

Chemoil will complete the seven-fold expansion of another storage terminal in Fujairah, the United Arab Emirates, to 675,000 cum by 3Q2012



PICTURES: CHEMOIL ENERGY

Fuelling GROWTH

Chemoil Energy has been whipsawed by volatile oil prices and slumping demand for marine fuel. Now, its new CEO Tom Reilly is leading the company into the aviation fuel business. Will that deliver the steady margins that have eluded it for years?

| BY KANG WAN CHERN |

It's early on a Wednesday morning in Singapore but Tom Reilly is already at his desk, replying emails and scrutinising reports. The CEO of marine fuel trader and supplier Chemoil Energy oversees operations that span at least three time zones, and acting quickly is the key to seizing opportunities, staying competitive and maximising profits.

Chemoil mainly supplies and delivers fuel by acquiring, developing and controlling physical infrastructure along key segments of the supply chain. Ensuring that each link in the marine fuel supply-chain is functioning optimally is essential to staying profitable in an industry known for its volatility. "In this business, it's very important to understand that each group along the supply chain — from the physical buying and trading of fuel to logistics, storage and risk management — is linked. And, if one group falls, it affects our entire profitability," says

Reilly, during a recent interview with *The Edge Singapore*.

To be sure, there hasn't been a dull moment for US-born Reilly since he took the helm of Chemoil in January, amid one of the toughest times in the marine fuel industry. A significant part of Chemoil's business is sourcing, moving, blending and storing marine fuel before selling it to customers in the shipping industry. But as shipping floundered, so too did demand for marine fuel needed to power the ships. The result was enormous volatility for Chemoil. After reporting earnings of US\$12 million (\$14.98 million) in 2009 from losses the year before, Chemoil slumped back into the red in 2010 as costs skyrocketed. The company's shares have fared no better, fluctuating from a high of 56.5 US cents each, to lows of 19 US cents over the past three years.

Now, Reilly has come up with a strategy to shield Chemoil from the volatility of the shipping industry and attract investors back on board. The key plank in his game

plan is diversification. In September, Chemoil said it would expand into the 65-billion-gallon-a-year aviation fuel market with its first marketing and supply office located in Fort Lauderdale, Florida. At its initial stage, the new division — Chemoil Aviation — will focus on supplying fuel to mid-sized commercial airlines, including passenger, cargo and chartered aircraft operators as well as corporate carriers.

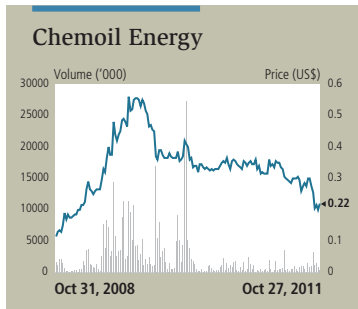
"We have a great trading, supply and distribution platform and great skill sets, so we should use it to diversify into other growth areas such as aviation fuel and biodiesels to minimise the swings in marine fuel prices," Reilly explains.

Marine fuel is blended from residuals left over from the crude-oil refining process. "Our costs are very susceptible to movements in oil prices," says Reilly. "If oil prices go up, fuel prices go up, and that represents acute stress for shippers who are getting hit on their largest costs when freight rates are already low." That usually results in late pay-

ments or defaults from shippers, which in turn translates into additional finance costs for Chemoil.

In fact, it was Chemoil's quest to gain better control over its marine fuel margins that resulted in Reilly joining the company. In January, it acquired marine fuel trader OceanConnect Holdings for US\$25 million, extending its presence into the US, the UK, the Middle East, Japan and Denmark. As part of the deal, Reilly, who was CEO of OceanConnect, moved to replace Chemoil's former CEO Clyde Michael Bandy, who had stepped up to helm the company when its founder, Robert Chandran, was killed in a helicopter crash in 2008.

The new CEO isn't promising a quick turnaround in profitability at Chemoil's marine fuel business, though. "Times are tough for our customers in shipping, which presents challenges for us. You can't have a healthy marine fuel industry with a sick shipping industry," says Reilly, who holds a doctorate in law and a postgraduate degree in environmental law. He



was previously also vice-president at Fuel and Marine Marketing LLC — a Texaco and Chevron joint venture — where he took charge of bunkering and fuel trading in the Pacific Rim and Middle East regions.

“That’s why we are diversifying and expanding amid the volatility,” says Reilly. “We are building the company up in such a way that if one part of the business faces difficulty, we can still excel in others and offset losses. This is how we can take the volatility out of our bottom line and grow.”

But it could be some time before Reilly’s plans to propel the new businesses forward have an impact on the company’s bottom line, especially with Chemoil’s bleeding core marine fuel business still forming a significant part of the company. Indeed, Reilly has no illusions about the enormity of the challenge that he faces in refashioning Chemoil into a company that’s capable of delivering steady profitability and sustainable growth. For one thing, the high cost of maintaining Chemoil’s assets such as storage tanks and barges at certain bunker ports has hampered the company’s ability to stay financially nimble in the face of volatile demand over the past few years.

“Chemoil has gone through tremendous change, from uncertainty in the ownership structure to one that was drifting without proper direction,” Reilly notes. “The companies that do well in this industry are those that are able to react to changes quickly and reduce costs when growth plans are no longer sustainable. If you are with high fixed costs, you will get run over like we have in certain areas.”

Repairing the bottom line

Fortunately, Reilly isn’t without a plan to free the company from the shackles of unnecessary high fixed costs. Since coming on board, he has struck off at least four dormant subsidiaries to save costs and achieve better efficiencies. On Sept 18, he sold Chemoil’s 50% stake in IPC USA — which distributes gasoline and diesel fuel to gas stations in the US — to Japanese conglomerate **Itochu Corp**, freeing up US\$20.75 million in funds.

Chemoil’s ownership structure has also stabilised over the years. In 2009, Swiss commodities supply chain manager **Glencore International plc** bought the Chandran family’s 50.8% stake in Chemoil for \$233.3 million and now holds a 51.5% stake in the company. That has also helped bring some measure of earnings visibility to the company. In March, Glencore renewed an agreement with Chemoil under which Glencore would be given preferential sales of marine fuel by Chemoil. Separately, Itochu controls a further 37.5% in Chemoil.

Reilly has also been spending a lot of time recruiting employees into the Chemoil fold. Since coming onboard, he has hired up to 118 people to man the ranks along each major link in the supply chain, while at least 45 have left the company. “Having the right people with the correct mindset and skills is a decisive factor for success in our business,” says Reilly, who has been expanding his trading and risk-management team as well as replacing key personnel in other departments



Chemoil owns marine fuel supply and storage facilities in Rotterdam, Europe’s largest bunkering port

such as credit and collections.

“Our business is made up of different business units and everyone must understand how all the links fit,” he says. “The chain at every level has to perform well or we don’t make any money.” For instance, a junior trader who undersells fuel could wipe out a large portion of the company’s profits. Similarly, a credit officer’s failure to evaluate a customer’s credit worthiness could jeopardise profits by selling to a shipowner who defaults or pays late, saddling the company with unnecessary finance costs. “But if we have people of the right calibre, we stand to make a lot of money,” Reilly adds.

While these strategic moves have kept Reilly busy, it hasn’t stopped him from finding the time for more mundane tasks such as overhauling the company’s internal IT systems to ensure information is accurate across the board. “Putting in new IT systems may not be interesting but it is critical for our success,” he says. “It is all part of restructuring the company and fixing what’s not working in the marine fuel business and the consequence is that we’ve had a pretty good year so far.”



BRIAN TAVILLE/THE EDGE SINGAPORE

For the six months to June 30, 2011, Chemoil reported a 43.8% y-o-y improvement in revenues to US\$5.2 billion, and earnings of US\$24.3 million versus a loss of US\$11.5 million in 1H2010. Gross contribution per tonne, the company’s key margin indicator, climbed to US\$10.6 per tonne for 1H2011. Sales volume was up 15% y-o-y to 8.9 million tonnes during the period. This year, Chemoil is aiming to increase bunker volume sales by up to 54% to 24 million tonnes, from 15.5 million tonnes the year before.

Strong balance sheet

With the cost savings expected over the next few quarters, Reilly isn’t ruling out another acquisition or two to speed up growth and better position the company against its rivals. Indeed, competition is already heating up in the bunkering industry, with Itochu taking up new capacity on Jurong Island and PetroChina eyeing storage facilities in Fujairah, the United Arab Emirates. Meanwhile, Indian state-owned refiner Bharat Petroleum Corp has begun offering bunker fuels at the port of Kandla, in the western Indian state of Gujarat, where Chemoil also oper-

ates supply facilities.

“We have to be very careful with acquisitions,” Reilly says. “If the takeover target is overpriced, it will take a long time to make that money back for the company in this environment.” However, the good news is that Chemoil’s existing infrastructure has “very little loans on them”, making it easier for the company to fund new acquisitions, he adds. “We have some very strong assets worth hundreds of millions in financing at our disposal. We have no issues when it comes to funding our growth plans.”

Indeed, Chemoil has the largest share of the marine fuel market in Los Angeles, New York and Panama. It is currently among the largest suppliers of marine fuel in Singapore. Its largest storage facility here, the Helios terminal, which can store up to 450,000 cu m of fuel, is located on Jurong Island. Meanwhile, Chemoil will complete the seven-fold expansion of another storage terminal in Fujairah to 675,000 cu m by 3Q2012. Chemoil also operates marine fuel facilities in Rotterdam, Europe’s largest bunkering port. And it operates a fleet of barges, which are used to transport oil from its suppliers to its ports.

Shares of Chemoil closed Oct 27 at 22 US cents apiece, down 35% since the start of the year. At those levels, it is trading at 11 times earnings and has a market capitalisation of US\$285 million. It has no active analyst coverage at the moment.

Yet, that might change if Reilly succeeds in improving Chemoil’s margins. “What’s important is that we have a plan, the benefit of a new team and solid shareholder backing as a foundation on which to build sustainable profits for the company,” he says. “We are not interested in being the biggest volume player as much as we are interested in growing our margins and being a profitable company.”

And he’s wasting no time in driving those plans forward. As he wraps up his interview with *The Edge Singapore*, he immediately begins preparing for a conference call with Chemoil’s senior executives around the globe. **E**

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