quarter conference call held a week after Stockwatch put questions to him about who owned the furnace, how much it cost and how it would be financed, however, Mr. Schimmelbusch did respond to a softball lob from Clarus Securities Inc. analyst Carolina Vargas, who wanted to know about the progress with "in-house ingot manufacturing."

After serving up a spiel about AMG, through its subsidiary ALD, being a leader in producing the vacuum furnaces and how it fast-tracked the delivery to the Becancour plant, Mr. Schimmelbusch remarked that the importance of the development "is not to be underestimated."

With the release of the third-quarter financial statements, Timminco shareholders now know a bit more about that important development.

Timminco released the third-quarter results after 4:30 p.m. and held its conference call at 5 p.m. on Nov. 11.

The spin

Mr. Schimmelbusch opened the conference call with some introductory remarks regarding the "highlights" of the third quarter.

"The third quarter was marked by our continued progress in the ramp-up of solar-grade silicon product as well as the ongoing expansion of production capacity at our facility in Becancour, Que.," Mr. Schimmelbusch began.

Earlier in the promotional cycle much was made of the relative simplicity of Timminco's black-box process and the ease of adding additional production capacity, but that narrative subsequently changed to one involving complexity.

"Of particular note, we resolved a number of challenges related to our first three production lines that we considered to be typical for the start-up of a complex industrial process," Mr. Schimmelbusch said, echoing remarks that he made after the company's disappointing second quarter.

Timminco's leader went on to note that the company had shipped 300 metric tons of solar grade silicon at an average selling price of \$53 per kilogram during the quarter.

During the second-quarter conference call, Mr. Schimmelbusch had balked at a request for information regarding month-by-month production, lamenting that quarterly reporting was enough of a burden. This quarter, however, he volunteered some information regarding monthly shipments.

"I will note that our shipments increased sequentially each month throughout the quarter, culminating in a record month in September," said Mr. Schimmelbusch.

"I will also note that the lower average selling price compared to the second quarter of this year reflects a change in the mix of customers to which we shipped material during the quarter under long-term, fixed-price contracts," he added.

According to Mr. Schimmelbusch, feedback from Timminco's solar-grade silicon customers has been positive, all shipments met or exceeded customer specifications and no material was returned during the quarter.

Remarking that product quality is a key differentiator for Timminco, Mr. Schimmelbusch reported that some of the solar-grade silicon shipped during the quarter had boron levels as low as 0.5 parts per million and phosphorous levels as low as 1.5 parts per million.

"Equally as important, our customers had reported cell efficiency as high as 16 per cent using our product in an unblended manner," he added. "This demonstrates the advances some ingot and wafer experts have made in process knowledge over the past year."

Mr. Schimmelbusch did not disclose which customers had achieved that rather impressive cell efficiency using unblended upgraded metallurgical silicon produced by Timminco.

"Clearly we are making solid progress in our solar-grade silicon business," Mr. Schimmelbusch remarked. "Nonetheless, it is important to understand that our solar-grade business is still in its initial stages and that neither the ramp-up of production nor the commissioning of additional lines is a trivial undertaking."

According to Mr. Schimmelbusch, the planned expansion to 14,400 metric tons from the initial 3,600 metric tons is going well. The fourth production line at Becancour was commissioned at the end of

October and Timminco plans to have the full 14,400-metric-ton operation commissioned by the middle of next year.

Mr. Schimmelbusch wrapped up his opening remarks by reiterating the company's guidance that it expected to ship between 1,200 metric tons and 1,500 metric tons of solar-grade silicon this year.

Timminco's chief executive officer then handed the call off to Robert Dietrich, the company's chief financial officer for a review of the financial results. Mr. Dietrich did not stray far from the financial summary released just ahead of the Nov. 11 conference call and published by Stockwatch.

Mr. Dietrich did "add some colour," as analysts are fond of saying, to Timminco's inventories, which increased by approximately \$20.4-million during the quarter and were valued at a rather hefty \$81.1-million as of Sept. 30.

"The increase relates primarily to a buildup of silicon metal feedstock to supply the ramp-up of our expanding solar-grade silicon facility and to the accumulation of by-products from our production of solar-grade silicon," Mr. Dietrich said.

"With respect to feedstock, it is operationally imperative that we have sufficient inventory of raw material on hand to support the commissioning and ramp-up of the new production lines over the coming months, while we concurrently bring the use of molten metal on stream," he added.

According to Mr. Dietrich, the goal is to reduce the inventories during the fourth quarter.

After Mr. Dietrich finished his financial recital, Mr. Schimmelbusch offered a few more upbeat comments before inviting questions.

The questions

Ms. Vargas, widely recognized as Timminco's most bullish analyst, was up first, opening by offering congratulations regarding the purity levels achieved during the quarter and the reported cell efficiency obtained by the company's unidentified customers.

Remarking that September's production must have been "really strong," Ms. Vargas asked for comments regarding the volumes exiting the quarter.

Mr. Schimmelbusch noted that he had already said that volumes increased sequentially through the quarter.

"But Carolina, you will not seduce me to issue now monthly statements because the next step will be weekly and I'm, you know, I'm out of here," Mr. Schimmelbusch added. "So that's it. We increased it month by month and September was very strong."

Ms. Vargas then wanted to know whether she could continue to target normalized solar-grade silicon production costs of between \$12 per kilogram and \$15 per kilogram, figures previously touted by the company. Timminco's solar-grade silicon production costs for the third quarter actually came in at \$31 per kilogram, down only slightly from \$32 per kilogram for the previous quarter.

"With respect to guidance going forward, we really now intend to report on a quarterly basis where we are in our costs rather than focusing on a specific cost target," Mr. Dietrich said.

As part of its Nov. 11 news release, Timminco reported that it would be removing an operational review report prepared by PHOTON Consulting from its website. In May, Timminco paid for the so-called operational review report, which included extremely bullish forecasts based on information provided by the company. The removal of that report prompted another question from Ms. Vargas.

"Could you give us a little bit of colour on why the report is removed?" the Clarus analyst asked.

Mr. Dietrich's attempt at colouring did not result in a much clearer picture. After offering some rambling remarks about the third party report, forward looking statements and updating information, Mr. Dietrich said that it was decided that it would be appropriate to remove the report.

Rupert Merer, an analyst with National Bank Financial, was up next with a question about production from the fourth furnace that was commissioned after the end of the quarter. Rene Boisvert, the head of the Becancour operation, handled that question.

"We've had a very successful startup of the fourth line (at) the end of October and it's producing at the same rate as the three other units in operation," Mr. Boisvert said.

"Can you give us a little more colour on the inventory?" Mr. Merer asked, turning to a topic that would prompt a number of questions during the call. "How much of the inventory is recycled silicon versus the raw material from the arc furnace?"

Mr. Dietrich jumped in to respond to that question.

"Well, we aren't going to disclose the dollar values related to it, but the proportion is definitely the raw material, the raw silicon material, is significantly larger in proportion than the by-product that we will recycle," Mr. Dietrich said.

Mr. Merer gave way to CIBC World Markets analyst Michael Willemse, who also had a question about inventory.

"The raw material inventory, that is expected to be worked down by the end of the fourth quarter?" Mr. Willemse queried.

"No, what I said is we would use it during the fourth quarter," Mr. Dietrich began his response. "The silicon metal that is on hand as feedstock for the ramp-up period, at some point we won't require that because we will be using metal from our electric arc furnaces -- molten metal -- and that will occur over the coming months.

"I don't think we know when the end of that is. We'll certainly update on our next call as to where we stand on that."

Mr. Willemse followed up with a question about the lower average selling price obtained during the quarter, asking whether that had anything to do with different purity levels or simply customer mix.

Mr. Schimmelbusch explained that the company's earlier supply contracts were set at lower prices than subsequent contracts and it just happened that earlier customers received more material during the quarter.

Ian Tharp of Dundee Securities Corp. was among the other analysts who had some questions for Timminco's executives.

Remarking that Timminco had previously given guidance regarding planned shipments of 9,000 metric tons of solar-grade silicon in 2009, Mr. Tharp wanted to know whether that guidance still held.

"What we have said is that we are confident that we (will) meet our customer obligations for 2009," Mr. Schimmelbusch responded without mentioning any specific target.

Further into the conference call, Cormark Securities analyst MacMurray Whale, who has been bearish on Timminco, had some questions.

"I'm wondering, in terms of the inventory, can you give us that in terms of metric tons?" Mr. Whale asked.

"No, we don't disclose our inventory to that level of detail," Mr. Dietrich replied rather brusquely.

Mr. Whale then asked for an explanation regarding the purity level of the inventory material when compared with the material made in the company's silicon metal operation.

"No," one of the Timminco executives muttered before Mr. Boisvert stepped in with some more helpful information.

According to Mr. Boisvert, the inventory material is of higher quality than the metallurgical silicon that Timminco has sold to its customers over the past few years, but not as high a quality as some of the other material that has been used as feedstock for the solar-grade silicon operation.

Remarking that Timminco had discussed its startup costs in the previous quarter, Mr. Whale said that he did not see that figure in the Nov. 11 press release.

"Could you just share that number with us?" Mr. Whale asked.

"No, it's specifically not in the material because we think it's important for people just to focus on what the costs are," Mr. Dietrich said. He went on to say that there had been some confusion about how Timminco had described the costs last quarter, so it is better to just think of a pool of costs related to the solar-grade silicon operation.

After some other callers had their turn, several analysts, including Mr. Merer, had some follow-up questions.

"Can you tell us what your customer obligations are for 2009 in terms of metric tons?" Mr. Merer asked.

After commenting that it was "tricky" inasmuch as he had already said that Timminco was confident of meeting its customer obligations for 2009, Mr. Schimmelbusch sidestepped the question by saying that he did not think that they had actually added up those commitments.

"But some of you have made a very good job of trying to figure out that number," Mr. Boisvert chimed in cheerfully.

The analyst did not press the issue, so just how Mr. Schimmelbusch can repeatedly express confidence about meeting shipment obligations for next year without knowing how many metric tons the company is supposed to deliver remains a mystery.

Mr. Merer, perhaps looking for some insight into the significantly lower average selling price attributed to customer mix, also wanted to know how many unique customers Timminco had shipped to during the quarter.

"We shipped to all of our contracted customers," Mr. Boisvert replied.

Mr. Willemse also jumped in with some further questions, returning to the popular subject of the inventory and wondering why the company would be able to process material in the fourth quarter that was not suitable for processing in the third quarter.

"Because we'll have better purification capacity and better control of the process," Mr. Boisvert said.

Rounding out his supplemental questions, the CIBC analyst wanted to peek further into the future.

"You're targeting hitting annualized capacity of 14,400 (metric tons) in the middle of 2009," Mr. Willemse began. "When do you start thinking about the next expansion after that?"

"We are always thinking about what will happen after that day," Mr. Schimmelbusch replied. "It will be, by the way, a happy day. All eyes are on ramping up the existing plant. We have ideas what happens after that, but they are not disclosed yet."

"Okay, thank you," Mr. Willemse said.

"If you analyze us carefully, you might draw your conclusions," Mr. Schimmelbusch added cryptically.

Ms. Vargas also made an encore appearance, first looking "for a bit more colour" on Timminco's magnesium business.

It is no secret that Timminco would like to unload the magnesium division. Mr. Schimmelbusch explained that it is a "non-core business" that the company hopes to stabilize.

Ms. Vargas then asked whether there would be any more impairment charges relating to Fundo.

"It's the end of the impairment charges because it's 100 per cent of the book value," Mr. Schimmelbusch said.

As the conference call was winding down, Sean Steuart from TD Newcrest asked why there was not much of an improvement in the solar-grade silicon production costs, which had only dropped from \$32 per kilogram in the second quarter to \$31 per kilogram in the third quarter.

Mr. Schimmelbusch explained that there had not been any additions to the production lines between the second quarter and the third quarter, but that would change going forward.

"As we have stated several times, every month another furnace goes on stream for the next nine months," Mr. Schimmelbusch said. "That is accompanied by adjustments of the flow sheet, naturally, and a rearrangement of how we use all these furnaces in a more mature fashion and that will change the cost structure. That's the major driver."

The conference call came to an end a short time later.

The reaction

As noted above, a number of analysts slashed their price targets for Timminco in the wake of the company's third-quarter results and conference call. Even the optimistic Ms. Vargas has revised her expectations. Stockwatch will review some of the analyst reports in more detail in a following article.

The market reaction needs little review.

On Nov. 12, investors hammered the stock. With more than 1.7 million shares changing hands the day after Timminco released its quarterly results, the already battered stock shed \$1.22 to close at \$6.77.

A more modest 949,000 shares were traded the next day. While the average price for the session was \$6.62 per share, Timminco staged a late rally to close at \$7.45 on Nov. 13.

Trading was even lighter on Friday. With approximately 360,000 shares changing hands, Timminco lost 45 cents to close at \$7 on Nov. 14.

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