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The Chemours Co. (CC)

Q3 2017 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Sheryl, and I will be your conference operator today. At this time, I would like to welcome everyone to The Chemours Company Third Quarter Earnings Call. [Operator Instructions]

Ms. Alisha Bellezza, Treasurer and Director of Investor Relations, you may begin your conference.

Alisha Bellezza
Treasurer and Director of Investor Relations, The Chemours Co.

Thank you, and good morning everyone. Welcome to The Chemours Company 2017 third quarter earnings conference call. I'm joined today by Mark Vergnano, President and Chief Executive Officer, who will begin the call with the highlights of our third quarter, 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 business results and conclude the call with our outlook.

Before we begin, let me remind you that comments on this call as well as the supplemental information provided in our presentation and on our website contain forward-looking statements that involve risks and uncertainties, including those described in the documents Chemours has filed with the SEC. These forward-looking statements are not guarantees of future performance and are based on certain assumptions and expectations of future events that may not be realized. Actual results may differ, and Chemours undertakes no duty to update any forward-looking statements as a result of future developments or new information.

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

I'll 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. As you saw in our release last night, we had another great quarter. Our strong third quarter performance reflects higher price and solid demand for many of our products, benefits from transformation initiatives, and favorable market trends. Each of our businesses contributed to the positive and meaningful year-over-year improvements across our financial metrics.

In Titanium Technologies, global average price rose 18% year-over-year and 6% sequentially. We continue to work closely with our customers to meet their increased demand. In Fluoroproducts, our Opteon refrigerants sales grew nearly 50% versus the prior year quarter. We also saw higher demand and stable price for our fluoropolymers. We now believe fluoropolymers pricing hit an inflection point in the third quarter. And Chemical Solutions reported year-over-year growth in adjusted EBITDA.

Overall, our businesses delivered improved sales, profitability and cash generation versus a strong quarter a year ago. We are pleased with our results and the advances we've made so far this year. Based on our continued progress, we are reaffirming our full-year adjusted EBITDA outlook of $1.3 billion to $1.4 billion and we now expect positive free cash flow for the year.

I'll now turn the call over to Mark Newman to review the financial results.

Mark E. Newman

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

Thanks, Mark. Let's cover the numbers on slide 3. We generated approximately $1.6 billion of revenue in the third quarter. This was an increase of 13% from the previous year quarter, more impressive growth when you take into account the lost revenue from divestitures of our Sulfur and Clean and Disinfect businesses.

GAAP net income of $207 million improved $3 million versus the third quarter of 2016. Remember, however, last year, we recorded a $169 million gain from the sale of the Clean and Disinfect business in the Chemical Solutions segment. If we exclude that gain, GAAP net income would have increased over $170 million year-over-year. Similarly, on an adjusted basis, net income was $214 million for the quarter, an approximate $100 million increase year-over-year.

Adjusted EBITDA was up 40% (sic) [42%] to $381 million versus last year's third quarter, our best quarter since spin. This drove adjusted EBITDA margin up an approximate 500 basis points over last year's quarter to 24%. As Mark mentioned, all three businesses contributed to the improved performance with all realizing margin expansions on a year-over-year basis.

As expected, we saw the usual start of the seasonal unwind in working capital with a release of $140 million after excluding the $320 million PFOA MDL settlement payment that was made during the quarter. As a result of the working capital release, stronger business operations and after funding our capital projects, free cash flow, excluding the PFOA payment, increased approximately $190 million over the prior year period. This provided the basis for our upward revision of our full-year free cash flow outlook.

Our pre-tax ROIC performance in the quarter was exceptional, expanding to 32% compared to 12% in the third quarter of 2016, reflecting our continued earnings expansion and our disciplined focus on working capital and capital investments.

The bridge on slide 4 provides further insight into adjusted EBITDA, which was up $113 million year-over-year. Increased overall pricing drove the majority of our improvement, adding $135 million. Higher average selling price for Ti-Pure TiO2 products and increased base refrigerant pricing were modestly offset by contractual reductions in OEM pricing for Opteon.

As you may remember, last year's third quarter was the beginning of the Opteon adoption ramp up in Europe to meet the January 1, 2017 deadline of conversion. Today's pricing reflects contractual productivity targets, which are built into all long-term automotive contracts. In addition to the improved pricing, we saw an increase of $59 million in adjusted EBITDA from higher overall volume. The improvement was broad based, including strong demand for Opteon refrigerants, Ti-Pure titanium dioxide, fluoropolymers and Chemicals Solutions products.

In the quarter, we incurred approximately $90 million of higher costs versus the prior year. These were comprised primarily of rising input costs in the areas of energy, chlorine, coke and ore. In addition, we had a number of charges in the quarter that I'd like to highlight. First, we had about $16 million of higher environmental liability expense, of which approximately $8 million was for the former USS Lead Superfund Site, which was assigned to us in separation. Second, we spent about $7 million to resolve some distribution challenges in our TiO2 business to better assure supply to our customers. And third, we had some adverse impacts from Hurricane Harvey, most of which will flow through inventory later this year.

We also saw higher expenses related to capital projects, primarily driven by our Corpus Christi investment. Even with these headwinds, adjusted EBITDA was up over 40% year-over-year. We remain vigilant on cost containment as we meet higher market demands.

Turning to slide 5, let's review our liquidity position. We ended the quarter with a cash balance of $1.5 billion, essentially unchanged from the second quarter even after completing our portion of the PFOA MDL settlement in August. Including revolver availability of approximately $750 million, our total liquidity at September 30 remained strong at $2.2 billion.

Net operating cash flow was $112 million, with approximately $108 million used to support capital expenditures. Excluding the PFOA payment made during the quarter, free cash flow of $324 million improved nearly $200 million over the same period last year, driven in part by the seasonal working capital unwind of $140 million.

Year-to-date capital expenditures were $246 million, with construction underway at both our Corpus Christi and Mexico sites. We expect to spend between $400 million and $450 million in CapEx this year. We are committed to continuously evaluating our core business and investing in them, as needed, to deliver higher returns.

Our net debt at the end of the quarter stood at $2.6 billion, translating into a net leverage ratio of approximately two times on a trailing 12-month basis. We are very pleased with the continued improvement in our credit profile, as recently recognized in the ratings upgrade from Moody's.

As you may have seen, we announced that we're hosting our first Investor Day in December. The significant progress we've made over the last couple of years to improve our cash generation and strengthen our balance sheet now affords us greater financial and strategic flexibility. We, along with our board, are determining an appropriate capital allocation strategy, which we look forward to sharing with you in December.

I'll now turn the call back to Mark.

Mark P. Vergnano

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

Thanks, Mark. Moving to slide 6, our Titanium Technologies segment generated approximately $800 million in revenue and approximately $250 million in adjusted EBITDA, an increase of over $100 million from the previous year. This improvement was primarily a result of higher global average prices, up high-teens percent compared to last year.

We sent letters to customers in September and October communicating additional price increases. Based on implementing these and our previous letters, we anticipate average price to increase sequentially in the fourth quarter. We continue to be on track with our plans for Ti-Pure pricing, and are working closely with our customers to manage the impact to their portion of the value chain. We believe there's an opportunity to change The Chemours experience for Ti-Pure titanium dioxide from one of large cycles to a more stable earnings performance over time. We anticipate this being the foundation of our future growth, and we look forward to discussing it further at our December Investor Day.

During the third quarter, demand for our Ti-Pure titanium dioxide remained healthy across all regions and applications, and led to an 8% increase versus last year's third quarter, a result of customer preference for our Ti-Pure products along with global supply tightness. As we have mentioned before, we expect full-year volume to be up high single digits. Our facilities are currently highly utilized and we would anticipate running that way for the remainder of the year. This strong financial performance was partially offset by the input and distribution costs that were previously mentioned.

As Mark reviewed in our adjusted EBITDA bridge, input costs such as coke, energy and chlorine were up modestly in the quarter, while ore spot prices also traded at higher prices in comparison to last year. At this point, we would expect this trend to continue into 2018. As a reminder, increased production does require some greater use of higher-grade ore in our process. We see these costs as manageable and our pricing anticipates raw material movements.

During the quarter, we made modifications to our Mississippi distribution center, alleviating some of the challenges in costs that we incurred in the quarter. Overall, our Titanium Technologies business continue to strengthen and grow profitably. Our adjusted EBITDA margin for the third quarter of 2017 improved 800 basis points to 31%. As we look toward the end of the year, we would expect further adjusted EBITDA margin expansion.

Turning to our Fluoroproducts business on slide 7, we generated $637 million in revenue and $158 million in adjusted EBITDA in the third quarter. We saw higher prices in base refrigerants compared to the prior year quarter, mostly a result of tightness in EMEA due to F-gas regulations. While have seen strong prices all year in comparison to 2016, we saw a peak in pricing for our base refrigerants last quarter, in line with seasonal demands. Volume of our base refrigerants was lower year-over-year due to quota reductions in Europe as well as the transition to HFO refrigerants.

Given regulatory phase-downs for some of our base refrigerants over the next decade and beyond, we anticipate being able to maximize the profitability of our products through the changing environment. Also connected to F-gas regulations, we saw notable adoption of our Opteon stationary blends in Europe, as the regulations begin to shift customer demand toward our Opteon HFO technology.

We are benefiting from a favorable European auto market this year and U.S. CAFE standards, which continue to incentivize auto manufacturers supplying the United States to convert to Opteon refrigerants. As a result, revenue from Opteon refrigerants grew nearly 50% year-over-year. Looking forward, we anticipate stationary HFO blends to contribute more meaningfully to results, as they are gradually adopted over the next decade.

We also saw a solid increase in our fluoropolymers volume. Demand was primarily driven by products sold into the automotive, semiconductor, and oil and gas end markets. The strong fluoropolymer demand was coupled with steadily improving pricing over the course of this year. We believe we have reached an inflection point in the third quarter and could see some additional pricing benefits as we close out the year. As an example, we announced a targeted price increase for certain fluoropolymers in Asia effective July 1, 2017.

We anticipate realizing price increases depending on the product or application of up to 5%. Our Fluoroproducts results were partially offset by costs associated with the construction of our Opteon Corpus Christi facility, some increased input and distribution costs, and the impact of Hurricane Harvey. We do expect to see some additional costs associated with Hurricane Harvey and the ongoing water disposal at our Fayetteville, North Carolina site going forward. These costs are fully contemplated in our year-end guidance.

Even including these offsets, margin still improved 100 basis points year-over-year to 24.8%. As we look to the end of the year, we continue to expect Opteon to deliver full-year revenue growth of over 60% and we anticipate our fluoropolymers business to see further price momentum as well as deliver year-over-year volume growth. We have mentioned in the past that our team has been working to realize the full value potential of our fluoropolymers portfolio through our commitment to our core markets, while also focusing on high-value applications. We plan to have an update on these efforts at our December Investor Day.

Moving to Chemical Solutions segment on slide 8, sales for the quarter were $148 million in comparison to $182 million in last year's third quarter. This reduction was primarily related to portfolio impacts from our divestitures and the closure of our Niagara site in 2016. Volume improved 5% in the quarter with contributions from both our mining solutions and certain performance chemicals and intermediate products.

Price was in line with last year's third quarter. An improvement in performance chemicals and intermediates price, primarily due to raw material pass-throughs, was offset by lower price in mining solutions. Adjusted EBITDA doubled year-over-year to $18 million, a result of lower fixed cost and strength in our retained businesses.

Our mining solutions business has been and is expected to remain sold out until year-end. In the fourth quarter, we anticipate taking a planned maintenance outage in our Memphis facility, which could reduce volumes available for sale. We continue to look for opportunities for cost improvements and efficiencies across this segment.

Turning to slide 9 to review our 2017 outlook. Our businesses continue to deliver strong year-over-year improvements and we are pleased with our progress so far this year. Performance has been driven by strengthened preference for our Ti-Pure products, robust sales of Opteon refrigerants, maximized profitability of base refrigerants, improved pricing and solid demand for our fluoropolymers products, and enhanced profitability in Chemical Solutions. We are very proud of our performance and reiterate our expectation of delivering well above our original transformation goal.

We anticipate 2017 adjusted EBITDA outlook to be within a range of $1.3 billion to $1.4 billion, supported by our year-to-date progress. Reinforced with our increased profitability, we now believe that we will generate positive free cash flow for 2017.

Our team is one of our greatest assets and their commitment to Chemours supports our ability to realize these strong results. I want to thank them all for their continued dedication.

We'll now open the call for your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] And our first question comes from Robert Koort, Goldman Sachs. Your line is open.

Christopher Evans
Analyst, Goldman Sachs & Co. LLC
Q

Hey, good morning guys. This is Chris Evans on for Bob. I guess, in the Fluoroproducts segment, you guys cited 50% growth of Opteon, strong sales in the base refrigerants, but only put up 5% volume growth. I was wondering if you could just maybe give some specific contributions from maybe all of the sub – different product lines in there to how you get to that 5% number.

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

Sure. Hi, Chris. If you look at Fluoro in the quarter, second quarter usually is the strongest quarter for our base refrigerants, because you're in the front end of the cooling season, so that's really where you're going to have a little bit more strength. So, some of what you're seeing between polymers and Opteon and base refrigerants was a little bit of a mix issue.

Real strong on the polymer side. Opteon continues its ramp up, probably not at the same levels as it was the past couple quarters, because now we're getting to the place, at least, in Europe where you're now coming up on a year where you've sort of lapped the year, right? And then the base refrigerants side was really probably a little bit lower volume than you saw in the second quarter because of the seasonality side of things.

So, one of the things I just want to make sure you and everyone understand around the pricing side of Opteon and I did – I hope we didn't spook you guys when we talked about it. It's just when you have OEM contracts and anyone who deals with OEMs should understand that annual contracts with OEMs have a productivity kicker each year and that's somewhere in the range of 3% to 4%. It's our job to come up with that productivity. So, even though you will see the top line be affected, if you do your job right, it shouldn't affect your bottom line, and that's really what's going on on the automotive OEM side of Opteon. So, that's maybe to give you just a sense of quarter-to-quarter, Chris, if that helps.

Christopher Evans
Analyst, Goldman Sachs & Co. LLC

Q

Yeah. Thanks for that. And then maybe just sticking with fluoro, you cited a bunch of maybe transitory charges and costs in this segment, can you size the specific impact or the number of charges you took in the quarter and what margins might have looked like when excluding some of those expenses?

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

A

So, Chris, it's Mark. The way I think about our cost in the quarter vis-à-vis the $90 million, about half of the cost in the quarter relate to either increased raws in both TiO2 and fluoro as well as some of the distribution items we mentioned. The remaining cost in the quarter, really we pointed to the $16 million of environmental, most of which is tied to USS Lead. And then we had a bunch of other stuff, for example, Hurricane Harvey, we would estimate somewhere between $5 million and $10 million, some in this quarter, some will flow through inventory in subsequent quarters.

And then finally as we indicated, we had a number of items around our investments both in Corpus Christi and Mexico on the Chem Solutions new products where we had higher project expense related to those investments. So, a pretty wide range of items, but I'd say about half relate to increased raws and distribution costs in the quarter.

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

A

But, Chris, I think you were going after fluoro specifically, the $5 million to $10 million of Hurricane Harvey was specific to fluoro. And then there was a little bit of, as Mark said, the increased cost because of the project we're running down in Opteon of somewhere close to $5 million as well.

Christopher Evans
Analyst, Goldman Sachs & Co. LLC

Q

Great. Thanks for that guys.

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

A

Yeah.

Operator: Thank you. Our next question comes from 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

Can you quantify raw material impact in TiO2? Iluka was out yesterday talking about a price increase of $70 to $100 per ton, and I know that you can process different ores. But can you talk about what you're seeing and what you're trying to do to mitigate that?

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

Sure. So, for us, we had mentioned that coke and chlorine modestly went up, and we talk about spot ore being slightly up. Now you got to remember, most of our ore is under contract, right? So, from that standpoint, it doesn't massively affect us. Spot ore prices will affect us, primarily in rutile when we're trying to change grades, if you will. So, to get more capacity, we go maybe a little bit higher rutile than we do with the ilmenite, that's where spot will play out. We contemplate all of that, P.J., within our pricing. So, our pricing targets all mitigate the increase in our raw materials.

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

Okay. And secondly, I want to go back to this pricing issue on the Fluoroproducts side. I mean, shouldn't you be seeing better pricing given that Opteon grew 50% and Opteon is much higher priced than the base refrigerants? So, the mix should get you better pricing.

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

True, if you look at it purely from Opteon, but you got to remember the base refrigerants right now are in a situation where we're in the phase-downs, and in the phase-downs you have solid pricing on base refrigerants. We had more volume in the second quarter than we did in third quarter. So, that's part of the mix issue that you're seeing there as well.

Pure Opteon, you're right because Opteon is growing faster, so that's adding to it. But you got to take the base refrigerants into play as well, and that is a positive contributor to price right now based on where we are with the F-gas regulations in Europe.

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

I guess one quickly, it would help if you can give us like how big is Opteon as a percent of total refrigerants? Thank you.

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

Yeah. We're going to talk a little bit more about that in our Investor Day, P.J., and as you'll see, as Paul lays that out in Investor Day, we've got a great 10-year ramp here with Opteon, that is really our – it's going to be a significant part of our growth engine going forward. Now, it's not going to be at the same ramp that we just had over the last year-and-a-half, right, because we just brought in all this OEM business in Europe. But it's going to be a solid ramp going forward.

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

Okay. Thank you.

Operator: Thank you. Our next question comes from Duffy Fischer from Barclays. Your line is open.

Duffy Fischer
Analyst, Barclays Capital, Inc.
Q

Yes. Good morning. Just you had made a comment about the Investor Day. Can you highlight maybe the three or four points that you guys want to bring out in Investor Day again without getting into all the details, but basically what should investors walk away from this upcoming Investor Day with?

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

Do you want me to give you a synopsis of Investor Day, Duff?

Duffy Fischer
Analyst, Barclays Capital, Inc.
Q

Sure.

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

Here is the key points. First of all, I think that folks should walk away seeing that this is a great company to invest in going forward, right? So, from a TiO2 perspective, we're going to be driving to stabilize that business. Bryan is going to be talking about that in terms of how we're trying to do that. Paul Kirsch is going to be talking on the Fluoro side about how the Opteon ramp up over the next 10 years is substantial and what we're doing as well in fluoropolymers, which I think people have overlooked the opportunity that we have to grow in fluoropolymers.

Chris Siemer will talk on Chem Solutions, specifically around mining solutions and our investment in Mexico and why we think that's going to add to the top and bottom line over the next several years, while we're fixing the base of the rest of that business. And then Mark Newman is going to lay out – will talk about our capital allocation plan going forward. And I think what everyone will recognize is these businesses will be generating a significant amount of cash and so for that we want to talk to you about what we're going to do with that cash going forward. So, in a nutshell, that's what we're going to try to talk about at Investor Day.

Duffy Fischer
Analyst, Barclays Capital, Inc.
Q

Okay. And then one of the issues that at least in the news has not been quite as positive, the situation down in North Carolina, the GenX, now granted there's a lot of noise out there. But just headline-wise, what should investors kind of be prepared for over the next month, what's the status? Again, you are trying to get to the point where you weren't putting any of it out of the plant. Can you kind of just wrap up where that stands and again from a headline perspective, what should investors expect?

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

Sure. I would say that, this is a very normal chemical operation and we've been working very closely with the regulators both in the state and at the federal level and we continue to be very transparent and open in working with them through this issue. But just to remind everyone, we stopped that effluent immediately. We were not asked to do that. We felt that was the right thing to do.

We do not believe that there is health effects of this in the drinking water and we've stated that. But nonetheless, we stopped the effluent going forward and we thought that was a good-faith effort for folks in the community as well as a good-faith effort with the regulators that we're dealing with. So, we'll continue to have those conversations with the regulators, and in a very open and transparent way.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Great. Thank you, guys.

Operator: Thank you. Our next question comes from Don Carson, Susquehanna Financial. Your line is open.

Donald David Carson
Analyst, Susquehanna Financial Group LLLP

Q

Yes. Thank you. Mark, you've got a very wide range of guidance for Q4, $100 million, does that reflect the uncertainty of a fourth quarter TiO2 price increase, which is quite rare? And then thinking longer term, if you go back to 2012 what really affected the cycle back then, it seemed that the numerous price increases drove some reformulation of the part of your customers and the price increases also encouraged the ore manufacturers to try and share in those chain economics. So, how do you see this cycle unfolding differently than the last cycle?

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

A

Yeah. Don, so let me get to the first part. I don't think you guys should read too much into the fact that we – other than the fact that we're reaffirming our guidance. We've said we don't give quarterly guidance, so we didn't want to move it, just to be very blunt and honest about it. So, that's why that range stayed the same. We try to give annual guidance. We updated it midway through the year when we saw the year was being significantly better than what we had anticipated in the beginning. But our goal is not to give guidance each quarter. So, that's why you're seeing the range as it is.

To your other point, we're being very thoughtful about how we're managing price through this period of time. And as I've said before, we know the mistakes that were made in 2010 and 2011, and I can tell you from a Chemours perspective, we're not going to repeat that. We're working very closely with our customers. That's why these price increases are happening on a regular basis, but a moderate basis and they're happening to allow our customers to be in front of those, so that they can get those prices through to their customers. So, very, very thoughtful, very close collaboration with our customers. I think that's very different than what we saw in 2011, and we continue to have those dialogues openly with our customers around this. And that's what they should be expecting going forward.

Donald David Carson
Analyst, Susquehanna Financial Group LLLP

Q

Thank you.

Operator: Thank you. Our next question comes from Jeff Zekauskas from JPMorgan. Your line is open.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Hi. Thanks very much. How were your Opteon volumes sequentially? How did they change?

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

A

Sequentially, quarter to quarter?

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Yeah.

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

A

Don – Jeff, I'm sorry.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Yeah, it's all right.

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

A

Yeah. Alisha's grabbing that number. They're up. I'm trying to think of the percentage wise, we'll give you an exact number here in a second.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Right.

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

A

I'm guessing it's somewhere around 10 to 15% (sic) [mid-to-high single digits], but they're going to give me the real number.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Okay. So, while they're reminiscing if I can just ask another question. How much of your Opteon volume right now is non-automotive?

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

A

About a third is non-OEM. So, we got to say two-thirds is OEM.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

So, I meant non – in other words, so some goes to the replacement market, I would imagine, I mean not for automotive applications at all.

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

A

The other third?

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Yeah.

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

A

I'm sorry.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

So, what is that?

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

A

It's a mix between aftermarket which is very small right now and stationary and refrigeration.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Okay.

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

A

So, think stationary and refrigeration being the biggest piece of that and aftermarket being a little bit smaller.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

So, how big is aftermarket demand, in general, for automotive refrigerants relative to OEM demand and is aftermarket demand a significant source of growth for you over the next several years in Opteon?

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

A

In the 10-year period, Don (sic) [Jeff], it is. This is something that plays out over time. So, it ramps up probably like year four, five is when you start getting substantial aftermarket. It's fairly light in the first couple of years, but over the 10-year period it starts to move up.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

But the aftermarket is much larger than the OEM market, is that right?

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

A

It is. So, the aftermarket is larger. You just don't have full charges all the time. So, obviously, with an OEM, I'm telling you what you already know, sorry Jeff, but with an OEM it's full charge, right? With an aftermarket, not every car gets a full charge, you get a full charge when you either have a crash where you have to have a replacement or when you have to top off which is a partial charge. So, from that standpoint, that's why it's more cars, but maybe not the same level of charge.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

How is the adoption rate in the U.S. OEM market evolving? I know that there's a requirement that everybody adopt by, I think, 2020. Is that adoption curve continuing to grow very strongly or are things leveling off either because of current legislation or different perceptions about the importance of global warming?

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

A

Yeah. It's north of 50% and it keeps ramping up. So, we expect it to move toward 100% in that timeframe. So, we continue to see it ramp up both with domestic manufacturers in the U.S. and also anyone who's exporting into the U.S.

Operator: Thank you. Our next question comes from John Roberts, UBS. Your line is open.

John Roberts
Analyst, UBS Securities LLC

Q

Thank you. A related question to that, do you have to close older base refrigerant capacity at some point, or does that stay stable for a long time in your view?

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

A

Yeah. John, we've worked really hard, I'd say, over the past five years to make sure that we weren't going to have a gigantic overhang in our base refrigerants. So, in some cases, we move to contract manufacturing for that to where we had to, again to give us our flexibility to be able to do that.

In the case of Corpus Christi, for instance, where we're putting our Opteon facility, we're able to utilize some of the equipment there to be able to – as we put in the Opteon facility, so we've been very thoughtful. And at this point in time, based on what we foresee over the next five, six years, we don't anticipate having any big overhang with our base refrigerants.

John Roberts
Analyst, UBS Securities LLC

Q

Okay. Thank you. And then when two large paint firms merge and they look for raw material savings, do they move to larger volume [ph] disconnects (37:57) or are they already at best price, typically the large paint companies? And can you serve larger customers at lower cost to give them bigger discount?

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

A

I wouldn't say you have to go automatically to more volume, lower price, right? Our products are really geared toward creating productivity for our customers. So, we worked very hard with our customer base to make sure that what we deliver them is what they need and gives them the competitive advantage as they need, and sometimes those competitive advantages aren't about price. So, I wouldn't automatically assume that if two players merge and there's a higher volume that we're serving that the price point is significantly lower than what that was to start with.

John Roberts
Analyst, UBS Securities LLC

Q

Thank you.

Operator: Thank you. Our next question comes from Roger Spitz, Bank of America. Your line is open.

Roger N. Spitz
Analyst, Bank of America Merrill Lynch

Q

Thank you. Good morning. Regarding the growth in fluoropolymers, is this mainly driven by the PTFE or perhaps some of the specialty fluoropolymers or fluoroelastomers, and does this continue to be driven by the closures in China for environmental reasons?

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

A

Well, for sure, the closures in China are additive to what we're seeing. I'd say our fluoropolymers business is actually growing across the board. If you think about it, we're in seven different product lines around that. I'd say the markets that are the strongest are oil and gas, semiconductor, as well as, what did I miss, automotive.

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

A

Automotive, yeah.

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

A

And so fluoroelastomers fall into that primarily on the automotive side. But our melts business primarily in the semicon side, and the rest of everything else is sort of falling into it, whether it's electronics or the energy side. So, good growth across, but I'd say maybe a little bit tilted toward our high-end melt and our fluoroelastomers.

Roger N. Spitz
Analyst, Bank of America Merrill Lynch

Q

Thank you. Can you talk a little bit methylamines and aniline business? I know they're not terribly important, but it sounds like both price and volume are up at least overall for that.

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

Yeah. The methylamines business is fairly small. It's fairly flat for us. The aniline business, we sold that to Dow earlier last year. So, we're not really in the significant aniline business.

Roger N. Spitz
Analyst, Bank of America Merrill Lynch
Q

And do you retain the plant or maybe you're keeping the business?

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

Oh, yeah. Sorry, we have a small plant in Pascagoula that – I'm sorry, you're right. Fairly small. It is actually up versus where it's been before. Sorry about that. That's part of the reason why we're seeing good results out of the Chem Solutions segment.

Roger N. Spitz
Analyst, Bank of America Merrill Lynch
Q

Thank you very much.

Operator: Thank you. [Operator Instructions] Our next question comes from Christopher Perrella from Bloomberg. Your line is open.

Christopher Perrella
Analyst, Bloomberg L.P.
Q

Good morning. Did you take any damage at the Corpus Christi site or was there any delay in the Opteon expansion because of the hurricane?

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

Yeah. Definitely, the hurricane came just about over the plant site. We were down about two weeks, but I can't tell you that it was primarily because of what was damaged there. I think the facility was – our team did an amazing job of preparation. We had minor damage that was fixed fairly quickly.

The reason that we were down for two weeks was, it took that long to get utilities up and running for the site. So, we've said – somewhere I think Mark mentioned $5 million to $10 million of costs that would be spread across this quarter and next quarter. And a little tiny bit of delay that we think we can make up in the construction of our Opteon facility.

Christopher Perrella
Analyst, Bloomberg L.P.
Q

All right. And with the added expense in Fayetteville, how much is that running per quarter to deal with the effluent and any other additional environmental costs associated with that, the issue with the GenX ?

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

Yeah, we haven't disclosed that. It is contemplated within our guidance that we've given, and it's contemplated within the way the business is looking at their cost and how they have to price the products accordingly.

Christopher Perrella
Analyst, Bloomberg L.P.

Q

All right. Thank you very much.

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

A

Sure.

Operator: Thank you. Our next question comes from Robert Koort, Goldman Sachs. Your line is open.

Christopher Evans
Analyst, Goldman Sachs & Co. LLC

Q

Hey, guys. So, I was hoping you could talk a little bit about your cash deployment strategy. I mean $1.5 billion of cash on the balance sheet even after settling the MDL. When would you start beginning to deploy that and can you update us on your priorities for that cash?

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

A

Hey, Chris, it's Mark. Obviously, we continue to focus on completing the strengthening of our balance sheet and as we said in the call, we are in active discussions with our board as how best to deploy that cash going forward. I think our view is, we continue to see significant opportunities to reinvest in our business. And so we want to deliver on that. But beyond that, I think our discussions with our board which we can share with you at Investor Day is where we're headed now.

Christopher Evans
Analyst, Goldman Sachs & Co. LLC

Q

Great. And then in TiO2 you mentioned strong utilization rates for Chemours. I was wondering if you could give just a broader view of where the market is and maybe an update on the influence of the Chinese environmental shutdowns and any other factors that might influence your ability to continue your strong volume and pricing gains.

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

A

For sure, we're still seeing some shutdowns in China. I think the environmental work is continuing within the country. I think everyone now realizes across the chemical industry, this is real. I think the Chinese government is really taking this seriously and working through each industry and trying to upgrade their environmental performance. So, we're seeing – continuing to see facilities not online or taken offline. For us, we're operating full with all our capacity. For sure, the industry appears to be somewhere, at least from the multinational standpoint, in the 90s of utilization. So, I'd say it's high utilization across the industry and we're running full out.

One other thing, Chris, just want to mention, we mentioned inside of our TiO2 segment, we had some distribution cost issues and I just want to make sure there wasn't confusion about that because that was about a $7 million hit to us that I would have liked to see go to the bottom line. But in our zest to be aggressive on taking cost out, we had an issue with our distribution center down in Mississippi that we had to go in and fix and we had to throw some cost at that to fix that.

We feel very good about it. So, we don't think that's a recurring cost, that was a one-time cost to get through, and we're past that. So, that was a little bit of a negative headwind for us in the quarter that we think will alleviate. But to your base question, we think that the industry will stay at pretty high utilization rates going forward.

Christopher Evans
Analyst, Goldman Sachs & Co. LLC

Q

If I could just squeeze a quick one in, on just the ore side. You mentioned the spot prices are up a bit, but when you think about kind of how contracts might trend and your ability to offset those, I guess, can you speak about that dynamic going forward, whether you think your customers will be able to take additional price increases as you might see cost inflation?

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

A

Yeah. Well, as we've said in the past, we don't have any big cliffs in our contracts. We build these contracts over time to allow us the flexibility, allows us the negotiating ability with our suppliers, and all our pricing is contemplated based on our raw material cost. So, as we're thinking forward on pricing, rest assured our forward thinking includes what we believe the cost of ore will be and we've been very open and transparent in that in our conversation with customers as well.

Christopher Evans
Analyst, Goldman Sachs & Co. LLC

Q

Thanks.

Operator: Thank you. Our next question comes from Jason Weinberg, Columbia Threadneedle. Your line is open.

Jason Alan Weinberg
Analyst, Columbia Management Investment Advisers LLC

Q

Hi. You guys have had a net leverage target of 3 times in the past. Does that level still hold and how should we think about that compared to the around 2 times that you're at currently? Thank you.

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

A

So, Jason, we had committed to be at 3 times in 2017. Obviously, we got to that point earlier. Today we're at 2 times. I think we will speak more to our overall capital allocation strategy at Investor Day, but obviously continue to have as a key focus a strong balance sheet and it was recently recognized with the Moody's upgrade.

Jason Alan Weinberg
Analyst, Columbia Management Investment Advisers LLC

Q

Great. Thank you.

Operator: Thank you. That concludes the questions in the queue. I will turn the call back to the presenters.

Mark P. Vergnano

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

Thanks, Sheryl. In closing, our strong portfolio combined with our valued customer relationships and really our unmatched employee talent will drive further improvement in our key metrics going forward. The successful implementation of our five-point transformation plan has really laid a solid foundation for our company's future, including a significantly improved balance sheet and cost structure. So, we look forward to talking to many of you more in detail at our Investor Day in December, and thank you all for your continued interest in Chemours.

Operator: Thank you very much, ladies and gentlemen. This concludes today's conference. You may now disconnect.