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The Chemours Co. (CC)

Q2 2018 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Lisa, and I'll be your conference operator today. At this time I would like to welcome everyone to The Chemours Company Q2 2018 Earnings Conference Call. All lines have been placed on mute to prevent any background noise. After the speaker's remarks, there will be a question-and-answer session. [Operator Instructions] Thank you.

Jonathan Lock, VP Corporate Development and Investor Relations. You may begin your conference.

Jonathan S. Lock

VP-Corporate Development & Investor Relations, The Chemours Co.

Thank you, and good morning, everyone. Welcome to The Chemours Company's second quarter 2018 earnings conference call. I'm joined today by Mark Vergnano, President and Chief Executive Officer and Mark Newman, Senior Vice President and Chief Financial Officer. Before we start, I'd like to remind you that comments on this call, as well as the supplemental information provided in our presentation and on our website contain forward-looking statements that involve risks and uncertainties, including those described in the documents Chemours has filed with the SEC.

These forward-looking statements are not guarantees of future performance and are based on certain assumptions and expectations of future events that may not be realized. Actual results may differ and Chemours undertakes no duty to update any forward-looking statements as a result of future developments or new information.

During the course of this call, management will refer to certain non-GAAP financial measures that we believe are useful to investors evaluating the company's performance. A reconciliation of non-GAAP terms and adjustments are included in our release and at the end of this presentation.

I will now turn the call over to Mark Vergnano, who will review the highlights from the second quarter. Mark?

Mark P. Vergnano

President, Chief Executive Officer & Director, The Chemours Co.

Thanks, Jonathan. Good morning, everyone, and thank you for joining us today.

Q2 2018 was another solid quarter for Chemours as our teams continue to execute and build upon the strong start to the year we reported last quarter. We delivered year-over-year gains on each of our key financial metrics, an achievement I am particularly proud of given the strong results from the same period a year ago. Not only did our overall adjusted EBITDA increased by 38%, we also delivered double-digit earnings growth across all our segments, led by momentum in Opteon refrigerants and the strength of our Ti-Pure titanium dioxide franchise.

We also completed the $500 million share repurchase plan announced at our December Investor Day, well ahead of the 2020 authorization timeline. Following the completion of that authorization, our board of directors has approved a new $750 million share repurchase plan through 2020 and an increase to The Chemours dividend of 47% from $0.17 per share to $0.25 per share. Mark Newman will speak to these two programs in more detail shortly, but taken together they are a tangible representation of our commitment to return meaningful capital to our investors over time.

This quarter marks another strong chapter in the history of Chemours. Looking ahead for the full year, we expect to deliver adjusted EBITDA in the top end of our guidance range of $1.7 billion to $1.85 billion with adjusted EPS of between $5 and $5.75 per share as well as free cash flow greater than $700 million. We also remain confident in our ability to meet or exceed our three-year financial targets.

I'll now turn the call over to Mark Newman to cover our second quarter financial details.

Mark E. Newman

Chief Financial Officer & Senior Vice President, The Chemours Co.

Thanks, Mark. I'll start by turning to slide 4. As Mark mentioned, the second quarter built upon the momentum from earlier this year resulting in higher revenue and adjusted EBITDA for all our segments. Net sales rose by $228 million or 14% from the same period a year ago with our two largest segments delivering double-digit revenue growth.

In comparison to last year's second quarter, GAAP net income grew roughly 75% and over 90% on an adjusted basis. This drove similar year-over-year increases in EPS and adjusted EPS of 82% and 99% respectively.

Adjusted EBITDA of $497 million increased 38% while our adjusted EBITDA margin expended nearly 500 basis points year-over-year to 27.4%. Despite the normal seasonal use of cash and approximately $90 million in cash interest payments, we generated over $200 million in free cash flow driven by our strong operating performance. We also continue to invest in our portfolio through high return projects resulting in a pre-tax ROIC of 42% this quarter.

Turning to the next slide, let's review our adjusted EBITDA performance. Higher global average selling prices of Ti-Pure titanium dioxide and increased price across all businesses in our fluoroproduct products segment delivered over $140 million of adjusted EBITDA growth year-over-year. Volume added $31 million, reflecting solid demand for Opteon refrigerant and chemical solutions products. Currency was a modest benefit in the quarter, providing an additional $26 million, in comparison to last year's second quarter.

We incurred higher variable cost, including distribution, raw materials and process water treatment costs at our Fayetteville facility, which partially offset some of the price and volume gains achieved. In total, we achieved $136 million improvement to adjusted EBITDA for the second quarter of 2018.

Moving to the adjusted EPS bridge on slide 6, you will recall we added this chart in Q1 to align with our 2018 and three-year targets. We continued the momentum built during the first quarter with adjusted EPS nearly doubling to $1.71 per share.

Our improved operating earnings drove the majority of the improvement, with a small tailwind from tax-related items of $0.04 per share. Our effective tax rate in the quarter was 13% versus 28% for last year's second quarter, reflecting our geographic mix of earnings, the impact of discrete items and the impact of U.S. tax reform.

The impact of our share repurchases contributed $0.07 per share. We expect the benefit of share repurchases completed in the first half of 2018 to become more meaningful in future quarters. The delta between adjusted EPS of $1.71 and GAAP EPS of $1.53 can largely be attributed to cost related to our refinancing during the quarter, which I'll now cover in more detail on the next slide.

On slide 7, you'll see that we continued to benefit from the flexibility that our balance sheet provides. We ended the first half of 2018 with a cash balance of approximately $1.2 billion, utilizing our cash position to return additional capital to shareholders, strengthen our balance sheet and reinvest to drive organic growth.

We are confident that these three investments will create value for our shareholders near and long-term. Second quarter net operating cash flow of $343 million was primarily driven by strong business results in the quarter, including $91 billion of cash interest payments and a $44 million increase in working capital. Free cash flow improved over $100 million versus last year's second quarter, even with increased capital expenditures versus last year.

We completed our $500 million share repurchase authorization during the quarter, repurchasing approximately $140 million of shares during Q2. In total, our authorization allowed us to repurchase over 10 million shares since its inception in December, reducing our total share count by approximately 5%.

Additionally, we continue to enhance our liquidity while adding flexibility to our company's balance sheet. During the quarter, we raised €450 million through senior unsecured notes. The proceeds were used to fully redeem our existing euro 2023 notes as well as a portion of our U.S. dollar 2023 notes. These transactions resulted in a debt extinguishment payment of approximately $29 million with an expected reduction in interest expense of approximately $16 million annually. Including the new credit facility we announced in last quarter's call, we expect to realize approximately $28 million of interest savings annually.

Our total liquidity is approximately $2 billion as of June 30 taking into account our $800 million senior secured revolving credit facility. Our net debt now stands at approximately $2.8 billion which translates into a net leverage ratio of approximately 1.6 times on a trailing 12-month basis.

One of the things that we have consistently said as a company is that our capital allocation strategy would include meaningful return of capital to shareholders over time through both share repurchases and dividends.

As you just heard from Mark, our board of directors increased the dividend for next quarter by 47% and authorized a new $750 million share purchase plan. The new dividend reflects our confidence and our ability to execute on Ti-Pure Value Stabilization while growing each of our businesses through investment in high return projects. It also reflects the long-term durability of the cash flows we can generate as a company with Ti-Pure TiO_2, Opteon refrigerants and fluoropolymers products leading the way.

Following the completion of our previous $500 million share purchase plan, our board has approved a new and larger program. The new share repurchase authorization of $750 million is valid through 2020. Given these two announcements, we now expect to return the majority of our free cash flow to shareholders through 2020. A new share repurchase plan and dividend increase demonstrates the board's confidence in the sustainability of our company's earning power and belief in our long-term value potential of our stock. From this point forward, we would expect to revisit our dividend on more of an annual basis.

And now with that, I'll turn the call back to Mark to review our segment results.

Mark P. Vergnano

President, Chief Executive Officer & Director, The Chemours Co.

Thanks, Mark. Beginning with fluoroproducts on the next slide, sales in the quarter rose 13% to over $800 million. Opteon continues to be a growth engine for fluoroproducts while the entire segment benefited from higher average selling prices in the quarter. Adjusted EBITDA of $230 million improved 17% as adjusted EBITDA margin grew to approximately 29%. The cost of temporary process water treatment as well as higher maintenance and distribution costs partially offset our double-digit revenue growth.

I want to provide a bit more color on the temporary process water treatment costs at Fayetteville which are impacting results in the fluoroproducts segment. For the full year 2018, we expect to spend approximately $35 million related to process water treatment at our Fayetteville facility in addition to associated remediation and legal costs. We believe that these expenses will decrease once the permanent abatement technologies are installed by the end of 2019. The adjusted EBITDA margins on this slide include the portion of these expenses which were incurred in the second quarter.

Let's review the fluoroproducts performance drivers in the quarter in more detail. Within Opteon refrigerant, this transition to our low global warming HFO technology continues in both the EU and the U.S. This quarter higher prices for our low-GWP stationary blends, more than offset the impact of contractual price reductions for mobile air conditioning. Our base refrigerant volume reflects phase downs of HFCs and conversion to Opteon blends within the EU as well as some impact from a seasonally cooler spring. This was partially offset by added volume from our acquisition of ICOR last quarter. At the same time, we saw prices on base refrigerants also move higher in Europe. In total, base refrigerant revenue is flat on a year-over-year basis.

Shifting now to fluoropolymers, Q2 revenue and profitability benefited from previously announced price increases. Demand for our fluoropolymer products remain strong, with some product lines sold out. Due to supply constraints, volume was slightly lower in comparison to last year.

Looking ahead to the full year, we remain optimistic in our ability to support our customers through the transition toward low GWP for refrigerants. Given robust demand in the first half, we now expect the Opteon top line growth of nearly 30% in 2018 driven by increased adoption of Opteon blends for stationary refrigeration in the EU and continued conversion within the U.S. mobile air conditioning market.

On the polymer side, we anticipate GDP-like volume growth, given our supply constraints, along with moderate price improvement. As we implement our application development strategy, we expect a larger percentage of our volume to come from our higher margin fluoropolymer product lines. The unique characteristics of our fluoropolymer products make them ideally suited for use in demanding applications, including automotive, consumer electronics and energy storage.

Moving to our chemical solutions segment on the next slide. We generated $153 million of sales in the quarter, a 3% year-over-year improvement. Second quarter adjusted EBITDA of $16 million more than doubled in comparison to last year, a result of higher volume for most product lines and lower costs. Demand for Mining Solutions products remains strong and we expect that to remain the case throughout the rest of 2018.

Performance chemicals and intermediates saw increased demand in the quarter across most product lines, while price was slightly lower on a year-over-year basis. During the quarter, we announced price increases across a number of our product line, including methylamines, glycolic acid, Vazo products and sodium cyanide. We expect to realize some impact from these price increases towards the end of this year and into 2019.

As a reminder, the construction of our Mining Solutions facility in Laguna, Mexico remains suspended. Our current Mining Solutions facility is sold out and we expect it to remain so given the strong demand in the Americas.

Turning to slide 11, to review our titanium technologies segment. Sales increased 18% to $862 million versus last year's second quarter, driven by higher global average prices for Ti-Pure titanium dioxide, up 16% year-over-year.

We recently communicated price increases to customers who have not signed Ti-Pure Value Stabilization contract. Because the price increases only apply to those who do not have Value Stabilization contracts, we anticipate modest impacts in the fourth quarter.

Volume in the quarter came in slightly lower when compared to a very strong second quarter of 2017. We believe that our customers have begun reducing their TiO2 inventory levels built over 2017 as a result of our stabilizing prices. This is entirely consistent with our expectation as we implement our Ti-Pure Value Stabilization strategy. Adjusted EBITDA improved 53% to $295 million when compared to last year's second quarter, translating into nearly 800 basis points of margin expansion. Higher global average prices were partially offset by increased raw material and freight and logistics costs on a year-over-year basis.

Looking at the full year, we expect 2018 annual volume to be consistent with 2017, which was up 8% versus 2016 as customers adjust to our Ti-Pure Value Stabilization framework. As a result, we are utilizing our facilities at a rate consistent with our customer's demand. We continue to see end market growth and are committed to meeting our customer's increasing pigment needs over time. We are pleased with the progress we are making toward our previously announced target of 10% additional capacity via debottlenecking. This capacity is expected to come online over the next few years and is roughly equivalent to the volume associated with a new production line.

Let's review our 2018 outlook on the next slide. Now halfway through the year and with a solid Q1 and Q2 behind us, we are on track to achieve our 2018 guidance. We anticipate adjusted EBITDA will be in the top end of our range of $1.7 million to $1.85 billion driven by solid execution and inclusive of the headwinds from process water treatment costs and fluoropolymers and continued raw material and distribution increases.

We also expect adjusted EPS to be at the top end of our previously disclosed range of $5 to $5.75 per share. 2018 free cash flow is anticipated to be in excess of $700 million. Finally, 2018 capital expenditures are on track to be within a range of $475 million to $525 million.

2018 lays the foundation of our longer term goals. We are on track to meet or exceed the three-year financial targets that we laid out for you on Investor Day back in 2017 supported by our commitment to Ti-Pure Value Stabilization, our ability to assist customers through the fluorochemical technology transition, and our shift to application development in fluoropolymers. We've updated this slide to reflect our increased capital allocation plan including the increased dividend and new share repurchase authorization.

Turning to the next chart, I'd like to take a moment to discuss the investment thesis for Chemours, add some strategic context to the three-year target and give you my insights on why we're excited about The Chemours story, both short term and long term.

This is not your typical commodity chemical story. We plan to deliver top line growth in excess of global GDP. How? Growth in Opteon refrigerants, the strength of our Fluoropolymers franchise and the implementation of Ti-Pure Value Stabilization, all will lead the way on the back of strong, secular growth trend.

Make no mistake. This is a multi-year story and one that's in its early chapters. We are executing against our long-term plan today and we are energized by its potential. Second, we expect to drive high returns in margins through our industry-leading process technology, which continues to give us durable cost advantage.

Across the company, we see the potential for future high return capital investments in our portfolio, like our current titanium technologies debottlenecking program and Opteon expansion in Corpus Christi, Texas. With opportunities like these, we would expect total capital expenditures to be similar to our current levels going forward.

Third, we plan to use targeted M&A to grow our existing businesses, with the view to maximizing shareholder value over time. We expect our portfolio of industry-leading franchises to continue to generate significant free cash flow. As part of a disciplined approach to capital allocation and long term value creation, we are committed to returning the majority of that free cash flow to our shareholders.

And lastly, do not underestimate the energy and passion of our workforce. They are more than ready to turn the same focus and resolve that we brought to the transformation plan toward our growth imperative. With every passing month, we are becoming a more nimble, dynamic culture rooted in our values, guided by our long-term strategy, and focused on the right outcomes for all our stakeholders.

Our employees' dedication to Chemours' success is strong. We see it and feel it at our plant sites, our labs, and our offices the world over. That energy and resolve are truly the backbone of this company. I'm excited about the progress we've made so far and I look forward to unlocking even more shareholder value in the years ahead.

With that, we'll now open the call for your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] And our first question comes from the line of Arun Viswanathan from RBC Capital Markets. Your line is open. Arun, your line is open.

Arun Viswanathan
Analyst, RBC Capital Markets LLC
Q

Hi. I'm sorry. Could you just give us an update about how much of your contracts are contracted now for under the long-term Value Stabilization proposition and where you expect that number to go over the next 12 months or so?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.
A

Hey, Arun. We're really pleased with the progress we have with our customers right now. We really haven't talked about the percentage there, but I'd say our key customers and our major customers are all lined up around Value Stabilization. And as we've always talked about, this isn't just good for us, it's good for them as well, because not only can they predict their year ahead, but also it allows them to know and feel confident that the supply for their growth is going to be there. So, we're real happy with where we are right now.

Arun Viswanathan
Analyst, RBC Capital Markets LLC
Q

And then as a follow-up, maybe you can comment on your outlook for titanium dioxide for the rest of the year. We've had some conversations with folks who believe that North American prices could rise on the chloride side, supported by raw material increases. And then we've also seen some softness in European sulfate. I would just love to get your thoughts on the trajectory from here. Thanks.

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.
A

Arun, I don't think our thoughts have really changed since we've talked to everyone. We've said in the second half of the year, we see low to single-mid-digit kind of price increases going through. For the most part, in the Value Stabilization play, a lot of those increases are done from that standpoint. So, we're talking about increases for the non-value stabilized customers from that standpoint.

As we look at the rest of the year, we see volumes still very strong, but we're seeing a little bit of adjustment as people are adapting to our strategy. And I know we'll get the question from others. But I would say that that adjustment is in weeks of inventory. So, it's minimal in our mind.

Arun Viswanathan
Analyst, RBC Capital Markets LLC
Q

And then lastly, if I may, just on fluoro, maybe you can just give me an update on adoption? You think was it better than expected from F-gas? Or what are you seeing on that side? Thanks.

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.
A

Yeah. We're real happy with the adoption levels. I'd say, we're very strong in Europe. Right now, it's maybe a little bit stronger than we had originally anticipated but that's because a lot of folks have transitioned over HFOs a little bit faster. Now, that's part of the plan of the EU of how they set their quotas. But at the same time, I think a lot of people have shifted and gone into new equipment, a little bit faster than we thought, which is a positive.

Arun Viswanathan
Analyst, RBC Capital Markets LLC
Q

Thanks.

Operator: Our next question comes from the line of Duffy Fischer from Barclays. Your line is open.

Duffy Fischer
Analyst, Barclays Capital, Inc.
Q

Yes. Good morning, fellas. First question is just around the fluoro gases. With all the noise, and Trump, maybe walking back on some of the miles per gallon regulations in the U.S., pushing back on tariffs and stuff like that, do you see any talk that any of your products will be hindered in their adoption, from any other noise around this stuff?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.
A

Hey, Duffy. The CAFE standards that are in place right now really drive miles per gallon through 2021. That's going to be really the fundamental driver in the mobile air conditioning market in the U.S. And we don't see that fundamentally being changed.

Many of us have talked with folks at the EPA trying to understand where their heads are around some of these. But I think that the transition that we're seeing were about 50% of the market shifting to 100% by 2021 of the U.S. auto market is still in play. That's our assumption. I don't think that's really going to change.

I think the big change going forward is the adoption of the Kigali agreement going forward. That's in time. And we think that there is great story attached to that which is really about U.S. ingenuity, U.S. facilities being put to play and also U.S. jobs. So, we think that there's a value story there that the site, the product going into the marketplace is good for the U.S.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Great. And then just on the two plants under construction, the one in Mexico that's stalled, what's the outlook there? Do we need to come up with a plan B and write that off or are we still confident we can go forward there? And then on the fluoro gas, are we still on track for the completion there in the ramp early next year?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

Yes. We are on track on our Corpus Christi facility for Opteon. That will be mechanically complete this year. So, we're right on track to be able to bring that on. For the Mining Solutions facility in Mexico, as I mentioned in my comments, we're stalled right now. We are confident that we're going to be able to get the approvals back. We had a little bit of a snafu. The elections were occurring in Mexico, but now we're on the other side of that. So, we hopefully will have an update for everyone in our next quarter call.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Great. Thanks, fellows.

Operator: Our next question comes from the line of John McNulty from BMO Capital Markets. Your line is open.

John P. McNulty
Analyst, BMO Capital Markets (United States)

Q

Hey. Good morning, and thanks for taking my question. So, there is a growing concern, I guess, on the raw material front that raws are going to push higher, and I know you have long-term contracts that help to at least mute the volatility of that. But I guess, as we look into 2019 and this will, I guess, go to the condition of what you think the market is right now, do you think you can get through whatever raw material headwinds you may come across in 2019 through in price between your locked in on some of the stabilization side and then also just thinking about what's not locked in there? I guess can you keep up with the raw material inflation next year?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

Hey, John. If you look across the board in Chemours, with all three of our business lines, we are seeing raw materials come at us with higher prices across.

Mark E. Newman
Chief Financial Officer & Senior Vice President, The Chemours Co.

A

Right. Across everywhere.

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

And our job and the job of the presidents is to keep price in front of them. I think they've done an excellent job of keeping that. And obviously, our job of our purchasing team – our crack purchasing team is to limit those raw material increases where they can. So, we feel very comfortable where we are and what we see going into 2019 that we're going to be able to stay ahead of that.

Specifically, on the TiO2 side, our Value Stabilization contracts and the way we put those in place contemplate the raw materials that are coming into that. So, we have that sorted out from our standpoint in terms of how we're setting up our contracts with our suppliers, as well as how we set up our contracts with our customers. So, we feel confident that we can maintain our margins going through this.

John P. McNulty
Analyst, BMO Capital Markets (United States)

Q

Great. And then just one quick question. With regard to the Arkema announcement, I guess during the quarter and your partnership with them for Europe, I guess, can you give us an update on that? Have you started delivering for that? Did it have much of an impact on the quarter? And how can we think about that going forward?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

Yeah. We really like that agreement. It's a distribution agreement. So, it allows more access of our Opteon products into the European marketplace. At some point, especially when you get into stationary refrigeration and stationary HVAC, you eventually get – these are blends, right? So you're taking your existing products and blending them at times with HFOs.

So, at times, you sort of get hamstrung if your quota amount isn't high enough. Well, with the Arkema distribution agreement that allows us to utilize basically their quota, so we can get more products into the marketplace. So, this is good because Arkema is allowed to get into the HFO marketplace with their customers so they could be serviced. But it's great for us as well because we can get more products not just more HFO but also utilizing Arkema's quota to be able to do that. Talk about a win-win, this is a pure win-win from that standpoint.

John P. McNulty
Analyst, BMO Capital Markets (United States)

Q

Great. Thanks very much for the color.

Operator: Our next question comes from the line of Laurence Alexander from Jefferies. Your line is open.

Laurence Alexander
Analyst, Jefferies LLC

Q

Hi. You mentioned passing on raw material costs to price hikes. I was wondering if there's a lag effect involved and how long it is.

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

Yeah. Well, we try to anticipate, right. So, we're trying to stay ahead of that. But you're absolutely right that we have to keep our eye on that all the time. But that's why we've been very aggressive with price increases. You heard on the chem solutions side, as things have tightened up, that team has been very aggressive with price. Some of that is raw material based but a lot of it is just market conditions and Ed and the team have been very aggressive around that. Paul's team on the fluoro side, especially on the fluoropolymer side, we've been ahead of this. In fact, we announced it earlier. So, our job is to get ahead of that and not wait for those to come at us.

Laurence Alexander
Analyst, Jefferies LLC

Q

Okay. And then if we think about fluoroproducts to the auto industry and Opteon, obviously, you're having good success there. But I was wondering if fluctuations in production volumes are having any effect at all or if it's changing the demand outlook at all? And what your outlook is for the rest of the year and into 2019?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

On the Opteon side, no, we are in good shape. We did have maintenance outages which we talked about during last quarter's call, during this past quarter. That has limited the amount of supply that we have in the marketplace that's made it a little bit tighter. We hope to get those production facilities up at their full potential going from now through the rest of the year.

So, I would say we're a little bit to blame to shorting that but the demand is there. And it's our job to make sure we can make the supply meet that demand.

Laurence Alexander
Analyst, Jefferies LLC

Q

Thank you very much.

Operator: Our next question comes from the line of Jim Sheehan from SunTrust. Your line is open.

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Good morning. Thanks for taking my question. Could you talk about what the impact was in the quarter from planned maintenance and fluoroproducts? And what are your expectations for the rest of the year?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

Welcome, Jim. On planned maintenance, we had, as we mentioned before, our normal big TAR shutdown in multiple facilities. As I mentioned, that was limited a bit of supply. We haven't been explicit on that, but it limited a bit of supply. Going forward, we have another TAR scheduled on one of our other facilities through the rest of the year. But we feel very confident that we're going to be able to meet those supply for what we have going forward. So, I'd say that from a cost perspective, that's spread across because that gets basically amortized. It's more of an issue on the supply side to make sure we have enough product to get to our customers.

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Great. And on TiO_2 ore inflation, can you help quantify what the headwind was in the second quarter, either the percent increase or the dollar impact from higher ore cost year-over-year?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

Yeah. We've talked in the past, most of our take on ores are long-term contracts that we have fairly well laddered. So, for the most part, we haven't had a huge impact from that piece of it. And again, we are contemplating on the other side of that equation our pricing to match up with any increases that come off across in ore. As many people know, we basically are the market for chloride ilmenite. So, those are very aggressive contracts that we have with our suppliers. And on high grade ore, we contemplate, as I mentioned, multiyear contracts that don't have any cliffs so that we can spread that across all our suppliers.

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Thank you.

Operator: Our next question comes from the line of Matthew DeYoe from Vertical Research. Your line is open.

Matthew DeYoe
Analyst, Vertical Research Partners LLC

Q

Morning. So, results have beat kind of again and you're lowering interest expense on the year, also introducing the new buyback program yet guidance is kind of staying relatively flat towards the high end. Would you say that's a sign of maybe incremental bearishness towards the second half or is that more just increased conservatism towards the outlook?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

Well, when we had set up the guidance in the beginning of the year, I think what is a little bit different from what we contemplated, we have as we talked about the process water costs at Fayetteville, which we shared with you that we think is going to be about $35 million for the year.

We are seeing raw materials come at us though as I mentioned we're trying to stay ahead of that with price, but we continue to see raw materials. And as I'm sure you've talked to others, transportation costs have been significant and higher than we had originally anticipated.

So, we're just being prudent as we look toward the rest of the year around that as we said. We believe we'll be at the high end of that range, but we're just trying to be prudent with the rest of the year in what we see.

Matthew DeYoe
Analyst, Vertical Research Partners LLC

Q

Sure. I mean can you quantify what the headwinds for water treatment and legal were to the quarter itself?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

Now, we haven't dropped it to the quarter. What we've said is for the water itself, the water treatment costs itself for the year are $35 million. Obviously, what occurred in the quarter was contemplated inside of the results that you saw.

Matthew DeYoe
Analyst, Vertical Research Partners LLC

Q

Okay. But it was – yeah, all right. That's helpful. I wasn't use if it was all kind of second half related or whether you'd already based some of that in the margins for 2Q. Yeah. That's it for me, thanks.

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.
A

Sure.

Operator: Our next question comes from the line of Vincent Andrews from Morgan Stanley. Your line is open.

Brian M. Scott
Analyst, Morgan Stanley & Co. LLC
Q

Good morning. This is Brian Scott on for Vincent. I was just hoping you could help us understand the volumes over the balance of the year. It seems like the flat guidance for the balance of the year or the flat guidance for 2018 would imply negative volumes in the second half. So, I'm just trying to understand with Altamira fully ramped now, could you just walk us through the dynamic there?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.
A

Yeah. So, let me give you a couple of angles on that. One is, the first half is really the strength of our fluorochemical business. When you think about an air conditioning season, especially you're going to see that strong and that's typical for us. You're going to see that stronger in the second quarter-first quarter timeframe than you are for the rest of the year despite the transition of HFOs from HFCs.

That's just very typical of us. You normally would see that same kind of a balance on at least in North America on the coating season. But Value Stabilization from a TiO_2 perspective is also playing into that because as I mentioned, I think our customers are now seeing and now able to clearly see what our pricing policies are going to be for the remainder of this year and into next year. And I think that eases some of the pressure for them around jumping ahead on inventory. So, from that standpoint, I think this is all contemplated in how we look at the year. And we feel very confident about where we're going from here.

Brian M. Scott
Analyst, Morgan Stanley & Co. LLC
Q

Great. Okay. And then I think this is the first quarter in TiO_2 and maybe the last eight quarters where your margins were actually down sequentially. Can you just kind of walk us through was that the lower utilization of the plants? Was that the raw materials versus pricing? Can you give us a sense of what's driving that?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.
A

Yeah. It's primarily the pricing versus raw materials. And again, it is intent, right, because it's part of what we're driving with Value Stabilization. As we had mentioned, after April, you would see low- to mid-single-digit kind of price increases for the rest of the year. And that's exactly what we have contemplated in terms of our guidance.

Brian M. Scott
Analyst, Morgan Stanley & Co. LLC
Q

Great. Okay. Thanks very much.

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.
A

Sure.

Operator: Our next question comes from the line of P.J. Juvekar from Citi. Your line is open.

P.J. Juvekar
Analyst, Citigroup Global Markets, Inc.
Q

Yes. Hi. Good morning.

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.
A

Hi, P.J.

P.J. Juvekar
Analyst, Citigroup Global Markets, Inc.
Q

One more follow-up on TiO2. I know you have a flexible raw materials slate. So, what percent of your raw materials are seeing price increases?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.
A

I don't know how to answer that, P.J., because I'm not sure – I would say that there's a percentage of our raws that have that but it's really based on where our contracts are and how those contracts play. So, I can't give you that number off the top of my head because it's not sitting on the top of my head. But there is a piece that we're seeing that. But your point is right. As we adjust to anything, right, we have the ability in our circuit to be able to operate our facilities different than most because of the way we could bring our ore blends through. So, whether that is the price point of our ore blends or the volume we want to put out the back door, it allows us that flexibility that's maybe a little bit different than others.

P.J. Juvekar
Analyst, Citigroup Global Markets, Inc.
Q

Thank you. And then second question on Opteon, where do we stand in terms of auto penetration in the U.S.? I think we're supposed to get to 100% by 2020. But just tell us where do we stand? And then as you mentioned that these Opteon contracts get adjusted downwards in the mobile market, so if that's the case, where do you think price increases will come in the future from? Is it base refrigerants? Is it European stationary opportunity? Where do you think pricing will come from? Thank you.

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.
A

Yes. So if you think about the refrigerant segment in overall, first of all, to your first question, we're about 50% penetration into the U.S. automotive market, at least the OEM side. Obviously, over time, that's going to grow when you get into the refill side of things, but it's 50% in the OEM. That will get to about 100% as we have always said by 2021, especially driven by the CAFE standards. You're right in terms of the way OEM pricing goes, but if you look at it as a balance, the reason we feel good about our price points overall in terms of our price increases, stationary refrigeration, stationary HVAC, not just in Europe but also in the U.S. will give us pricing power from that standpoint. And base refrigerants, as the quota drops, your price points go up there as well. So, those are the offsets to the OEM price down.

P.J. Juvekar
Analyst, Citigroup Global Markets, Inc.
Q

Thank you.

Operator: Our next question comes from the line of Bob Koort from Goldman Sachs. Your line is open.

Christopher Evans
Analyst, Goldman Sachs & Co. LLC
Q

Hey. Good morning, everyone. It's Chris Evans on for Bob. I was hoping you could give us some more specifics on how the Value Stabilization efforts are going. Are you on pace to get 50% of sales under contract in 2018?

And also you mentioned a price increase for some spot customers. Curious, do Value Stabilization customers also see higher prices as a result of cost inflation in your basket?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.
A

So from a standpoint, Chris, as I mentioned, we're really happy with the progress we're making on the Value Stabilization contracts and discussions that we're having with customers. We haven't and we're not going to really talk about a percentage of how many of those contracts. But we're on our pace that we want to see as we go into next year of what that should be. Your point is right. We're having price increases with the customers that are not on Value Stabilization contracts. Those have gone out and going into effect now in August.

And most of our Value Stabilization customers are not seeing that price increase because we've already negotiated what those prices would be over time. And they contemplated what we believe our raw material cost would be. So, we feel comfortable and confident that we're covering the cost of raws as we execute those contracts for those customers.

Christopher Evans
Analyst, Goldman Sachs & Co. LLC
Q

Great. And then maybe just on your multiple. The market seems to be completely disregarding your specialty chems exposure and instead valuing you as a pure play TiO_2 company. Would like to get your thoughts here? Just do you continue to allocate lots of cash for share repurchase to take advantage of this low valuation? Or do you think something maybe more strategic is available to better highlight the valuation disconnect?

Mark E. Newman
Chief Financial Officer & Senior Vice President, The Chemours Co.
A

So Chris, Mark Newman. We obviously think given our current valuation, the reloading of the buyback makes a lot of sense. Obviously, we completed the first authorization relatively quickly. And so, as we think of return of capital to shareholders, we think first a meaningful portion of it through the buybacks. Second, given the confidence that we have in Value Stabilization and our earnings power over time, we made a fairly meaningful 50% almost increase in our dividend. So, we see this as a way of returning the majority of our free cash flow to shareholders over the next three years, but in a way that we think will be very accretive.

We also believe that there is significant reinvestment potential in the business. So, we believe in our top line growth story over these three years, and we also believe that we can compound that impact on our income statement by the actions that we're taking on the share buyback and other actions like we have in terms of our reduced interest cost. So, we think this is a really great story with meaningful top line growth, operating income growth, and compounding that with even more EPS growth over time, given the strong free cash flow generation of the company.

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.
A

So, Chris, we completely agree with the thesis that the multiple doesn't really make sense for the kind of company we are and the kind of company that we're growing to be. So, as Mark said, in our three-year plan, I think those top line and bottom line and cash generation numbers warrant something a little bit different. And as Mark said, our board is very confident of that, and that's why we came out with not only a share buyback plan, but also a significant increase in the dividend because we want to give everyone confidence that we have confidence of what we're going to deliver over the next three years.

Christopher Evans
Analyst, Goldman Sachs & Co. LLC
Q

Thanks, guys.

Operator: Our next question comes from the line of Jeff Zekauskas from JPMorgan. Your line is open.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC
Q

Thanks very much. When you look at your Opteon product line, what's the percentage of automobile applications versus non-automobile applications? Is it, I don't know, 90%, 10% something like that? And are the mobile applications growing at faster than a 10% volume rate this year or at a slower than 10% rate?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.
A

So, Jeff, right now as we start up Opteon, obviously, you're going to have a lot more auto, but it's more than 50%, but it's nowhere near 90%. So, I would say we're probably in this 60%, 65%, 70% range, that's automotive and the rest, stationary, but stationary because of the F-gas regulation in Europe is growing very fast.

So, that's why you're seeing the offset if you will to P.J.'s earlier question of why our price points or why our price growth is significant is because the stationary is starting to come in significantly, especially with the F-gas side. So, we feel comfortable in terms of the balance, but the higher level of growth because we have so much growth in European automotive to start, we're seeing this as we mentioned 50% to 100% growth in the U.S. side. It's the stationary side that's really the growth engine going forward over the next few years.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC
Q

Right. I guess this is my follow-up. In roughly which year do you expect a new entrant into the HFO market? That is for how long do you think it can be maintained as a market with two major participants because of the patents? And, in very rough terms, when do you think a new competitor would emerge when the patents expire?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

Our job, Jeff, is to continue to drive IP to give ourselves protection longer and longer. And I would say our team is doing a fantastic job of that. We also have – one of the aspects of our agreement with Arkema was to allow more products to get into the marketplace as I mentioned. So, we believe customers have access to what they need from an HFO perspective. Arkema adds some of that ability to be able to do that in the European marketplace. But on top of that we are continuing to work hard at protecting our IP and adding protection over the top. So, I really can't give you a time because our job is to continue to keep that protected for as long as possible.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Okay. Thank you.

Operator: Our next question comes from the line of Don Carson from Susquehanna. Your line is open.

Donald David Carson
Analyst, Susquehanna Financial Group LLLP

Q

Yes, Mark. I want to go back to kind of your view of the cycle as previous questioner mentioned. We've seen Q3 EU contracts settling down and increased local supply and higher Chinese imports. So, I guess the issue for investors is, is this a pause in the cycle, or are we at a cyclical peak? And related to that, when you've seen prices stabilize in the past, for what period do customers tend to destock because presumably they accumulated a lot of inventory as prices were rising over the last 18 months?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

Yes, Don. It's a good question. And I think it's probably the question that's probably on everyone's mind from that standpoint. I guess our view on this is that one is we are trying to do something dramatically different than a typical TiO2 cycle and that we're giving an opportunity to our customers to be able to lock-in on value with our Value Stabilization play.

On top of it, if you recall in the past, a lot of capacity would come on stream that really drove a different behavior. We just don't see that right now. And so, I know that there's more Chinese imports into Europe, but fundamentally, a lot of that is still filling for a void that [ph] La Porte (00:53:40) facility was filling, primarily on the ink side.

We're not seeing any of that product intercept us in the markets that we serve and the customers that we serve and the applications that we serve. And if you look at it net/net, we just don't see a significant increase in capacity over the next three years. I mean just to keep things in line, you're going to need about 200,000 tons a year of new TiO2 capacity to be able to just keep up with the demand.

And that's one of the reasons why we're driving the debottlenecking work that we're doing is over that period of time to try to bring in at least half of that. So, from our perspective, we just see some very different dynamic. Yes, we're seeing some inventory adjustments by some of our customers. But as I mentioned, I think that's in weeks, not months of inventory because I don't think there was a lot built up. But in a rising price environment when you're unsure of where those prices are going, I'm sure people hedged with some inventory.

But now that we're giving them confidence of where things are going from the price standpoint, you're going to see a little of that back off. But again, I think that's a matter of weeks of inventory. So, we just don't see it being massively significant at this point in time.

Donald David Carson
Analyst, Susquehanna Financial Group LLLP

Q

Thank you.

Operator: Our next question comes from the line of John Roberts from UBS. Your line is open.

John Roberts
Analyst, UBS Securities LLC

Q

Thank you. In your 10% TiO2 expansion program, are you expanding anywhere other than Altamira?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

Really, across the board for the most part. So, it's our three large facilities that really have the opportunity to be able to expand. And so it's not just one facility, John. Altamira, we have actually ramped up fully. It's probably one of the best ramp ups we've ever had in the history of our plant start-ups. But the work that we're doing is fundamentally across multiple locations.

John Roberts
Analyst, UBS Securities LLC

Q

And is there any update on your search for bolt-on deal opportunities?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

As we've said in the conversation before, we're targeting our M&A right at the existing businesses that we have. We've looked, we've scoured the world around opportunities, and I think from our standpoint where we've come back to saying we want things that sort of connect into our business. ICOR I know was small, but ICOR is a great example of that.

That acquisition gives us distribution power that we didn't have before and especially with HFOs coming into the U.S. marketplace, that's just going to help us get more product out. Those are the kinds of things you're going to see from us are things that enhance our current portfolio. You shouldn't worry about seeing something that is going to be disconnected from anything else that we're doing. That's not our goal.

John Roberts
Analyst, UBS Securities LLC

Q

Great. Thank you.

Operator: [Operator Instructions] Our next question comes from the line of Roger Spitz from Bank of America Merrill Lynch. Your line is open.

Roger N. Spitz
Analyst, Bank of America Merrill Lynch

Q

Thank you and good morning. First, you talked about higher freight. Would you be able to provide the impact of the higher freight on the quarter and/or the half?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

We have not broken that out. So, no, Roger, we wouldn't be bringing those numbers specifically out.

Mark E. Newman
Chief Financial Officer & Senior Vice President, The Chemours Co.

A

Maybe I'll just add to that. When you look at the cost delta in the quarter, I'd say think of freight and raws being the predominant factor, in addition to the water treatment cost.

Roger N. Spitz
Analyst, Bank of America Merrill Lynch

Q

Okay. And in fluoroproducts, you mentioned higher raw materials. Can you mention which were the particular fluoroproducts raw materials that you were facing pressure on?

Mark E. Newman
Chief Financial Officer & Senior Vice President, The Chemours Co.

A

Yeah. I think distribution probably is a bigger number than raws. We don't have a significant amount of raws that aren't our own from – in the fluoro side. The biggest single raw is fluorspar and we're not seeing significant increases in that area.

Roger N. Spitz
Analyst, Bank of America Merrill Lynch

Q

All right. Got it. And chemical solutions, you referred to a adverse mix shift. Was that a shift away from NaCN to say methylamines or aniline or what was that adverse mix shift?

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

That was inside the performance chemicals and intermediate side. On the Mining Solutions side, we have very, very strong demand right now. And our job is to supply all that demand out of our current facilities. But it was really in the performance chemicals and intermediates, where we saw a little bit of that shift. It wasn't significant, but we saw a little bit of that shift.

Roger N. Spitz
Analyst, Bank of America Merrill Lynch

Q

Okay. And lastly for working capital outflow – inflows over the next two quarters, can you talk about any guidance there in terms of the amount and/or pace of say inflows?

Mark E. Newman
Chief Financial Officer & Senior Vice President, The Chemours Co.

A

So, I think our free cash flow guidance is kind of what we would stand behind, which is on a full year basis, greater than $700 million. We always guide folks to understand that we build working capital in the first half given the nature of our business. And so, I think if you look at that that would suggest that there's higher free cash flow generation in the second half of the year.

Roger N. Spitz
Analyst, Bank of America Merrill Lynch

Q

Got it. Thank you very much.

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

A

Thank you.

Operator: I'll now turn the call over to Mark Vergnano for closing remarks.

Mark P. Vergnano
President, Chief Executive Officer & Director, The Chemours Co.

Listen, we really thank you all for your time and your interest in the company. As you can tell, we continue to be excited about our future and our three-year plan in front of us and our job is to execute off of that. So, again, thanks for your time and your continued interest in Chemours.

Operator: This concludes today's conference call. You may now disconnect.