02-Aug-2019

The Chemours Co. (CC)

Q2 2019 Earnings Call

CORPORATE PARTICIPANTS

Jonathan S. Lock
Vice President-Corporate Development and Investor Relations, The Chemours Co.

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

Sameer Ralhan
Chief Financial Officer, Treasurer & Senior VP, The Chemours Co.

Mark E. Newman
Chief Operating Officer, The Chemours Co.

OTHER PARTICIPANTS

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

Duffy Fischer
Analyst, Barclays Capital, Inc.

Dylan Campbell
Analyst, Goldman Sachs & Co. LLC

Arun Viswanathan
Analyst, RBC Capital Markets LLC

Steven Haynes
Analyst, Morgan Stanley & Co. LLC

John Roberts
Analyst, UBS Securities LLC

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

Peter Osterland
Analyst, SunTrust Robinson Humphrey, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Melissa, and I will be your conference operator today. At this time, I would like to welcome everyone to The Chemours Company's Second Quarter 2019 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.

Jonathan Lock, Vice President, Corporate Development and Investor Relations, you may begin your conference.

Jonathan S. Lock
Vice President-Corporate Development and Investor Relations, The Chemours Co.

Good morning. Welcome to The Chemours Company's second quarter 2019 earnings conference call. I'm joined today by Mark Vergnano, President and Chief Executive Officer; Mark Newman, Senior Vice President and Chief Operating Officer; and Sameer Ralhan, Senior Vice President and Chief Financial Officer.

Before we start, I'd like to remind you that comments made 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 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. Before we jump in, I wanted to take a moment to discuss the recent leadership changes here at Chemours, starting with the promotion of Mark Newman to the newly created position of COO.

As you all know, Mark has been CFO of Chemours since our spin from DuPont in 2015 and was instrumental in the transformation of the company post spin. We've worked hand-in-hand through some difficult issues during those early years. In his new role, Mark will assume direct responsibility for our three business units, purchasing and capital projects and will continue to report directly to me. This will allow me to focus more on our growth strategy as well as external advocacy on behalf of Chemours with all of our stakeholders.

Following on the heels of Mark's promotion, I'm proud to congratulate Sameer Ralhan on his elevation to the CFO position. Sameer has held a number of roles here at Chemours, including strategy, M&A, Finance and Treasury, and has been a key member of our management team since spin. Over the years, he has worked closely with Mark Newman to make our finance function more efficient and has been a steady hand as our treasurer.

I'm proud to have such a capable team of leaders here at Chemours and I look forward to working together over the coming years as we unlock the full potential of this company. So, again, Sameer and Mark, my hearty congratulations.

In addition to these promotions, we also recently announced the appointment of Erin Kane to our board of directors. Erin is the CEO of AdvanSix, a specialty chemicals company recently spun from Honeywell. Erin is a well-respected leader in the chemicals industry and I've had the pleasure of getting to know her through her involvement on the American Chemistry Council, which I will chair in 2020. I look forward to working with her closely as we shape the future strategy of Chemours. I speak on behalf of our Chairman, Dick Brown, and our entire board in welcoming Erin to The Chemours' Board of Directors.

As a management team, we will benefit from the diverse points of view we all bring to the critical issues we face as a company, and we'll continue to look for ways to reinforce our commitment to inclusion at all levels in the company.

Turning to the next page, as you know, we are currently engaged in a lawsuit with our former parent, DuPont, in the Chancery Court of the State of Delaware. While I believe that the complaints speak for itself, I wanted to clear up a few misconceptions about the lawsuit, which we've been hearing.

As to the claims asserted, DuPont continues to contend that it is entitled to unlimited indemnity from Chemours from many of its historic liabilities, including those which they recently passed to Corteva. The lawsuit requests that the Chancery Court enter a declaratory judgment limiting DuPont's indemnification rights against Chemours to those actual high-end maximum realistic exposures DuPont established for Chemours at spin or, in the alternative, return the approximately $4 billion dividend it extracted from Chemours [ph] premised upon those (00:05:35) maximums.

Some have implied that the lawsuit speaks to our insolvency. This could not be further from the truth. The allegations of the complaint were directed to the time of the spin-off, not the present. Nowhere in the complaint is it alleged that Chemours currently fears insolvency because we do not. All of our accruals are taken in accordance with the appropriate accounting standards. Thanks to the tremendous efforts of our employees and difficult choices we were forced to make as a result of the financial condition DuPont left us in at the time of the spin-off, our company is on solid financial footing, as reflected in our filings.

From our start as an independent company, we have worked hard to build and maintain shareholder value while proactively addressing numerous issues we were handed, environmental and otherwise. We remain committed to the communities we are part of. Our success has not come without some difficult choices, but we've made every decision with a view to a bright and successful future for this company. This lawsuit is in line with our effort to protect the rights of Chemours and all of our stakeholders.

I hope that is helpful context. And I'd ask that you please understand that we will not be commenting further on this call given that this is ongoing litigation.

Finally, on a different note, moving to the next chart, I'd like to briefly address the topic of firefighting foams. Questions have arisen regarding Chemours' connection to firefighting foams. Let me be clear, PFOS was the dominant chemistry in the firefighting foam industry for decades. Chemours and DuPont before it have never made or sold PFOS, period. Any PFOA contained in Chemours' short-chain [ph] telomer (00:07:47) surfactant would be at trace levels as an impurity. Chemours' potential contribution to PFOA in the environment from our ingredients used in firefighting foams is, therefore, negligible, if at all. We never manufactured or formulated firefighting foams, and we'll continue to vigorously defend our reputation.

Moving to our 2Q results and highlights from the quarter on the next chart. Our results in the second quarter reflect global economic uncertainty, a slower-than-expected start to the coating season in North America, and the impact of illegal imports of legacy refrigerants into Europe. Despite this difficult backdrop, I'm proud to report that Opteon continues to demonstrate positive momentum in the mobile sector, as we head toward full adoption in the U.S. market, and we are underway in Asia with the start of HFO mobile adoption in Japan. We have also put our Fluoroproducts operating issues behind us here in Q2 and are ramping production back to normalized levels.

I recently attended the opening of our Corpus Christi Opteon facility in Texas, and I'm proud of the great team we have running that plant. We remain fully committed to our Ti-Pure Value Stabilization strategy, and I am proud to report that we are on track to the 50% target for our AVA contract structure. With Ti-Pure Flex now fully rolled out globally, we have started to see increased customer engagement and are working to ensure the platform is well understood and leveraged by our global customer base.

We believe Flex represents a meaningful opportunity to better understand customer behavior and to engage with customers who are not currently on AVA contracts. In support of TVS and our TT business, yesterday, we announced the acquisition of Southern Ionics Minerals, an ore miner in Georgia. We'll share more thoughts on the acquisition when Mark Newman reviews the TT segment results. But I wanted to take this opportunity to publicly welcome the team from Southern Ionics Minerals to The Chemours family.

Overall, our results in the second quarter are disappointing. And I do not believe we see the second half recovery, which underpinned our original full-year outlook. I will speak to our revised outlook for the full year later in the call.

But the issues we face are temporary headwinds, which are affecting our near-term results. They do not cloud the long-term clarity, with which I see our future nor my conviction that we have the right strategies in place to create more value for our shareholders.

We have three best-in-class franchises and are working to make each one even stronger. Our combined balance sheet continues to be a source of strength and gives us the staying power to overcome these headwinds. I believe that the investments we are making today will result in a more profitable, higher growth and more stable Chemours.

As I look back on the journey we started four years ago on July 1, 2015, a lot has changed. We've made significant progress from where we started after the separation from DuPont. Chemours is a leaner, more focused, action-oriented organization, ready to face our challenges head on. We have never backed down from any challenge in our first four years and we certainly don't plan to do that now.

So, with that, I'll turn the call over to Sameer to review the quarter's results.

Sameer Ralhan

Chief Financial Officer, Treasurer & Senior VP, The Chemours Co.

Thanks, Mark.

Let's move to chart number 7. As Mark mentioned, our second quarter results came in softer than expected as global economic uncertainty created softer demand conditions across the core markets. Sales came in at $1.4 billion for the second quarter, off a record high of $1.8 billion for the second quarter of 2018. This decline was primarily driven by lower volumes of Ti-Pure TiO2 pigment and weaker demand for stationary blends due to illegal imports of HFC refrigerants into Europe.

GAAP net income was $96 million with adjusted net income of $120 million. GAAP EPS of $0.57 per share and adjusted EPS of $0.72 per share reflect lower earnings, partially offset by reduced share count. Adjusted EBITDA of $283 million was a result of weaker results across both Titanium Technologies and Fluoroproducts. This includes approximately $15 million of costs related to operating issues we experienced in our Fluoroproducts segment in the first quarter. The $15 million represent the additional cost we carried over into the second quarter. Our overall adjusted EBITDA margin was just over 20%.

Free cash flow was negative in the quarter, which is not typical for the start of coating season and cooling season. Negative free cash flow was a result of high inventories and working capital, mainly driven by lower-than-anticipated demand for our products in the quarter. Q2 capital expenditures totaled $124 million. On a more positive note, we did generate positive free cash flow in the last month of the quarter and we expect Q3 and Q4 to return more normal patterns of free cash flow positive quarters.

Moving to the next chart, adjusted EBITDA was $283 million in the second quarter of 2019. Price has a slight headwind in the quarter, driven by lower refrigerant prices mainly due to illegal imports of HFC refrigerants into Europe.

Ti-Pure prices were stable year-over-year despite some mix shift across the portfolio. As you can see, the real story in the second quarter was lower volumes. In the quarter, we experienced the combined impact of lower Ti-Pure pigment volumes and lower refrigerant sales. The former driven by lower demand for Ti-Pure pigment and latter by illegal imports of HFC refrigerants from China into Europe. Mark will speak more to the detail when he covers our segment results.

Moving to chart 9, lower earnings drove our adjusted EPS of $0.72 in the quarter, down from $1.71 in the second quarter of 2018. Our adjusted effective tax rate in the quarter was 22% versus 17% for the last year's second quarter, reflecting a geographic mix of earnings. Our lower share count contributed approximately $0.07 per share, reflecting the benefits of our capital allocation program.

Moving to the next chart, our liquidity position remains strong despite lower earnings in the quarter. Our cash balance at the end of the second quarter was $630 million. In the quarter, we spent $124 million on CapEx and returned $108 million to shareholders in the form of dividends and share buybacks.

We borrowed $150 million on our revolving credit facility in the quarter. This was primarily to help manage global cash needs. I do note that subsequent to the end of the second quarter, we repaid the entire $150 million outstanding on the revolver. Currently, we have full availability of our revolver. Our net debt at the end of the second quarter stood at approximately $3.6 billion, which translates into a net leverage ratio of approximately 2.7 times on trailing 12-month basis.

Taken together, we feel comfortable with the strength of our balance sheet, total liquidity position, and capital structure. We will continue to operate with a clear view to maintaining net leverage at or below 3 times, and remained committed to returning the majority of our free cash flow back to shareholders.

I will now turn things over to Mark Newman, our Chief Operating Officer, to discuss our segment results in more detail.

Mark E. Newman

Chief Operating Officer, The Chemours Co.

Thanks, Sameer. Let's turn to slide 11. Before addressing the Fluoroproducts segment, I wanted to start with a few words on illegal imports. Despite our ongoing efforts, illegal imports continue to weigh on the results and outlook for Fluoroproducts. We firmly believe that the F-Gas regulation is an excellent mechanism to help control the effects of manmade climate change by replacing legacy HFCs with advanced HFO technology. However, the illegal importation of older HFC refrigerants from China into the EU threatens the credibility of this program and hurts the environment.

Furthermore, this illegal trade undermines innovation, hurts local businesses, and deprives the EU of significant tax revenue, which accompanies legal and fair trade. We will continue to campaign aggressively against this spot market activity, and to work with our industry partners and government authorities to control the flow of illegal refrigerants into Europe. We remain hopeful that the EU will uphold the aims of the European F-Gas regulations and stamp out illegal imports.

So now to the results. Net sales in the quarter totaled $711 million. Pricing and currency were each 2% headwinds in the quarter. As Sameer said, lower volumes are the primary issue in the quarter as illegal imports took their toll on Opteon stationary blend adoption in Europe and also contributed to weaker base refrigerant pricing and volume in North America. Flouropolymer volumes were impacted by lower industrial demand, including softness in the global auto industry.

Adjusted EBITDA in the quarter was $180 million, reflecting the drag of the operating issues we experienced in the first quarter, partially offset by some productivity gains in our manufacturing circuit. The operating issues we experienced in Q1 at our Louisville and Corpus Christi facilities are now behind us and we continue to ramp Corpus up to its full potential.

The quarter saw a solid global adoption of Opteon HFO refrigerants in mobile applications. Growth in the U.S. and Asia continues, driven by new platform conversions, which is helping to offset the global slowdown in vehicle production. We are on track for the U.S. to be fully converted to HFO for new builds by 2021 and in Japan by 2023.

On the stationary side, we continue to add new equipment partners who will help accelerate the adoption of next generation Opteon refrigerants, which go beyond retrofit replacements. In the second quarter, we are proud to have announced partnerships with Carrier Transicold, [ph] Axial (00:19:23) and MEHITS and Mitsubishi Electric Company (sic) [Mitsubishi Electric Corporation] (00:19:29). We look forward to supporting the next generation of HVAC and cooling equipment design specifically for HFO technology together with our partners.

Let's turn to our Chemical Solutions segment on the next slide. Sales in the second quarter were $130 million. Volumes were lower year-over-year, driven by softer demand in some markets served by our Performance Chemicals and the Intermediates products, and operating issues at a key customer mine impacted the Mining Solutions segment. This volume weakness was partially offset by higher prices in Mining Solutions, glycolic, and aniline products. Despite the weaker top line, the segment generated $16 million of adjusted EBITDA in the quarter, up 4% from the second quarter of 2018.

This improvement reflects the impact of previously communicated price increases and other income from licensing agreements executed in the second quarter. For the balance of the year, we expect demand in Mining Solutions to remain strong globally and in our core markets in the Americas, and we are well positioned to support our customers as they look to responsibly develop and operate their mines.

As we move through the year, we will continue to optimize the Performance Chemicals and Intermediates business, and we are confident that our Chemical Solutions segment will be a consistent source of profit growth and value creation for Chemours going forward.

Let me know cover our Titanium Technologies segment on slide 13. Our sales in the quarter of $567 million were lower than in Q2 of 2018. The revenue decline was driven primarily by lower volumes and share loss in certain segments, most notably plastics and laminates. Price was stable on a year-over-year basis, as well as sequentially. Adjusted EBITDA of $127 million reflects higher fixed cost absorption due to lower volumes.

In the quarter, we completed the global rollout of our new Ti-Pure Flex portal and now have hundreds of active users on this site. The team is actively working with customers to help familiarize them with this new channel.

As a reminder, the Flex portal represents a totally new buying experience for our customers, with prices offered by Chemours for specific lots and grades and with specific delivery time horizons. The Flex portal is constantly evolving to adapt to new customer needs and generate new insights about buying behaviors. It's a perfect complement to our Assured Value Agreement or AVA contracts.

While we are a long way from becoming the Amazon of TiO_2, this is a first step in what we envision for the new digital Chemours. In the quarter, we also announced the acquisition of Southern Ionics Minerals, a miner of mineral sands with operations in Georgia.

Southern Ionics Minerals represent a strategic acquisition for Chemours, enabling new options to further expand our internally sourced ore capabilities. We are especially proud of the great track record of environmental stewardship, which Southern Ionics Minerals brings to Chemours. And I would like to add my personal welcome to the 130 new Chemourians who joined the company on August 1. I look forward to working with all of you to help reinforce the strength of our world-class supply chain.

Looking forward, we now expect a lower demand environment to persist to the back-half of the year given the uncertain macroeconomic backdrop. We continue to remain steadfast in our commitment to our TVS strategy. This includes the signing of new long-term AVA agreements, with an emphasis on plastics and laminates customers and fully leveraging the Flex channel to reach new customers. We know that this strategy is the best way for us to support our customers and their growth over the long term and as such remain committed to this vision.

I'll now turn things back over to Mark.

Mark P. Vergnano

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

Thanks, Mark.

Turning to the next chart. We are revising our guidance for the full-year 2019 to reflect the second quarter results and our view that a second half recovery is less likely. We are reducing our adjusted EBITDA guidance to a range of $1 billion to $1.15 billion, EPS to $2. 37 to $3.08 per share, and free cash flow to approximately $100 million. In total, our midpoint estimate of adjusted EBITDA changes by $400 million. $200 million comes from lower earnings in our Titanium Technologies segment due to weak market demand and share loss as we install our TVS strategy. Our new outlook calls for a slower recovery of share in the second half of 2019 with a return to more normalized demand sometime in 2020.

Anticipated weaker results in Fluoroproducts account for the other $200 million of change. Roughly $125 million of this figure is related to illegal imports of HFC refrigerants into the European Union, mainly from China. The remaining $75 million is related to the operating issues we encountered in Q1 and a softer demand outlook in fluoropolymers, partially offset by cost productivity across the Fluoroproducts circuit.

I speak for the entire management team here at Chemours when I say we are focused on delivering better results for all our stakeholders in the near, medium and long term. While we cannot control global politics or the broader economic cycle, we can and will continue to manage the things under our control. As I said at the start of the call, I believe that the headwinds we face are temporary, not permanent. The things that each of the 7,000 members of this team are working on every day will make us a stronger company and set us up for long-term success.

We will continue to work with customers on AVA and optimize Flex to support their long-term Ti-Pure needs. We will drive the adoption of Opteon globally and push back against the legal HFC imports using all available means. We will continue to innovate across our fluoropolymer lines to ensure that our products are at the heart of next-generation technologies, including 5G, which are poised to change the world.

Finally, we will work diligently on managing cost and driving productivity across the company. That's what the second half will be all about. I take immense pride in leading this company. I believe in our collective strength. I know that we will push through the challenges we face, big and small and emerge on the other side a stronger and more vibrant company.

Operator, can you please open up the line for questions?

QUESTION AND ANSWER SECTION

Operator: Certainly. Thank you. [Operator Instructions] Your 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

Yeah, good morning. Thanks for taking my question. So with...

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

A

Hey, John.

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

Q

...regard – good morning. With regard to the TiO2 business, so the level of volume weakness and how it's continuing, I guess given that it looks like a lot of the destocking is over at this point, is a bit surprising. So I guess can you help us to better understand kind of the pressures that you're seeing in that business? And I guess tied to that, do you feel that there's any risk that some of this price stabilization approach that you're taking is actually getting customers to shift away from say chloride to more of a sulfate-based solution or mix going – and so how should we be thinking about that?

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

A

Yeah. Thanks, John. First of all, to your last point, absolutely not. We're not seeing a shift from chloride to sulfate. I would say that, the difference for us is we're – for sure, through the destocking side, we're just seeing some fundamental market weakness, at this point in time and as we had talked in the beginning of the year, we really thought we'd see a second half pull on demand. We're not seeing that pull on demand market wide.

So number one, I think, that's the big issue that we're really facing. But on top of that, one, we're fully committed to TVS. But as we look at this, the majority of our contracts are now in the AVA contract side. Majority of our volume is on the AVA contracts. Then primarily on the coating side, we are now working with our plastics and laminate customers to work with them to try to make this fit for them as well. But what we're encouraged about is now that we have the Flex channel up and running and people are starting to understand how to use it, we're seeing significant volume now flowing into the Flex channel.

So, it's not just the contracts. We're seeing things now flowing out of that Flex channel, which is giving us a lot of encouragement. And we're able to convert some of those Flex customers over to AVA contracts. So, that's why we believe the second quarter was definitely the bottom and we're starting to see pickup as we're going forward.

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

Q

Great. Very helpful. And then, I guess, when you think about some of the volume pressures and maybe how extreme they've been, does – I guess, how are you thinking about this from the cost side in terms of your ability to flex down the capacity facilities and flex them back up when they're needed, I guess? And how much cost relief can that give you?

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

A

Yeah. Well, obviously, we're running our facilities on the lower end of their capabilities. That requires – the beauty of this business and the beauty of our technology is we have the ability to do that, right? So, you could use ore blends as much as you can. We're probably using it at the maximum level, to be honest with you right now. So, as we turn up in volume, that cost sharing really helps a lot.

So, you'll see a significant difference on the cost side because we're covering all this cost on a much lower volume base. As we add volume to – as we anticipate in the second half of the year and especially as we go into next year, you'll see a much different cost profile exactly to your point, right? Because we're able to spread that over higher volume but these operations run a lot better at higher utilization.

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

Q

Great. Thanks very much for the color.

Operator: Your 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. Question around the Fluoro in Europe. Volumetrically, how much illegal product do you think on an annualized basis is flowing into Europe? And what has that actually done to price at that lower level if you go below HFO and kind of everything else? How much has price come down from the peak in Europe?

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

A

Yeah. So, Duffy, let me start, and Mark might be able to add to this. We're seeing about 20% to 30% of the total quota in Europe being offset by illegal imports. And how it affects us is sort of in three buckets, right? So, number one, it affects our volume of HFCs. That volume actually is a negative in Europe obviously but it also has a flow through side over to the volume in the U.S. because a lot of European producers now aim their volume over to the U.S. side. So, we're seeing volume on both Europe and the U.S. being affected.

Its price of the HFCs, so that's come down significantly, as well as quota sales. The amount you pay for CO2 equivalence and quota sales are down significantly. That obviously the quota side is in Europe, but the price on HFCs is a negative both in Europe and the U.S.

And then finally, the way it affects us and flows through us is it slows down the adoption of our Opteon blends in stationary because people can use HFC refrigerants a little bit longer because there's more available to them. So, it really hits us in three ways from that standpoint. And I would say, think about the volume as the 20% to 30% that is coming against the quota, but the price has been in that kind of a neighborhood as well in terms of the drop in price.

I thought it'd be helpful maybe if Mark can talk to you a little bit about, so what are we doing about that? Because we're not just standing still here, but we are being very, very aggressive around it.

Mark E. Newman
Chief Operating Officer, The Chemours Co.

A

Yeah. Thanks, Mark. So Duffy, I think we are really working hard with other responsible industry participants in Europe to focus on, I would say three primary areas: advocacy on enforcement, with a view to really focusing on the tax evasion angle, as a way to get at more interest from member states in really taking a more active role here on the enforcement side, We continued to really work on public awareness to really – and create a better understanding of the environmental impact. This is the equivalent of 20 million tons to 30 million tons of CO2. Think of 5 million to 6 million extra vehicles being on the road.

So it's a meaningful environmental impact. And then the final area is funding a more detailed investigation of the sources of illegal imports. And so, we can share that information with enforcement authorities. So this is a full-fledged effort really on a number of fronts to get at this.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Great, thanks.

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

A

Yeah. And then Duffy, Just to follow up with Mark, because I think this is important for everyone on the call. That obviously we're taking this extremely seriously, because Opteon is our crown jewel, right? Opteon is the lowest GWP player out there. This is not just a financial issue for us. This is also an environmental issue for the world, right? So these illegal imports as Mark said are keeping reductions of CO2 happening. So, we think this is important for both the EU and for ourselves. I can't tell you if this is a three-month or six-month or a nine-month solution here. But what I can tell you is we are putting all our effort and I know a lot of our industry peers are putting their effort in this as well, not just for our economic well-being but it's good for the world.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Great. And then just two quick ones on financial. So one, why did free cash flow guide come down so much more than the EBITDA guide? And two, if we hit the lower end of the EBITDA guide, $1 billion. We're basically at 3.6 times leverage then what does that do to the buyback program if that's where we're trending?

Sameer Ralhan
Chief Financial Officer, Treasurer & Senior VP, The Chemours Co.

A

Hey, Duffy. This is Sameer. So let me first address on the free cash flow side. Look, the free cash flow guide came down primarily in line with lower earnings and also from the working capital point of view because if you look at the detail then you'll have a lot more detail in the 10-Q. We have been seeing some headwinds on the working capital side as the volume declined. So it's a combination to lower earnings and the working capital that we have.

And then on the capital allocation and what we'll do to the share buyback, essentially really nothing changes about our capital allocation policy. As you know, we've always said our first call on cash is around what we want to invest in the plant. We want to make sure we have safe and reliable operations. Then we'll look at opportunistic acquisitions in our core businesses. And after that, maximum free cash flow is – majority of that is going to go back to the shareholders. So nothing really changes around that. And we want to do that in the context of making sure our balance sheet is flexible and our leverage is less than 3 times.

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

A

And if you look, we've always said, the majority of our cash is going to go back to our shareholders. This year hasn't played out exactly the way we'd like to have, because of the headwinds we talked about. But we've returned a significant amount of cash still to our shareholders, if you look at where we are year-to-date.

So I think our shareholders should understand the drive for the majority cash going back to the shareholder, is still and will continue to be our focus and our drive.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Great. Thank you.

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

Dylan Campbell
Analyst, Goldman Sachs & Co. LLC

Q

Good morning. This is Dylan Campbell on for Bob. A quick follow-up on that free cash flow conversation. You maintained the CapEx of $500 million, how much of that is maintenance and/or I guess, kind of how much flex do you guys have on a CapEx front?

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

A

Yeah, Dylan. To give you a couple of things around that. One is as we had laid out to everyone before, we usually are in the ballpark of $250 million of maintenance capital. That's really dependent on the kind of tariffs that we have during the year. But we have two large projects this year that are essential to get done, that sort of limits our flexibility.

One, is we'll be spending about $100 million as we've talked about, as we complete our new lab. We don't have a choice around this. Our labs were within DuPont, we were required to exit those labs by the end of the year. So we had to build and move our facilities, again, not optional for us. We will have that completed in October and that will be behind us. And the other is, with our consent decree in North Carolina, the facilities that we're putting in there about $100 million of capital, that has to be completed by the end of the year as well, and we're on track there. So when you take that together, we're in the $450 million range just on those areas. And then the rest is really specific growth capital that we've been using. So, we don't have a whole lot of dial down capability beyond the $500 million. That's why we stayed in that range.

Dylan Campbell
Analyst, Goldman Sachs & Co. LLC

Q

Got it. That's helpful. And then on the Flex portal, when you think about pricing, how do you expect that to trend? Is it more aligned to kind of your contract [indiscernible] (00:39:48) stabilization contracts or closer to maybe spot pricing?

Mark E. Newman
Chief Operating Officer, The Chemours Co.
A

We really continue to experiment Flex in terms of the product offering, price, and other various aspects of customer requirements to really see what works best for our customer needs. So we continue to look at Flex as a way that we can experiment outside of the majority of our volume being on AVA contracts.

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

And to add to Mark's point, our customers on AVA contracts will always be advantaged in totality. That's the promise we made upfront and we're staying with that promise to our customers. So, in totality, when you look at the full offering AVA contract holders are always going to be advantaged.

Dylan Campbell
Analyst, Goldman Sachs & Co. LLC
Q

Got it. Thank you.

Operator: Your next question comes from the line of Arun Viswanathan from RBC. Your line is open.

Arun Viswanathan
Analyst, RBC Capital Markets LLC
Q

Great, thanks. Good morning. I just wanted to go back to Fluoroproducts. Although you are lowering your outlook and continues to see some pressure from the imports, I guess would you characterize the operations in the quarter as equivalents to your expectations or slightly better or slightly worse? And similarly, going forward, do you expect any further kind of startup issues or anything at Corpus?

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

No, we're really happy with where our operations are right now and we had a tough first quarter not just in corporates but one of our other facilities. Those are all behind us. Corpus is running extremely well, as I said, in the comments when I opened. I was just down there a couple of weeks ago. That is operating extremely well. So from that standpoint, we don't anticipate any operational issues going forward, and I feel very confident in terms of how that team is operating.

I will say that as you look at Fluoro in general, outside of the illegal imports, we have some macro issues that I think everyone is dealing with in the semiconductor and auto industry from the polymer side. But our application development engine is continuing to ramp up. We're really excited about the level of application development we have, particularly in the electronics and semicon side although automotive is continuing to grow as well.

And I will also say Opteon still will be despite this issue we're having on the stationary side, when you look at the mobile side, our volume will still be double-digit volumes growth this year. So just want to remind everyone, Opteon is still our growth engine. Our application development work on polymers continues to move ahead. And I believe we have all our operation issue all behind us.

Arun Viswanathan
Analyst, RBC Capital Markets LLC
Q

And this is a follow-up on TiO2. What's your outlook here? You mentioned kind of a slower start on coatings and weaker demand there. I guess there's been some fits and starts and price increase announcements over the last year. Obviously, you're going through your Value Stabilization strategy. So you may not necessarily be in that camp. But any thoughts on tightness of the market and potential for pricing in the rest of 2019 or maybe early 2020? Thanks.

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

A

Yeah. I would say, the macro would tell you that it's not a robust market. I think we're going to see significant improvement in the second half from where we were in the first half. But remember, we have this flexibility around, as Mark sort of laid out to you, around our Flex portal. So our Flex portal allows us to really aim our pricing at what our customers' needs are from that standpoint.

So maybe a different scenario than we bore in the past. And to be honest with you, our customers are still learning how to operate with us inside that portal. But the majority of our customers still are on the AVA side, but we're seeing a lot of uptake now on the Flex portal as well. So I would tell you that, I'm a bit wary, just to be honest about what the market situation looks like, not about where we fit in that market situation, but just in general.

I still think that there's uneasiness in the macros around the world, outside of the U.S. The trade issues with China don't help. I think we've all understand that, because it creates a little bit uncertainty. But where we are inside of that market, I'm feeling better every day as the portal really picks up volume.

Arun Viswanathan
Analyst, RBC Capital Markets LLC

Q

Thanks.

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

Steven Haynes
Analyst, Morgan Stanley & Co. LLC

Q

Hi, guys. This is actually Steve Haynes on for Vincent. Maybe just going back to the TiO2 outlook. Can you maybe talk broadly towards what normalized TiO2 demand kind of looks like in 2020, and what the [ph] catalyst is to you (00:45:06), on the demand side to kind of bridge the gap from where we are now to get there? Thanks.

Mark E. Newman
Chief Operating Officer, The Chemours Co.

A

So I would say when we look at the long-term indicators, they're all pointing to a recovery in TiO2 demand. I would say to the point Mark raised earlier, we're seeing a more gradual recovery that we would expect to start in the second half and versus some more robust recovery that we had predicted earlier in the year. So I'd say our long-term outlook still remains for a more gradual recovery and as we had talked to earlier, we've seen share loss with the implementation of TVS earlier this year. But our expectation is that we would make strides towards more of [indiscernible] (00:45:58) as we approach 2020.

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

A

And to sort of tie into that, we believe we're at the bottom of the cycle in the second quarter. And as Mark said, when these cycles turn in the past you've seen more of a sharp turn. We just think this turn is going to be a bit more gradual. But again, our goal is to aim at back to our capacity share in 2020 which will be a significant delta versus where we are today.

Mark E. Newman
Chief Operating Officer, The Chemours Co.
A

The other thing I would add is we're not seeing any new supply come online in any meaningful form. So our view is recovery will be more gradual and obviously our expectation is that we would revert to share obtainment more in line with our capacity through 2020.

Steven Haynes
Analyst, Morgan Stanley & Co. LLC
Q

Okay. Thank you.

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

John Roberts
Analyst, UBS Securities LLC
Q

Thank you. Your lawsuit to recover the [ph] dividend (00:47:04) from DuPont upstream prior to the spinoff, is there any legal precedence for that among other spinoffs other than [indiscernible] (00:47:12)?

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

Yeah. John, we really don't want to talk too much and as I mentioned in the opening, I want to give that statement because we felt that there was misconceptions about the lawsuit. And that's why want to clear up, but we really don't want to talk about anything that we're involved in a legal situation at this point, or talk about our defense of that lawsuit. So, I apologize but we really can't answer that.

John Roberts
Analyst, UBS Securities LLC
Q

Okay. And then I would have never guessed that the Chemical Solutions segment would be the relative outperformer here. Does this give you more capital going forward?

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

Yeah. You know that segment is the one that I think people don't get to see a whole lot. Number one, the Mining Solutions business inside of Chem Solutions is an extremely strong business. As we've said, this is well beyond GDP. It's probably beyond 2x GDP growth that we're seeing in gold mining in Mexico, U.S. and Canada. We are a key supplier to that. And we're one of the more advantaged suppliers from that standpoint. So, that is sort of the ballast inside of that. But even on the other side of the segment there, the team has done a really good job of increasing our profitability.

So, if you remember this segment lost money when we took it over from DuPont. And now it is approaching the margins of the rest of the company. So, a great job by our segment team. But it also has some really good market pull, if you will, for the future. So, we're very happy with that segment from that standpoint.

John Roberts
Analyst, UBS Securities LLC

Q

Thank you.

Operator: Your 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

I think you're thinking with AVA is that you may lose volumes initially. But as the market grows, you would get those volumes back. And I guess my question is, what if customers formulate with somebody else and those volumes are gone permanently? And B, are you incentivizing other players to add capacity with your market share loss?

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

A

Yes. So, number one, we don't believe that people are formulating away from us. For a variety of reasons; one, we have a great product line; two, as I said, you're not seeing this shift from chloride to sulfate here. This is just shifting between the chloride producers, which allows the formulation to come back to us.

To your other point, we have the best reinvestment economics than anybody out there. And so, from that standpoint, at this point in time – and you'll have to judge when you look at other's results – I don't think you're going to be seeing that anyone else is going to be in a position to add that capacity. We will be at the right point in time. I will tell you that we feel very confident around the strategy that we've put in place.

I mean, you could look at things like go back in second quarter of 2016, look at the [ph] TIT (00:50:27) results from that standpoint versus this quarter, and what you'll see is we had much higher volume and lower earnings. So, from the standpoint of where we are right now, we think we're in the right place. And then as you grow from that, it's going to really substantially improve our earnings. So, we feel really good about where we are, we feel really good about the reinvestment economics that we have versus our peers. We think we're in a very good position.

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

Q

Okay. And then, quickly on HFCs, the illegal imports into EU, what legal actions can you take because this is obviously not good for you and not good for the environment?

Mark E. Newman
Chief Operating Officer, The Chemours Co.
A

So, the enforcement is really done at a member state level. And so, we're really working from an advocacy standpoint on driving better enforcement while we investigate the sources of illegal imports coming into the EU. As I said earlier, I think our focus after a lot of work with other industry participants is now around tax evasion. And I think that's got the interest of the enforcement agencies in the EU. So, it really is a work in progress with each of the member states to drive a more rigid enforcement on this issue.

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

And P.J., the fact that we've been working with our industry peers and have an outside investigation firm who is helping us sort of target exactly the violators and we bring those right to the member states and their enforcement agencies so that they can then take the legal action that needs to be taken there. We also are working with the EU to try to get the penalties similar across the member states because they're different between the member states, and we're trying to get those to be high, enforceable and also equal. And we've had a lot of receptivity around that.

So, there's a lot of work here, but all of these are – we call it illegal imports because that's what they are. They are illegal and we are bringing those to the enforcement officials so that they can take the proper action. In some cases, they find them themselves. In some cases, our investigations through a third party finds them and they go ahead and execute off of that.

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

Thank you. And Sameer, congratulations.

Sameer Ralhan
Chief Financial Officer, Treasurer & Senior VP, The Chemours Co.
A

Thanks, P.J.

Operator: Your last question comes from the line of Jim Sheehan from SunTrust Robinson. Your line is open.

Peter Osterland
Analyst, SunTrust Robinson Humphrey, Inc.
Q

Good morning. This is Pete Osterland on for Jim. In TiO2, your EBITDA margin was relatively flat but still down a bit quarter-over-quarter. Are you experiencing any margin pressure from rising ore costs? And what is your outlook for ore costs through the end of the year?

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

Yeah. We're not. We look at flat ore costs throughout the rest of the year. What you're seeing on the margin side is really our coverage of fixed costs primarily because as you could see, prices are fairly flat, our ore costs are fairly flat. It's really about our utilization rates and the fixed cost coverage. That's what put the margins under a little bit of pressure.

Peter Osterland
Analyst, SunTrust Robinson Humphrey, Inc.

Q

All right. Thanks. And just related to the mining acquisition you announced, how much of your ore do you currently source internally and do you have a target for how much you'd like to increase this to?

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

A

Yeah. So, today, we have about 8% – just under 10% of the ore internally. This will add to this, but the beauty of this – and not that it will do it immediately, but the beauty of this is this can enable much higher percentage of our own ore usage over time. Now, that'll take additional investment to be able to do that.

But from a standpoint of where we are, I just want to just mention something and Mark might want to add to this. This is the same area of mining – if you think of the vein from Florida up to Virginia, this is the Trail Ridge vein that we've been pulling off of in our Starke operation. We know this ore. It's a perfect fit for our process. I mean, you couldn't design an ore better for our existing processes. So, we like it from the standpoint of the quality. We understand the cost to extract this because we do it today from that standpoint. But it also opens the door for us to be able even bring up – use up to a quarter of our ore needs through our own mines with the right investment over time, if we decide to be able to do that.

Mark E. Newman
Chief Operating Officer, The Chemours Co.

A

Yeah. A high quality ilmenite source, that's really advantage for us, allows us to gain additional synergies with our existing activity there, and bring a very responsible, environmentally friendly mining operation onboard. So, this is really works for us and it's a great investment.

Peter Osterland
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Great. Thank you.

Operator: And thank you, Mark Vergnano, President and CEO, I turn the call back over to you for any closing remarks.

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

Thanks, Melissa, and thank you all for joining the call today. As you could hear from us, obviously, the quarter wasn't exactly the way we want it to turn out, but we are very excited about the future of this company. Our strategies are intact. Our growth plans are intact. And hopefully, as investors, you all are excited about the future that we can really bring here. So, again, thank you very much for your time this morning and your continued interest in Chemours.

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