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The Chemours Co. (CC)

Q1 2018 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Emily, and I will be your conference operator today. At this time I would like to welcome everyone to The Chemours Company First Quarter 2018 Earnings 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.

Alisha Bellezza, you may begin your conference.

Alisha Bellezza

Vice President, Treasurer & Head of Investor Relations, The Chemours Co.

Thank you, and good morning, everyone. Welcome to The Chemours Company first quarter 2018 earnings conference call. I'm joined today by Mark Vergnano, President and Chief Executive Officer, who will begin the call with a discussion of the quarter's highlights; and Mark Newman, Senior Vice President and Chief Financial Officer, who will review our financial performance and liquidity position. Mark Vergnano will then review our quarterly business results and conclude the call with our outlook.

Before we begin, 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 that 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.

Mark P. Vergnano

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

Thanks, Alisha. Good morning and thank you for joining us today. Before we begin today's call, let me take a minute to walk through some of the personnel changes we announced this morning within our finance function. Alisha Bellezza, who you all know well as our current Treasurer and Vice President of Investor Relations, is transitioning to the role of Vice President, Commercial Operations and Supply Chain for the Titanium Technologies segment. So, although she'll no longer be the face of our Investor Relations, you can be sure that her talents are being put to great use in driving our future results. I would like to personally thank Alisha for standing up the IR function in Chemours and being our chief navigator with investors through our transformation.

With Alisha's move to our Titanium Technologies segment, Sameer Ralhan, our current Vice President of Business Finance, will also assume the role of Treasurer. Sameer has also been a key player in the execution of our five-point transformation plan. And he is also no stranger to the Treasurer responsibilities previously holding the position prior to Alisha. In his dual role, Sameer will continue to oversee our global business finance and corporate finance functions.

I also want to welcome and introduce Jonathan Lock, who is joining Chemours as Vice President, Corporate Development and Investor Relations. Jonathan brings with him a wealth of knowledge surrounding corporate strategy and investor activity joining us from SunCoke Energy. In his new position, Jonathan will help to drive the Chemours growth journey while also being the key source of communication for our investors.

So, with that, let's move to our first quarter results. We began 2018 at full speed, energized by execution of our workforce and the continued momentum from our strong 2017 full-year performance.

We reported meaningful improvements across all key financial metrics. Notably, our net income and EPS doubled on both a GAAP and adjusted basis, driven by the strength of our businesses. In addition to our outstanding organic performance, we continue to execute on our capital allocation strategy. Since announcing our authorization in December, we have repurchased approximately $400 million worth of shares of our common stock through today.

In April, we enhanced our current refrigerant portfolio with the addition of ICOR International to our fluorochemicals business. We want to welcome our new ICOR International employees to the Chemours team. Chemours' first quarter performance is a great step on our shift to being a growth-oriented company. We are well on track to deliver on the three-year financial targets we previously provided.

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

Mark E. Newman

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

Thanks, Mark. Let me begin on slide 4. Our changing focus from transformation to growth is clearly evident in our first quarter 2018 results. We exhibited significant increases on a year-over-year basis in several of our key metrics. Net sales rose 20% or nearly $300 million over last year's first quarter, a result of increased sales across all segments.

Net income on both the GAAP and adjusted basis roughly doubled when compared to our first quarter of 2017. Adjusted EBITDA of $468 million increased 64%, a demonstration of our growing profitability while our adjusted EBITDA margin expanded approximately 700 basis points year-over-year to 27%. Even though we experienced our normal seasonal working capital use of cash during the quarter, we generated almost $100 million in free cash flow, driven by our strong operating performance.

Our pre-tax ROIC rose to 40%, significantly above the 30% level we set as our three-year target even while we ramp up investment in our businesses. We remain focused on the profitability of our existing assets while investing in high ROIC projects like the 10% capacity unlock we expect from our Titanium Technologies circuit over the coming years. Further, we are demonstrating our ability to grow inorganically through the recent targeted acquisition of ICOR International.

Turning to the next slide, let's review the drivers of our adjusted EBITDA performance. Higher global average selling price of Ti-Pure pigment on a year-over-year basis drove the $140 million favorable price variance. Overall, prices for our Fluoroproducts and Chemical Solutions products were consistent with the previous year's quarter. We saw broad-based volume growth in the quarter, resulting in $47 million of year-over-year improvement. Within Fluoroproducts, the conversion to Opteon refrigerants was accompanied by increased demand for fluoropolymers products.

In Titanium Technologies, continued preference for our Ti-Pure titanium dioxide also contributed favorably, while Chemical Solutions' increased demand was modestly positive to overall results.

Currency provided a nice tailwind when compared to last year's first quarter, resulting in a $43 million benefit, primarily related to the appreciation of the euro. Higher variable costs, including distribution and water treatment costs, were a headwind on a year-over-year basis. We, however, remain vigilant on our fixed cost structure. Overall, we recorded $183 million improvement to adjusted EBITDA for the first quarter of 2018, an excellent start to the year.

Given our focus on growing EPS, we have added a new chart on slide 6. This quarter's adjusted EPS of $1.41 more than doubled when compared to the last year's first quarter. This is even more impressive when considering the negative effects on tax on year-over-year performance. Our business results translated into a $0.97 improvement, driven by the contributions from each of our segments that I covered on the previous slide. These strong results were somewhat offset by the change in the effective tax rate, due to our geographic mix of earnings versus last year's first quarter, along with the impact of discrete items. Our tax rate in the quarter was 22% versus 13% for last year's first quarter.

The impact in this quarter of our share repurchases was negligible due to timing. However, we were able to more than offset the dilutive effect of equity compensation, and we anticipate the benefit of share repurchases to become more meaningful in future quarters. Our operating results have also translated into additional cash generation with a solid balance sheet position, which I'll cover on the next slide.

As you can see, the strength of our balance sheet provides us ample flexibility which we put to good use during the quarter. Our three primary uses of cash were working capital in line with seasonal demands, increased capital investments to fund organic growth, and additional share repurchases completed in the quarter, along with the higher dividend level we announced at Investor Day.

We ended the first quarter with a cash balance of approximately $1.4 billion in comparison to $1.6 billion at yearend 2017. Net operating cash flow of $196 million was primarily driven by strong business results in the quarter even after including our use of $192 million to support working capital. Free cash flow was nearly $95 million, a $122-million improvement versus last year's first quarter, even with increased capital expenditures versus last year. We continue to execute our capital allocation strategy, repurchasing approximately $240 million of shares in the quarter. Since quarter end, we have purchased an additional $40 million, leaving approximately $100 million remaining on our existing $500 million authorization.

Additionally, we're enhancing our liquidity while adding flexibility to our company's balance sheet. In April, we amended and restated our credit agreement and entered into a new seven-year term loan B while also reducing principal by approximately $75 million. As part of this transaction, we also entered into a new five-year $800 million senior secured revolving credit facility. Including the new revolver, our total liquidity on a pro forma basis stood at approximately $2.2 billion at quarter end. Our net debt of approximately $2.7 billion translated into net leverage ratio of approximately 1.7 times on a trailing 12-month basis.

We are pleased with the flexibility that our cash balance and cash flow provides us. Our current liquidity position has given us the ability to consider targeted inorganic prospects such as the ICOR International acquisition that closed in April while continuing our return of cash to shareholders and investing in our core businesses.

And now, I'll turn the call back to Mark.

Mark P. Vergnano

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

Thanks, Mark. Beginning with a review of our Fluoroproducts segment on the next slide, we generated over $730 million of sales in the quarter. The 12% year-over-year increase was driven by strong demand for both our Opteon refrigerants and fluoropolymer products. Price came in line with last year's first quarter as a result of mix across the segment, which I'll review a bit later. Adjusted EBITDA improved 33% to $206 million. This translated into an adjusted EBITDA margin expansion of nearly 450 basis points to approximately 28%, exemplifying the capability of this segment. Opteon refrigerants continue to see increased adoption, primarily within Europe and the United States, driving the year-over-year volume increases.

In Europe, the increase was and continues to be from demand for stationary HFO blends in response to the 2018 F-gas quota reductions. In the United States, the mobile market is moving toward the full conversions to low GWP technology, encouraged by CAFE carbon credits. As a reminder, we anticipate the current CAFE standards that are in place to drive the U.S. mobile market to full conversion by the end 2021.

Base refrigerant volume was flat in comparison to last year's first quarter as we were able to completely offset the impact of quota phasedowns in Europe with higher demand for our base refrigerants in developing countries. Quota phasedowns in Europe, as well as tightening global supply, drove a favorable price increase in our base refrigerants, mostly offsetting the Opteon contractual pricing commitments.

In April, we completed the acquisition of ICOR International, a supplier of ozone-safe refrigerants and related products for heating, ventilation, air conditioning, and refrigeration applications in North America. This acquisition enhances our ability to meet our customer needs in North America while also expanding our U.S. market channel access.

In fluoropolymers, volume growth rates for our products were above global GDP for the seventh quarter in a row. We continue to see increased demand from favorable market trends paired with environmental regulation enforcement in China which has constricted global supply. Fluoropolymer price also improved year-over-year, a result of the increases implemented during 2017. We expect the additional price increase announced earlier this year will lead to further price momentum in 2018.

Current fluorochemical market trends are expected to fuel the technology transition toward Opteon refrigerants.

We anticipate Opteon top line to grow over 20% in 2018 compared to last year, driven by further continued adoption of low GWP stationary blends and mobile refrigerants.

We remain committed to supporting our customers' requirements both on the base refrigerant side as they move toward adopting Opteon technology. As such, we are managing our quotas given the regulatory environment and expect base refrigerant demand to be relatively flat for the year. We anticipate prices for our base refrigerants to modestly increase in comparison to last year driven by the tightening global supply of those base refrigerants.

At the same time, the favorable market trends in combination with our application development work in automotive, energy storage, and electronics are leading to higher demand for fluoropolymers. We expect this momentum will continue through 2018 and beyond. As we look over the course of the year, we have planned maintenance outages at certain fluoropolymer facilities in the second and third quarters. We are working closely with our customers to ensure that their supply needs are met during this time.

Moving to our Chemical Solutions segment on the next slide. Sales in the quarter rose 4% to $144 million on higher year-over-year demand across the segment. The segment generated $11 million of adjusted EBITDA in the quarter reflecting lower technology licensing income along with higher increased variable costs. This also included higher distribution expense and cost related to the construction of the new mining solutions facility in Mexico.

Mining solutions demand is anticipated to remain strong throughout 2018, while Performance Chemicals & Intermediates is expected to improve modestly.

We mentioned in our release that the construction of our new facility in Laguna, Mexico has been delayed as a result of a complaint filed against several local and federal authorities involved in the permitting process of our facility. We are working with the community and our stakeholders to address any additional questions they may have regarding our operations.

We are committed to working with all stakeholders and believe that our investment in Laguna not only benefits the local community but also serves the growing market need for our products in Mexico. We have previously stated that our current mining solutions facility is sold out, and we expect it will remain so due to sustained strength and demand in the Americas.

Turning to slide 10 to review our Titanium Technologies segment. Sales increased over $200 million to $854 million versus last year's first quarter. The improvement was primarily driven by higher global average prices for Ti-Pure titanium dioxide up 22% year-over-year. We also communicated price increases to certain customers in North America and Asia-Pacific during the quarter. The most recent communications were affective April 1. These communications aligned with our value stabilization strategy while also taking into account our expectation of higher raw material costs for the remainder of the year.

As you may recall, last year's first quarter saw very strong demand. Even against that tough comparison, continued preference for our products resulted in 5% volume growth year-over-year. We saw increased Ti-Pure TiO_2 demand from the plastics, coatings and laminate end markets. Adjusted EBITDA improved $135 million to $294 million, an 85% increase compared to last year's first quarter. This translated into approximately 900 basis points of margin expansion. As anticipated, higher global average prices were partially offset by increased raw material costs. We also incurred higher distribution costs in the quarter.

Looking to the remainder of the year and consistent with our value stabilization strategy, we expect volume growth to be modestly higher level than global GDP in 2018. Our team continues to work with customers to implement previously communicated price increases. Based on this we expect to realize further margin expansion throughout the remainder of 2018.

Turning to slide 11 to review our outlook. As we reflect on our strong first quarter performance and look forward through year-end, we have great confidence in our previously disclosed 2018 outlook. We expect to deliver adjusted EBITDA at the top end of our previously communicated range supported by the continued positive momentum of all our businesses. We also anticipated adjusted EPS to be above our original range taking into account the impact from the share repurchases we have already completed.

Our fluorochemicals business continues to successfully optimize its product portfolio, supporting customers on both sides of the technology transition as they move toward low global warming potential refrigerants.

Solid demand for our fluoropolymers products, along with steady price improvement, is expected to carry through the remainder of this year and beyond.

And within Titanium Technologies, the implementation of previously communicated price increases for Ti-Pure TiO2, are expected to result in sequentially higher average prices in the coming quarters. We continue to expect CapEx to be within a range of $475 million to $525 million for 2018, even with the delay of construction in Mexico. Not only do we have other high-return projects to fund, but we are also committed to reducing the environmental impact of our products and continuously improving our manufacturing operations. Owing to the strength of the first quarter and our expectations for healthy results for the balance of the year, we now expect 2018 free cash flow to be in excess of $700 million.

Let us take another look at our three-year targets on the next slide. Based on our anticipated results for the full year 2018, we have full confidence in the longer-term goals we previously described. We continue to anticipate revenue across the company to grow above global GDP rates with expanding margins, translating to even higher profits on the bottom line. Adjusted EPS is expected to grow at a compounded annual growth rate of at least 15% to 20%. Free cash flow is expected to remain healthy, generating approximately $2 billion to $3 billion on a cumulative basis.

The new mining solutions facility construction delay is not expected to impact 2018 operating results. We expect to exceed our three-year targets for the overall company in spite of this delay. We are energized by our first quarter performance and expect to leverage this momentum throughout the next three years.

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

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first 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

Thanks for taking my question. So, I guess a couple of questions. First one would be on – earlier, you had talked about trying to lock up your customers in terms of longer-term contracts that facilitated you working with them a little bit more effectively. I guess can you give us an update as to where you are in that push?

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

A

Sure, John, and thanks for opening your coverage with us as well, John. I would say that we're very happy with where we are with our value stabilization work, with our customers. I've been out to see many of them and it's going along extremely well. I think it's a value proposition for them as well as us, and I think they recognize that. And as we've always said, we don't want all of our volume to be in value stabilization contracts. We want to have a significant portion of it in that, and I think we're on our path – exactly the right path we want to be on.

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

Q

Great. And then, maybe just a follow-up to that. I know there's some discussion about how the ores and the raw materials are starting to look relatively tight as well, and I know you're advantaged on that side. But I guess when you think about the potential for ore prices to move for your platform, I guess how insulated are you from that? And when you think about longer duration contracts with your customers, how does that balance out with the longer-term relationships or the need for them with your ore suppliers?

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

Yes. So John, first of all, as we have this quarter and as we look to the year, ore is sort of in the range of what we thought it would be. So, we have contemplated that in terms of how we've thought about the year and how we've planned for the year. But to your point, we have multi-year contracts on our ore bodies. They're laddered contracts, and all of that is contemplated as we work with our customers on the value stabilization contract. So these are all intertwined and thought through extremely well from our 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 Duffy Fischer from Barclays. Your line is open.

Michael Leithead
Analyst, Barclays Capital, Inc.
Q

Hey, guys. This is Mike Leithead on for Duffy this morning. Mark, the first quarter is typically not your seasonally strongest quarter for your business. Is there any reason why that is not the case this year? Because if I just annualize this quarter's earnings, I already get above the high end of your EBITDA range without even plussing up for seasonal strength in 2Q or Q3 or further TiO_2 price flow through. So, just trying to get a sense of how conservative the guide is for this year

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

Yeah. So first of all and as we've said, we feel very confident about the top of our range. And as the year progresses, we'll revisit that if we feel that the additional guidance should be given. But to your point, Mike, I think that the seasonality of this business is changing a little bit because with Opteon so heavily on the mobile side, you don't see as much of a spike on the fluorochemicals side as you used to see in the past.

And I would say that on the TiO_2 side, you still have a bit of seasonality in the second quarter for the North America coating season. But I would say it's a little bit less of a seasonality. I will say toward the end of the year, both businesses are a little bit lighter than they are in the beginning of the year. But I think your read on this is fairly good that we don't have the massive seasonality that we used to have.

Michael Leithead
Analyst, Barclays Capital, Inc.
Q

Great. And then on the buyback. I mean, Mark, you previously said that you like buying your shares in under $50. They've stayed in that range and it looks like you're on pace to finish your current authorization actually here in 2018. I was hoping you could talk about your willingness to go to the board for another authorization. And if so, how soon we should expect those conversations to happen?

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

A

Yeah. So, I think we've been very transparent about what we want to do with cash. Growth capital is on the top of our list, how do we use our capital to grow the company, cash return to our shareholders, and then targeted acquisitions. Our ICOR acquisition I think fits into that category of targeted acquisitions, the kind of things that we're looking to add to the company.

So, you're right. Mark and I talk all the time about the fact that we believe that this company is undervalued. And at that point in time, we felt like this was a great opportunity and a great return to buy our stock. We'll continue to do that as long as we feel that it makes sense for us and our shareholders. And we anticipate going back to our board mid-year and talking to them about additional share buyback opportunities. Obviously, it's a board decision, but we will engage with them mid-year.

Michael Leithead
Analyst, Barclays Capital, Inc.

Q

Great. Thank you.

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

Vincent Stephen Andrews
Analyst, Morgan Stanley & Co. LLC

Q

Thank you, and good morning, everyone. Just a question on foreign exchange. If I look at slide 5, you had a $43 million currency benefit. So it looks like you have a very strong pass-through from a margin perspective. So, can you just remind us sort of where you have transactional benefits from FX and then what are your assumptions for FX benefit for this year, and how does that change versus the beginning of the year, if at all?

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

A

Yeah. Hi, Vincent. This is Mark Newman. I would say most of our currency benefit comes from the euro-U.S. dollar currency pair. And it manifests itself probably more so in our TiO_2 business than in other segments although we saw currency as a benefit in all three segments. And so, I think sitting here today, our view on currency is contemplated in our guidance. There's been a lot of talk recently of U.S. dollar strengthening with fed tightening. So, I think some of the currency that we see in this quarter may not necessarily be ratable throughout the year. But clearly, it's a benefit in the quarter and it's something that we've factored into our thinking for the rest of the year.

Vincent Stephen Andrews
Analyst, Morgan Stanley & Co. LLC

Q

Okay. And just as a follow-up on slide 12, the headline now says that you expect to meet or exceed the three-year target. So, I'm just wondering can you kind of drill that down to is it – do you mean – do you serve line items there, or do you mean in all segments, or how should we be thinking about where you see the upside?

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

A

Yeah. And Vincent, we didn't mean to be cute with the meet or exceed, but obviously you picked up on it. There's elements in there that we feel very confident that we can exceed especially with the strength we have in 2018.

And as you look over the three-year period and some of those maybe more on a meet standpoint. So, obviously, the EPS side of things, cash return to shareholders, we think probably sit in those exceed buckets. We'll most likely update this toward the end of the year for everybody, but you're reading it well. With a good start to this year and what we see for the rest of this year, we think at least in some of those metrics we are very confident on the exceed.

Vincent Stephen Andrews
Analyst, Morgan Stanley & Co. LLC

Q

Okay. Thank you very much.

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

P.J. Juvekar
Analyst, Citigroup Global Markets, Inc. (Broker)

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. (Broker)

Q

So, on Opteon, you've been adjusting Opteon prices to – or to OEM customers for a while – and while your base refrigerant prices keep going up. I mean, that's opposite of what you were saying. You were saying that new product prices go up and old product prices decline. So, can you talk a little bit about that dynamic and how you see that going forward?

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

A

Yeah. So you got to think of this, P.J., I think in three buckets. Number one is Opteon for mobile air conditioning with OEMs, right. And as we've been very open with everybody, as you put multi-year contracts in with an automotive OEM, you have productivity each year that you have to deliver to that OEM which our job and our – it manifests itself in lower price to the OEM and our side is to try to come up with productivity opportunities to offset that. So that's one area that price fundamentally goes down.

Second is on the stationary refrigerant side, where we've had a nice uptick specifically because of F-gas regulations in Europe. That's been strong in price for us. And then, the third leg is your base refrigerants, and you're absolutely right that you would think new products go up and old products go down in terms of price, but remember the quota system for base refrigerants actually drives volume down. And because of that, if demand doesn't come down subsequent or equal to that, your price is going to pop up. So, you have a stronger price position at least in the areas where the quota plays, so when you put those three together that's why the composite on our fluorochemical business price is what it is.

P.J. Juvekar
Analyst, Citigroup Global Markets, Inc. (Broker)

Q

Thank you for that. And I have a second question on TiO2, you mentioned chloride feedstocks are going up, so given your flexibility in your system, you can low grade your ores and adjust, or you can use that as an excuse to go out and raise TiO2 prices. So, how do you think about that optionality that you have that is unique to you and what kind of actions would you take?

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

A

Yes. So, I would say that's something that Bryan Snell and the team work on every month, right, in terms of – they look at the options they have in front of them. You're exactly right. We have the ability to operate those ores or blend differently. Now you have to understand you can't turn necessarily on a dime on that, you have to plan that out. So, you stage the ores in front of your facilities in the right timeframe. But we think about that all the time and that's part of the logic for us on value stabilization is working with our customers, so they can get a dependable supply of TiO2, we get a dependable demand signal from them, and they can plan out their year or subsequent years in terms of knowing what they're going to be paying for that so they can run their business more efficiently, and we can run ours more efficiently. So, you're right, we have that flexibility all the time but it is contemplated inside of the whole strategy of value stabilization.

P.J. Juvekar
Analyst, Citigroup Global Markets, Inc. (Broker)

Q

Thank you.

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

Laurence Alexander
Analyst, Jefferies LLC

Q

Good morning. I guess a couple of questions. First, can you quantify how much outages should hit your EBITDA line year-over-year? And then can you also – for the TiO2 market, could you maybe compare and contrast the current environment with the environment right before the last peak in the cycle in terms of what you're seeing in terms of order trends, the breadth of order strength around the world, inventory levels, raw materials. I mean just if you can sort of just give a feel for where you think we are and how it's different?

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

A

Yes. So, let me hit the first one first for you, Lawrence. So, outages, obviously, we take – like any company, take normal maintenance outages on your facilities all the time. This year, because of the work, and I'd say excellent work that our team has done on really when we take these outages, we've been able to spread these out a little bit longer than normal. And because of that, there's a cost benefit for us. There's also a capacity benefit for us on that. We just happen to be in the year where we have some fluoropolymer outages well planned for.

Teams have been working on this for probably 18 months, to be honest, to get ready for these. So I think we'll execute these extremely well. But at the same time, we build the inventory upfront to be able to handle our customer's needs. These are all contemplated as we're going forward with it. So, we don't quantify that. It obviously is all part of our guidance. We don't quantify those, Laurence. But I will tell you that this is probably a year where we have a little bit more than less around that, but all planned for, and I feel very confident that the team's going to execute off of that well.

Your second question around TiO2, this is very different from when – from the timeframe you talked about before. I don't think we're seeing – at least from our standpoint, we see very good steady demand across the industry. We see clear signals from our customers, from a demand standpoint. We monitor inventories across, and we don't see any spike in inventory or holding or hoarding.

So, I would say this is an extremely different situation than what we've seen in the past. Very manageable. And, again, what we've said all along is, I think the industry is at a very high utilization rate and we don't see that being disrupted over the next several years.

Laurence Alexander
Analyst, Jefferies LLC

Q

Okay. Thank you.

Operator: Our next question comes from the line of Jeff Zekauskas. Please state your company name. Your line is open.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

JPMorgan. Mark, I was wondering what you've thought of the March Chinese titanium dioxide export numbers in that it seemed to represent a departure from previous levels. And do you – what's your expectation of, I don't know, monthly exports from China for the remainder of the year and do you think that that disrupts the titanium dioxide supply-demand balances?

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

A

Yeah. So, you're right, Jeff. The exports out of China were a little bit higher and going into different parts of the world, primarily Europe and Asia Pacific and the Middle East. I'd say they continue – so, first of all, they don't intercept us. They are still going at the lower end of the market. And I also think that they are actually fulfilling demand. So, what's happening here is I think you're seeing demand continue to be pulled around the world, and this supply is actually fulfilling demand versus offsetting supply that's already there. So that's a very different dynamic. And if you looked at that data, the price point was higher coming out from the last period.

So, we're having a higher price coming in. Supplanting, not supplanting anyone else's supply, really fulfilling demand, and that demand is at the lower end of the quality curve. So, at this point in time I think it's just very normal and natural, if you will, for global supply to be able to seek where it needs to go. And I do not see that as being disruptive nor do I see that being disruptive for sure for us.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

And then for my follow-up, a question for Mark Newman. In your slides I think you talked about $47 million of inflationary costs. But there was no discussion of any cost reduction or the effects of cost reduction. Is your cost reduction done or what do you expect to accomplish for 2018 and what have you accomplished year-over-year in the first quarter?

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

A

Yeah. I'd say we – first of all, I think we've said before on our TiO2 business we had contemplated higher ore costs which are reflected in the pricing actions that we took. So, I think they're just showing up in that line. We keep a very tight lid on our fixed cost structure. If you notice, Jeff, while our revenues were up 20%, our COGS is up probably close to 10%. Our SG&A is down nominally year-over-year, and our SG&A as a percentage of sale is actually a single digit.

So, we've done a lot of work to really dial-in the costs – the fixed costs out of the business and continue to do that. But, really, we continue to be focused on growing our earnings and investing in areas of the business where it makes sense to do so versus the initial focus on the transformation plan, primarily cost focus.

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

A

And, Jeff, just to add to Mark's point, I want to just reiterate. We have not and will not take our eye off the cost side of the equation. We're always looking for how to drive efficiency inside the company, how to do things better. So, a lot of the cost that you saw was really raw material or distribution or cost of goods sold from a manufacturing standpoint. We continue to keep our eye very, very closely on the fixed cost side.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Thanks very much.

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. This is Chris Evans on for Bob. First, I just wanted to congratulate Alisha. It was really fun and I appreciated all the time, you helping us up on the story as we ramped in, so thanks and congrats.

Next, a question on the fluoro margins, a nice uptick in the quarter, I just wanted to make sure in terms of how your quota was being – for the legacy refrigerants was being outlaid, that there wasn't any sort of onetime or any special considerations that might have had that step-up higher than you might see for the rest of the year. And then, just I wanted your comments, Mark, on how that margin looks just sort of over a longer period of time.

You previously targeted the high 20s, and you're – over a longer period of time and you're already there. So, I just wanted maybe some commentary on what you think the ultimate profitability could be for the segment?

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

A

Yes. And Alisha – you made Alisha blush. So, thanks for doing that, Chris. I think there's nothing strange in the quarter. So there wasn't any one-time opportunity in the quarter. I think this is what you should expect of the fluoro margins, mid to high 20s is what we've said and that's where we're living right now. And you're right. We got there a little bit quicker. I think Paul Kirsch and the team have done an exceptional job of getting the fluoropolymers side. We always knew the fluorochemicals side was rock solid with Opteon.

I think F-gas regulations in Europe have pulled a little bit harder on our stationary refrigerant side, but it's just accelerating volume more than anything else. And then we had benefited on the price increases on fluoropolymers last year. We have a very targeted price increase going on this year. But the application development engine is really starting to work on the fluoropolymer side. So, maybe a little bit earlier but I would say these are very sustainable margins.

Christopher Evans
Analyst, Goldman Sachs & Co. LLC

Q

Great. And the F-gas regulations were helpful this year but the Kigali Amendment goes into force I believe January 1 of 2019. And so you're already seeing some positive pricing or some strong – really strong positive pricing in the legacy HFC business. But I mean do you imagine Kigali could be an additional incremental benefit going into next year?

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

A

Yeah. For sure, Kigali is very important for this business. And Paul and his team are very focused on that. And you're absolutely right, that's a huge benefit for us going forward because now you get the global impact that we've been seeing in Europe.

Christopher Evans
Analyst, Goldman Sachs & Co. LLC

Q

Thank you.

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

Emily Wagner
Analyst, Susquehanna Financial Group LLLP

Q

Good morning. This is Emily Wagner on for Don. In the longer-term TiO_2 contracts, what downside protection do you get for not raising the contract prices in line with spot? Is there an absolute floor price or a certain percentage above the spot price during a down cycle?

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

A

Thanks, Emily. Emily, we don't really talk specifics about the contracts. We think those are proprietary with each of our customers. But I can assure you that the cost of ore is contemplated inside of how we evaluate those contracts or at least our understanding where ore costs will be. So, we protect both ourselves and our customers through that. But we don't really talk specifics about that.

Emily Wagner
Analyst, Susquehanna Financial Group LLLP

Q

Got it. And then in terms of the debottlenecks you referenced at your Investor Day, what capacity in production increases do you see in 2018 through 2020?

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

A

Yeah. We said 10% is what we were really trying to drive through now and 2021 from that standpoint; and those are on track. We're really excited about getting the teams motivated to do that. Some of those are equipment, some of those are process changes and we're executing all of those.

Emily Wagner
Analyst, Susquehanna Financial Group LLLP

Q

Okay. Thank you.

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

Roger N. Spitz
Analyst, Bank of America Merrill Lynch

Q

Thank you and good morning. Can you tell us what the expected EBITDA impact if any of the fluoropolymer planned turnarounds in Q2 2018 and Q3 2018?

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

A

Yeah. Those are all contemplated (sic) Roger inside of our guidance. So, from that standpoint, we have always known of these and we've always planned around them, so they are absolutely part of our guidance going forward.

Roger N. Spitz
Analyst, Bank of America Merrill Lynch

Q

Sure. I was just trying to see what the size might be so I can know how to shape the EBITDA over the next [ph] couple of quarters (47:31)

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

A

Yeah. So I would say the best way for you to think about this is, and I know this is going to sound a little goofy, ignore it. Because with the way we plan the year and the way our costs flow because remember when you do a shutdown of this nature, these are large shutdowns that are actually ratable over a period of time. So, all those costs don't flow into one period and we still kept the revenue because we have the product that we have in inventory going forward. So, as you think about modeling, I would say ignore that from a standpoint because it's already contemplated in terms of how our cost and revenue are going to play.

Roger N. Spitz
Analyst, Bank of America Merrill Lynch

Q

Okay. And my other question is, maybe just asking it a little bit different, talking about your view of the shape of the TiO2 cycle from where we are over the next year or so.

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

A

Yeah. We would say that we don't believe there is a cycle and we believe it's going to be fairly steady and flat from that standpoint. That's part of the whole concept that I know not everyone has bought into our value stabilization theory, but I could tell you I am absolutely bought into it, based on how the team is executing off of it and the interactions we're having with customers at the same time.

So, I really believe that this is something that you're not going to see any form of a cycle over the next couple of years.

Roger N. Spitz
Analyst, Bank of America Merrill Lynch

Q

Thank you very much.

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

A

Sure.

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

John Roberts
Analyst, UBS Securities LLC

Q

Thanks. Nice quarter, guys.

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

A

Thanks, John.

John Roberts
Analyst, UBS Securities LLC

Q

Back on the Chinese exports, the increase to Europe is most striking, and that's probably related to the Pori outage. But do you think that business is profitable for the Chinese or do you think they're making a strategic investment to gain a foothold there and willing to lose money on those sales?

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

A

Well first of all, prices are pretty high there, John, so I don't think anyone's doing that from a strategic purpose. I think there is a need for product because of Pori. I think that you're absolutely right, at least from our perspective. There's a market that's served that isn't getting served right now, and I think that's why you're seeing it go in there. But I would ask you guys, look at price going in there as well as the volume, and I think you'll see that this is filling a need and it's filling a need at a pretty good price point. So, from that standpoint, that's why we're not concerned about it.

John Roberts
Analyst, UBS Securities LLC

Q

Okay. Great. Thank you.

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

A

Sure.

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

P.J. Juvekar
Analyst, Citigroup Global Markets, Inc. (Broker)

Q

Thank you. Mark, do you think the TiO2 industry over-earned a little bit in 2017 with the Pori outage and the Chinese shutting down capacity? And related to that, how much of that Chinese capacity do you think can restart back up with some new investments in pollution control equipment? Thank you.

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

A

Yeah. P.J., I don't know if I'd call it over-earned from that standpoint. Did it have an effect on supply into the market? For sure, right? But I don't think it was from an over-earning standpoint. I would say that, from our view, we're not seeing a whole lot of restart of everything that was shut down. I think that there might be some new capacity coming in in time. But I spent a lot of time, Mark Newman and I went over to China about a month-and-a-half ago. We spent a lot of time with our customers there and a lot of time inside the market. And we are absolutely convinced and I'm sure many of the folks you talk to would say the same thing, that this environmental regulation enforcement in China is real. I think it not only is it real, but it's sustainable. I think the government is very serious about it. I think it's become a KPI inside the country for a lot of the provincial governments.

And so from that standpoint, I don't see these things coming back unless a major investment is being made in their facilities which will increase their costs or something significant changes from the standpoint of how they operate. So again, I think this is still going to play out over the next couple of years, and I don't see all that supply coming back.

P.J. Juvekar
Analyst, Citigroup Global Markets, Inc. (Broker)

Q

Okay. Thank you.

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

A

Sure. Well again, thanks everybody...

Operator: And there are no further...

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

A

Sorry, I stepped on you there, Emily.

Operator: That's okay. Thank you. There are no further questions at this time. I will turn it back over to Mark Vergnano for closing remarks.

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

So, thanks again. And thanks, everyone, for joining us. Our first quarter 2018 results really exemplify the commitment we've made to earning our way to growth. I want to again say the efforts of all our employees are really paying dividends and are continuing to be really the cornerstone of us achieving our 2018 outlook and, as I said before, exceeding our three-year targets.

So again, thank you, all, for joining on the call and thanks for your continued interest in Chemours.

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