PHOSPHATE HOLDINGS, INC

Moderator: Robert Jones
November 11, 2010
3:30 p.m. CST

Operator: Good day everyone and welcome to the Phosphate Holdings Inc., Third Quarter 2010 Earnings conference call. Please note that Phosphate Holdings Inc., issued their Third Quarter and 2010 operating results on November 9th, 2010.

As you read the company's press release which is also posted on the company's Web site at (www.missphosphate.com), and as you listen to this conference call please recognize that both contain forward-looking statements within the meaning of federal securities law. All statements in the release and (oral) statements on this call or other discussions, other than those relating to historical information or current condition are considered forward looking statements.

These forward looking statements are subject to a number of risks and uncertainties, any of which are beyond the company's control and which could cause actual results to differ materially from such statements. These risks and uncertainties include those spelled out in the Safe Harbor statement included in the press release. Consider all forward-looking statements in light of those and other risks and uncertainties and do not place undue reliance on any forward-looking statements.

Now let me introduce Mr. Robert Jones, Chief Executive Officer of Phosphate Holdings, Inc. Mr. Jones, please begin.

Robert Jones: Good afternoon, everyone and welcome to our earnings call for our third fiscal quarter of 2010. In the room with me in Madison, Mississippi, are Ed McCraw, our Chief Operating Officer, Tim Cantrell, our Chief Financial Officer and Jim Perkins, our Vice President of Sales and Marketing.

Following a very difficult second quarter during which we incurred a loss of $4.9 million, we are very pleased to report positive results for our third fiscal quarter of 2010. During the quarter we recorded a profit of $2.5 million on sales of $70.4 million. EBITDA for the quarter was $7.3 million, this represents a nearly $12 million increase over our second quarter EBITDA of negative $4.6 million.

During the course of our third quarter production problems once again affected our results. These problems primarily impacted our sulfuric acid plant which in turn limited that production and impaired our ability to fully participate in a rapidly improving phosphate market.

For the quarter, we were able to produce only 156,000 tons of DAP. We have gone back and prepared pro-forma results assuming that we had produced acid and DAP at planned levels and under that scenario we would have generated approximately $13 million of EBITDA during the quarter.

We are currently engaged in a major maintenance turnaround during which we intend to address all known issues impacting our sulfuric acid, phosphoric acid and DAP production. Due to the extended scope of the work being undertaken the current turnaround will cost more money, approximately $6.5 million, and will require more downtime than our customary and normal turnarounds.

It is very important that we complete this work on time, on budget and that we achieve the targeted results of this effort. But no assurances can be given; we believe that we should emerge from this turnaround in late October with materially improved production rates.

While operational issues were again a major topic for the quarter, the lead story for the third quarter was unquestionably a rapidly improving phosphate market. A strong bullish trend in Ag outputs which began in mid-summer drove fertilizer demand and prices throughout the quarter.

At the beginning of the quarter the price of DAP, FOB NOLA was approximately $400 per short ton. By quarter's end, the NOLA price had risen approximately 37.5 percent to $550 per short ton. Prices have continued their upward movement in our fourth quarter to date and we are currently in the mid $560s, FOB NOLA.

The outlook for the balance of 2010 and well into 2011 is positive. The global supply/demand balance for grains is tight, crop prices are high across the board, farm income is very strong, the outlook for planted acres is favorable and all this of course adds up to a strong fertilizer demand and hopefully strong prices.

During the balance of our call, I'll ask Jim Perkins to discuss the market conditions that drive our business in greater detail. Tim Cantrell will then review our third quarter financials and finally Ed McCraw will discuss production during our third quarter and the outlook for production for the balance of the year and into 2011. After that we'll return and answer any questions that you may have. Jim?

Jim Perkins: Tight supply and stable pricing continue to characterize the current phosphate market.

Domestic DAP prices began a bull run in mid-June, and the trend of upwardly rising prices continued through the third quarter, as we saw domestic prices for NOLA barges increase by roughly 35 percent, from $408 per short ton in early July to $550 per short ton in late September.

More recently, with the fall application season beginning to wind down, the rate of domestic price increases has moderated, and current NOLA barge pricing is in the mid $560's per short ton.

While export DAP pricing followed a similar upward trend, domestic sales yielded a premium over export sales for the bulk of the quarter. That premium had grown to as much as $40 per short ton by the end of Q3. Consequently, all of our third quarter sales were directed to domestic markets.

In more recent weeks, with reports of Latin American and Australian sales at the equivalent of $600 per metric ton Tampa, the spread between export and domestic net-backs appears to be narrowing. Nevertheless, the domestic premium still remains, and that premium will continue to draw imported tonnage to the US until the net-backs eventually converge.

Looking ahead, the outlook is good for the fertilizer sector, and supply/demand fundamentals seem set for continued firmness through the fourth quarter and into 2011.

- Global grain consumption, led by growing populations and demand for higher quality diets in developing countries such as China and India, is outpacing global grain production. Ending global stocks this year are currently projected down by 12.7% and 11.7% for corn and wheat respectively, on a year-to-year basis.

  Earlier this week, the USDA cut the projected 2010/2011 US corn crop by 124 million bushels, to 12.54 billion. The reduction was primarily due to a reduction in yields, from 155.8 bu/acre to 154.3 bu/acre.

  Granted, a 12.54 billion bushel corn harvest is huge – it would rank as the 3rd largest corn crop ever. However, corn usage in 2010/11 is projected at 13.54 billion bushels, an all-time high that pushes ending stocks to only 827 million bushels – the lowest corn carryover since 95/96. That results in a stocks-to-use ratio of 6.2%, also the lowest since 95/96.

- Crop prices are surging across the board.

  Since early in July, cotton prices have risen 32%, to the highest levels seen since the 20's.
  Over the same period, soybean prices have risen over 32%, to over $12/bu.
  Earlier this year, Russia announced a ban on wheat exports due to a wheat harvest severely damaged by drought. Wheat prices jumped and today December 2011 wheat is trading above $8.20/bu.
  However, corn remains the bell weather crop for phosphate demand, and corn is short and corn prices are very strong, having risen almost 34% since early July. In mid-summer, December 2011 corn was trading around $4.10 per bushel. Falling estimates of world production and predictions of lower stocks-to-use ratios have since led to a surge in corn pricing. This week, December 2011 corn has been trading around $5.50 per bushel. At these current price levels, farming economics provide strong incentive for high planting acreage and fertilization for maximum yields.

- With a huge 2010/2011 corn harvest and high corn prices, farmers should have money to spend on their next crop. USDA has forecast net farm income of $77.1 billion for 2010. If achieved, that level of income will approach historical highs.

- The supply/demand picture remains tight, both from an international and domestic perspective.

  In China, phosphate demand is strong and prices are on the rise. There has been much speculation as of late that the Chinese government may soon take action to limit DAP exports in order to ensure adequate domestic supplies.

  In the U.S., producers seem to be comfortable with their current inventory positions, and the domestic pipeline, currently very thin, is expected to be essentially exhausted at the end of the fall season. One domestic producer is expected to cease production soon, while others may find production constrained by limitations on phosphate rock and/or sulfur availability.

Again and in summary, we are optimistic regarding demand and pricing as we look through the fourth quarter and beyond.

Briefly, regarding input costs:

The ammonia market has been firm for several months and we have seen month-to-month price increases since the beginning of the third quarter. Since July, ammonia has risen from $355 per metric ton U.S. Gulf to current prices in the range of $465 to $470. However, going into December and on into the first quarter of 2011, there is the expectation of subtle softening, by perhaps as much as $25 to $40 per metric ton.

Regarding sulfur, demand is strong and supply is tight. From the third quarter to the fourth, the Tampa molten sulfur posting increased from $95 per long ton to $160 per long ton. Demand is expected to continue strong with no supply relief in the near term. Thus, suppliers may very well push for yet another price hike going into first quarter of 2011.

I'll now turn the discussion over to Tim Cantrell for a review of Q3 operating results.

Tim Cantrell: Thanks, Jim.

I would like to briefly point out a few highlights from our third quarter 2010 operating results. As Robert stated, the third quarter of 2010 represented a marked improvement from our second quarter 2010 results. During this quarter, we had total sales of $70.4 million; of which $69.4 million represented DAP sales on approximately 152,500 tons of DAP sold. Our average sales price for the third quarter of 2010 was approximately $455 per short ton, a 13.8 percent increase over second quarter 2010 average sales price, and a 70 percent increase from the prior-year period average sales price.

In the third quarter of 2010, we had a gross margin of $5.1 million or 7.2 percent of sales. We produced approximately 156,000 short tons of DAP in the third quarter of 2010.

Robert previously mentioned the production issues in our sulfuric acid plant and the impact on downstream production of phosphoric acid and DAP. With the substantial majority of our costs fixed, production shortfalls have a significant impact on our margins. During the quarter, we experienced a $1.6 million improvement in our cash outlays for conversion and water treatment costs over second quarter 2010 levels. Additionally, we purchased nearly $1.2 million in sulfuric acid in an attempt to augment lost DAP production. Margins realized on DAP produced from purchased sulfuric acid are lower than margins realized on internally manufactured sulfuric acid.

Moving on, SG&A expenses for the third quarter of 2010 were $1.6 million, or 2.3 percent of net sales.

During the third quarter of 2010, we expensed approximately $0.3 million related to environmental matters. At quarter end, we anticipated incurring an additional $2.4 million in capital costs to further address the EPA's 7003 Administrative Order and the MDEQ's Notice of Violation issued last September. However, I would caution that estimates attributable to addressing our environmental matters are subject to on-going evaluation and, will likely, be subject to change.

During the third quarter, we settled a pending claim against a contractor's excess insurance carrier related to a 2007 boiler repair. We collected and recorded net litigation recoveries of $750,000.

For the third quarter ended September 30, 2010, we had an operating income of $3.9 million and net income of approximately $2.5 million.

EBITDA for the third quarter of 2010 was $7.3 million, an $11.9 million improvement of Q2 EBITDA.

Capital expenditures for the quarter were approximately $1.4 million and were $5.9 million year to date. We anticipate capital expenditures of approximately $3.9 million during the fourth quarter of 2010, largely related to our current turnaround.

Now, let me briefly address our liquidity position.

Cash flow provided by operations for the third quarter ended September 30, 2010 approximated $1.9 million and we ended the quarter with approximately $3.6 million in cash and had $9.3 million in borrowings under our revolving credit facility. Presently, we have approximately $2.4 million in cash on hand and outstanding borrowings of $11.5 million. Our liquidity position requires and receives our constant attention. As Ed McCraw will address, we are spending a significant amount on this turnaround. Our near-term liquidity could be severely strained if we do not see marked improvement in our DAP production volumes. Thus, it is imperative we complete the turnaround on time and on budget.

Now, I would like to turn the presentation over to Ed McCraw, our Chief Operating Officer, for a few comments.

Ed McCraw: Thank you, Tim.

In the third quarter, we produced 187,000 tons of sulfuric acid or approximately 77 percent of planned production. This, of course, had a negative impact on DAP production, which was partially offset by DAP produced with purchased sulfuric acid. DAP production for the quarter was approximately 156,000 tons.

The single most significant issue that negatively impacted sulfuric acid production was the reduction in the maximum, instantaneous rate the plant could achieve as a result of the catalyst damage associated with the failure of the waste heat boiler that occurred in June of this year.

The operating factors for the No. 2 and No. 3 sulfuric acid plants were 86 and 90 percent, respectively, versus a target of 92 percent. The most significant events that impacted sulfuric acid operating factors during the quarter were, <u>first</u>, scheduled outages to install the rebuilt coolers that we discussed in our second quarter earnings call, <u>second</u>, leaks in the vestibule area of the waste heat boiler in the No. 3 sulfuric acid plant, and <u>third</u>, high vibration in the main turbine of the No. 2 sulfuric acid plant, which was caused by the improper installation of a bearing by an outside contractor.

On November 1, we began an extensive maintenance turnaround, which will address all known issues in the No. 3 sulfuric acid plant (including those I just mentioned), as well as the phosphoric acid and DAP plants. The No. 2 sulfuric acid plant will require a short outage after the No. 3 plant returns to service to correct an issue in one of the heat exchangers.

The No. 3 plant outage was scheduled for 18 days and the plant is expected to return to production on November 18. The phosphoric acid and DAP outages lasted about a week and those plants have resumed production. (Comment on how they seem to be operating.)

We are replacing one of the four digesters in the phosphoric acid plant. Replacing this major piece of equipment will take the rest of the month of November and we will operate at somewhat reduced rates until that work is completed.

This is a very extensive maintenance turnaround. As we said, all known issues are being addressed, our planned expenditures, at approximately $6.5 million, are more than double those for a typical turnaround because of the additional capital work that we are performing and we are optimistic that production rates will improve as a result of our efforts. Robert?

Robert Jones: Hi, Ted. And at this point we will be glad to entertain any questions that you may have.

Operator: Thank you, ladies and gentlemen. If you have a question at this time please press star than one on your touchtone keypad. If your question has been answered or you wish to remove yourself from the queue you may press the pound key. Again ladies and gentlemen if you have a question please press star than one on your touch tone telephone at this time. One moment for the first question.

All right, our first question comes from (Steven Gidumal) of (Choice Capital).

Robert Jones: Hello, (Steve).

(Steven Gidumal): Hey, Robert, you guys can hear me OK?

Robert Jones: Yes, very fine.

(Steven Gidumal): OK, so, I think I understood most of the presentation. I guess the one question I have is probably the question everyone has got is, you know, what's the level of confidence on doing the, you know, completing all the work all this month, and then, you know, do you feel, you know, can you just say a few more words about, you know, how you guys have scoped it out engineering-wise and your confidence level and is this fairly routine, you know, repair or was there something of a technology jump that we had to deal with that should, you know, have everybody holding their breath.

I mean it's, you know, we obviously want to get this plant back and running.

Robert Jones: Well absolutely. And so do we; I can tell you that without question we are not pushing the state of the art. The turnaround is really unique in its expanded scope but not – not in its difficulty.

One thing that we – at least partially accomplished with the other plant is after an extended review of our sulfuric acid plants, we identified the areas that were causing the most downtime. And we developed plans to address those. And at the first plant they were successfully addressed and the fixes that we implemented have proven out and worked well. We're now doing that in the second plant.

Overall confidence level, we believe that we'll come in on budget, that we'll finish the turnaround in time and that we'll achieve the targeted results which are substantially improved operating rates.

(Steven Gidumal): This is just to follow it up. Is it – will that lead us then to have a production budget I guess for Q1 and then, you know, certainly for Q2 of next year, you know, in the 175 to 180 range?

Robert Jones: We think our target, certainly in December, will be close to 2,000 tons per day. That's a good target. Looking ahead, given the age of the plants, this problem is not going to go away. I mean this turnaround is not magic, it's going to restore operating rates but we're hopeful that we'll achieve in the range of 60 per month going forward.

(Steven Gidumal): OK.

Robert Jones: And at this, as Ed mentioned earlier, we are addressing everything in these plants that we know about and, certainly we believe we know about everything that's impacting our production.

(Steven Gidumal): OK, and in this pricing environment with the – you know, the dynamics of where ammonia is and where sulfuric acid is, how much you should be able to now make on your own versus having to buy plus, you know, the pricing, the very positive price environment for DAP, I'm sorry, I might have missed that, is it still 450, is that what you're thinking now for DAP?

Robert Jones: No, DAP today is mid 560s per short ton, FOB NOLA, and the export price per metric ton is ranging between 575 and 580. And there's good liquidity in the export market at those levels and there's still liquidity in the domestic market although we are moving into a traditionally slow period.

(Steven Gidumal): Right, and you're expecting – you're hoping those prices or expecting those price to hold up in Q1 and Q2?

Robert Jones: Well, that's the current expectation and really, primarily driven by very strong fundamentals in market conditions and grain markets, and the positive outlook for – or the absolute need to plant a lot of acres of corn next year to just keep up and to have some semblance of ending stocks.

(Steven Gidumal): And you'll probably get that extra demand prices from dealers too that will pull through.

Robert Jones: Pardon, I'm sorry?

(Steven Gidumal): The dealers will probably pull in and build inventory on top of all that.

Robert James: Well, they're not building yet, that's been the amazing thing. We've had an incredibly strong fall season. And one thing, I'm not looking for trouble but, you can always cannibalize your spring with a very, very good fall but it's been my experience in the past that when we have a good fall we have a good spring.

(Steven Gidumal): Right.

Robert James: You know, something spoils every party; but in this particular case I don't think the troublemaker is going to be grain markets. So, the Ag output fundamentals certainly look strong for the near term.

(Steven Gidumal): So with these dynamics of the sulfur and the ammonia and then obviously with DAP pricing the margin should be pretty good I would right if you can get back to, you know, 175 to 180 a quarter. Is that what you think?

Robert James: Well, today, and in recent months, the upward movement in sulfur and ammonia prices has not kept pace with the rise in DAP prices but you must recall that our phosphate rock pricing is sensitive to changes in market conditions, but all that being said, our outlook is positive.

(Steven Gidumal): Great. And with respect to the liquidity I'm not – and maybe I missed this but how much availability you have now?

Robert James: As of today? Or, I mean, quite frankly as of this morning I don't know.

Tim Cantrell: Approximately $3.5 million of availability in our revolver.

(Steven Gidumal): It's like 3.5 million?

Tim Cantrell: Three and a half million, of course, we have about another 2.5 million in cash right now.

(Steven Gidumal): That's great, OK.

Robert Jones: But that should begin growing as the plant's come back online.

(Steven Gidumal): OK. OK, so that's...

Robert James: I don't but as we mentioned earlier we need to complete this maintenance turnaround on time, with the cost allowed and it needs to work.

(Steven Gidumal): Right. OK, great, I'll let (inaudible) ask some questions.

Robert James: All right, thank you, Steve.

Jim Perkins: Thanks, (Steve).

Operator: Our next question comes from David Silver with Bank of America Merrill Lynch.

David Silver: Yes, hi guys, how are you doing?

Robert Jones: Hi, Dave.

David Silver: I have a couple of questions. The first question maybe on the sulfur side, you know, I heard the earlier comments and I know that sulfur prices are up but I just wanted to check with you on availability.

So in other words are you able to procure the, you know, the sulfur that you think you need this quarter. Are there any issues if you needed sulfuric acid? Do you think that that's available to you? So kind of availability question more than the absolute price?

Robert Jones: Well, first of all sulfur is extremely tight as Jim mentioned. We currently have adequate sources of purchased sulfuric acid to meet our expected demand for the balance of the year, in addition we've arranged for supplies during the first half of 2011, but let me ask Jim to further elaborate on sulfur availability and what he's seeing moving forward.

Jim Perkins: In our geographic area, we procure from a number of sources, some refinery source, some sour gas field source. The refinery run rates are such that there have been some availability impacts there so we've had to go to some alternative sources or may have to make up the difference. But there does not appear to be a problem with an adequate supply, the mix may change somewhat but the supply is there.

But even when our acid plants are running at full rates from time to time there's an opportunity to make even more DAP if we have additional purchased sulfuric acid available and we're carrying inventories of acid today. We have additional sulfuric acid at favorable rates lined up all the way through June 30 of next year.

David Silver: OK. And then, I had a marketing question I guess for Jim and this is kind of – there's a lot of moving parts in the market. You identified a lot of positive factors but, you know, you are, I think you are trying – it sounds like you're trying to be cautious with your sales commitments right now until, you know, maybe the mechanical reliability of your unit is a little bit better.

So can you just talk about a couple of things but just, you know, how do you market in an environment like this? I mean, do you limit your commitments in terms of timing. I mean, are you going out a couple of months or are you trying to just, you know, guarantee that any commitment you make can be – you know, you can fulfill – you know, it's a tight market overall but, you know, I'm looking at your inventory balance of about $27 million here, I'm just trying to figure out how much availability, you know, you think you have here and how do you handle your marketing in this, you know, tight market for the market where maybe there's some uncertainty over exactly how hard you can run this quarter?

Jim Perkins: I think Robert would like to speak to that and I'll back him up if need be.

Robert Jones: Well, (David), our philosophy has been and it serves us well. We make it and we sell it. And, we don’t play inventory levels to try to have that to our benefit. We sell as we produce the product. The vast majority of our products are sold under contract that provide for prompt deliveries upon production of the product.

David Silver: OK. One other question, I think in Jim's prepared remark he mentioned another supplier that may have to halt production pretty soon. Do you have a sense of when that might occur, in other words if you've gotten inquiries from maybe some of these producers, particular producers, and customers looking for alternate sources of supply from you, I mean, any kind of insight on exactly when that competitor may have to halt production?

Robert Jones: (David), they are rampant rumors, but I'm prepared to say we all read the same publications and all see the same projections of that plant ceasing production sometime in the first quarter and that continues to be our expectation.

David Silver: OK, very good. Thanks, guys, I appreciate it.

Robert Jones: (David) before you leave let me ask you a question. Did you agree with our analysis of the outlook for having outputs? (Inaudible).

David Silver: You know, I mean, I generally agree with everything you say and, you know, if you'll look at it on a daily basis where crop prices are, where the supply and demand seems to be from the domestic market. I mean, you know, it's a little crazy, I guess, from my perspective, or not crazy, that's a little unusual here because we're getting imports into the U.S. market, right? And, you know, that speaks to a tight market, well priced market right there as well.

I guess the one thing – so I get paid to worry about stuff that might not happen but might. And, you know, it's just interesting but I wonder if you guys have an opinion, I actually am a little worried that crop prices might be a little too strong here, you know. I mean I would be more comfortable with corn, you know, closer to $5 rather than $6, that to me personally, you know.

So I don't know if that's affecting exports or, you know, if it leads to some severe demand destruction down the road. But, you know, I'd have to say on a scale of one to ten you're at about 9.9 kind of rate here.

Robert Jones: OK, I find it interesting.

David Silver: (OK).

Robert Jones: Next question?

Operator: Our next question comes from Charlie Antrim with SAC Capital.

Charlie Antrim: Hey good afternoon and thanks for taking my question. Most of – actually most of my questions have been answered. But just so I'm clear is it safe to assume that your (inaudible) from that upside are going to be on the spot?

Robert Jones: Yes.

Charlie Antrim: Yes. And then no issues with regard to phosphate rock. I mean, I think you guys have had strategic relationships in the past that have (inaudible) this year but I just want to check that box as well.

Robert Jones: We've been dealing with the same rock supplier for many, many years and I don't think we've ever lost a ton of production because we didn't have rock.

Charlie Antrim: OK. And you said the specific date, I may have missed it but the date you expect to completely come out of the turnaround, at least a target date I should say?

Robert Jones: The sulfuric acid plants should both be back up and operational on the 18th of this month. Thereafter, we'll have short outage of one of the plants for four days, but it will occur within the month of November and, as Ed mentioned, after the completion of the replacement of the digester in the phos acid plant, we should be fully back on stream by the end of November. So, we should start December with the full effects of our turnaround.

Charlie Antrim: Great. Thanks very much.

Operator: Again ladies and gentlemen if you have a question please press star than one on your touchtone telephone.

I'm not showing any other question in the queue at this time.

Robert Jones: All right, well, now let me sum things up by letting everyone know that, we're not content with our third quarter. It could have been better. And it should have been better, but at the same time, we are satisfied that the hand that we were dealt was well played, confronted with the deteriorating production rates, the instantaneous rates throughout the quarter.

Our people did a good job of keeping the plants online. We also did a good job of controlling our cost and those efforts together with an accommodating market enabled us to produce the results that we were able to register.

I'd like to thank everyone again for joining us and we appreciate your interest in our company.

Thank you.

Operator: Ladies and gentlemen thank you for your participation in today's conference. This does conclude the conference, you may now disconnect. Good day.

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