07-Aug-2019

Tronox Holdings Plc (TROX)

Q2 2019 Earnings Call

CORPORATE PARTICIPANTS

Brennen Arndt
Senior Vice President-Investor Relations, Tronox Holdings Plc

Jeffry N. Quinn
Chairman & Chief Executive Officer, Tronox Holdings Plc

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc

Jean-François Turgeon
Chief Operating Officer & Executive Vice President, Tronox Holdings Plc

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

OTHER PARTICIPANTS

Patrick Fischer
Analyst, Barclays Capital, Inc.

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

Frank J. Mitsch
Analyst, Fermium Research LLC

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.

Steven Haynes
Analyst, Morgan Stanley & Co. LLC

Roger Spitz
Analyst, Bank of America Merrill Lynch

MANAGEMENT DISCUSSION SECTION

Operator: Good day, ladies and gentlemen, and welcome to the Second Quarter 2019 Earnings Conference Call. At this time, all participants are in a listen-only mode. Later, we'll conduct a question-and-answer session and instructions will follow at that time. [Operator Instructions] As a reminder, this call will be recorded.

I would now like to introduce your host for today's conference, Senior Vice President of Investor Relations, Brennen Arndt. Please go ahead.

Brennen Arndt

Senior Vice President-Investor Relations, Tronox Holdings Plc

Thank you, Chris, and welcome, everyone, to our second quarter 2019 conference call. On our call today are Jeff Quinn, Chairman and Chief Executive Officer; Jean-François Turgeon, Chief Operating Officer; John Romano, Chief Commercial and Strategy Officer; and Tim Carlson, Chief Financial Officer.

We'll be using slides as we move through today's call. Those of you listening by Internet broadcasts through our website should already have them. For those listening by telephone, if you haven't already done so, you can access them on our website at tronox.com.

Moving to slide 2, a reminder that our comments made on this call as well as the information provided in our presentation and on our website, including certain statements that are forward-looking and subject to various risks and uncertainties including but not limited to the specific factors summarized in our SEC filings, including those under the heading entitled Risk Factors in our Annual Report on Form 10-K/A for the year-ended December 31, 2018. This information represents our best judgment based on today's information. However, actual results may vary based on these risks and uncertainties. The company undertakes no obligation to update or revise any forward-looking statements.

During the conference call, we will refer to certain non-U.S. GAAP financial terms that we use in the management of our business and that we believe are useful to investors evaluating the company's performance. These include EBITDA, adjusted EBITDA, adjusted EBITDA margin, adjusted earnings per diluted share and free cash flow. Reconciliations to their nearest U.S. GAAP terms are provided in our earnings release and in the appendix of the slide deck.

For the company's guidance with respect to full year 2019 adjusted EBITDA, adjusted earnings per diluted share and free cash flow, we're not able to provide without unreasonable effort the most directly comparable GAAP financial measure or a reconciliation to such GAAP financial measure, because certain items that impact such measure are uncertain, out of our control or cannot be reasonably predicted.

As you saw in our earnings release, we provided our results on both a reported basis and a pro forma basis to assist in our discussion of the second quarter performance compared to the second quarter 2018 and the first quarter 2019. Our primary focus today will be on the pro forma comparisons to enhance your understanding of the underlying trends, our business performance and our markets in the appendices of our earnings release and the slide deck, our pro forma statements of operations and pro forma adjusted EBITDA statements for the second quarters 2019 and 2018.

Moving to slide 3, it's now my pleasure to turn the call over to Jeff Quinn. Jeff?

Jeffry N. Quinn
Chairman & Chief Executive Officer, Tronox Holdings Plc

Thanks, Brennen. Good morning, everyone, and thank you for joining us today. I am pleased to report that we delivered strong performance in our initial quarter following the closing of the game-changing Cristal acquisition on April 10. As we laid out for you at our Investor Day in late May, we were well prepared for the closing of the acquisition. Because of our significant planning and preparation, an aligned and energized global team came out of the starting blocks strong on day one and has generated substantial momentum across our organization.

Our global team feels a real sense of ownership regarding the commitments that have been made to our shareholders and has already begun delivering on those commitments.

On a pro forma basis, second quarter revenue of $827 million increased 15% from the first quarter of 2019 with TiO2 sales volumes up 17% and zircon sales volumes up 8%. Selling prices for TiO2 were level on a local currency basis and zircon selling prices were down 1% due to customer and product mix.

In a moment, John Romano, our Chief Commercial and Strategy Officer, will talk about the success his team is having, working with our pigment customers on our bespoke win-win margin stability initiatives, harmonizing contract terms across a customer base that has more than doubled in size and capturing the benefits of the broadest category-leading product portfolio in the industry.

Pro forma adjusted EBITDA of $200 million in the second quarter increased 42% from the first quarter of 2019. The substantial increase was driven in part by the sales volume growth across our product lines, but even more so in our operations by the capture of $12 million of synergies in the second quarter and $28 million of margin benefits from our shift to fully integrated operations.

As we discussed on last quarter's call and at Investor Day, we took a number of actions in the quarter's preceding closing in preparation for moving from a long to a short feedstock position. As we reported, these actions diminish margin in the quarters prior to the closing. However, we are now deriving significant benefits from those actions.

Jean-François Turgeon, our Chief Operating Officer, during his comments, will discuss the success his team is having, bringing to the bottom line the significant benefits from our combination. We are very pleased with the progress. Every day, we are finding new value-creation opportunities in the New Tronox.

Regarding our outlook for the full-year 2019, clearly global macroeconomic conditions remained uncertain. However, as we anticipated, TiO2 pigment markets in Europe and Asia have stabilized as inventory destocking has run its course. North American market conditions remain resilient. We have, however, recently seen some softness in the zircon market. But many of the key drivers to our profitability are within our control, including delivering the synergies, optimizing our global vertically integrated operations, capturing the benefits of our global footprint, controlling our overhead cost and wisely allocating our capital.

Considering all of these factors, we remain confident in our ability to deliver the results we committed to in May. We are maintaining our outlook on the financial measures within the previous issued range for the full-year 2019 on a reported basis. For revenue and adjusted EBITDA, we are narrowing our outlook to the lower half of the previous provided range of $2.83 billion to $2.98 billion and $635 million to $740 million respectively. For adjusted diluted earnings per share, we are guiding toward the top-end of the previous range of $0.43 per share. And for free cash flow, we are maintaining the range of $130 million to $160 million for the year.

The early months of 2019 were marked by significant strategic accomplishments for Tronox. In May, we articulated our goals and the strategy based upon our five pillars and unique advantages that we would use to achieve those goals. We believe now more than ever that our strategy is the right approach and we are on the path to substantial value creation.

We, as a unified global organization, also made commitments to our shareholders in May. As we said at Investor Day, it is now all about execution. We get that and we embrace that challenge. And best of all, we were already executing well and will continue to do so.

I'd now like to turn the call over to John Romano, our Chief Commercial and Strategy Officer, and Jean-François Turgeon, our Chief Operating Officer. John will report on the commercial performance and the trends we are seeing in the global markets. Jean-François will report on our operating performance and on the strong start we've made integrating two great companies and delivering synergies.

John?

John D. Romano

Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc

Thanks, Jeff. Moving to slide 4, as Brennen said, our discussion today will focus on the pro forma numbers to provide a clear understanding of the commercial performance of the New Tronox and the trends in our business. I'll briefly review the second quarter revenue performance versus the year-ago quarter, then focus my remarks on the sequential comparison to give you a sense of the direction we're taking in the business.

Year-on-year, revenue of $827 million was 8% lower than $903 million in the second quarter of 2018 or 7% lower excluding revenue of $15 million in the year-ago quarter from the Electrolytic business sold in September of 2018. Revenue was down for two primary reasons, the two we've spoken about on recent calls and presentations, Cristal's commercial approach in 2018; and lower year-on-year zircon sales and production volumes at legacy Cristal mining's operations in Australia.

In TiO_2, sales of $657 million was 7% lower. Sales volumes increased 3%, reflecting the completion of the destocking in Europe and Asia and continued resilience in the North American market. Selling prices were 6% lower on local currency basis and 8% lower on a U.S. dollar basis as the translation of the euro was a $16 million headwind on revenue. Regarding the year-on-year TiO_2 selling price decline, as I discussed at our Investor Day in May, since closing the acquisition on April 10, we fully implemented our single, unified commercial approach to serving our combined global customer base.

We were pleased to find minimal customer overlap across the regions and our average pricing across regions was quite similar. Price harmonization program across the merged customer base went very well and is now completed. So, the 6% year-on-year decline in pricing on a local currency basis is essentially a prior-year issue as we discussed with you at Investor Day and in the previous call.

In zircon, sales of $89 million were 18% lower as 12% higher selling prices were more than offset by 27% lower sales and production volumes at legacy Cristal mining operations in Australia. The mineral concentrator at the Ginkgo Mine in Australia went down in October of last year. The concentrator is on a floating barge and one of the pontoons ruptured. The lower production volumes from Gingko resulted in lower sales volumes. We discussed the concentrator in detail at our Investor Day in May and at that time committed to restarting the concentrator in early August.

I'd like to congratulate Jean-François and his team led in Australia by Managing Director, Russ Austin, as the concentrator was safely restarted this week right on schedule.

Moving to feedstock and other products, sales of $81 million compared to $77 million in the year-ago quarter. Higher CP slag sales volumes drove the increase, which were partially offset by lower ilmenite sales. As you know, we no longer actively sell ilmenite in the market given our expanded internal requirements.

Now, moving to slide 5 for the sequential comparison versus the first quarter of this year, again on a pro forma basis, revenue of $827 million was 15% higher than the $720 million in the prior quarter. Higher pigment and zircon sales volumes were the primary driver of the increase. In TiO2, pigment sales of $657 million increased 15%. Sales volumes increased 17%, reflecting the normal seasonal uptick, the completion of destocking in Europe and Asia and continued resilient North American market conditions. Selling prices were level to the first quarter on a local currency basis and 1% lower on a U.S. dollar basis.

As I mentioned earlier, we benefited from minimal customer overlap across regions and lower price harmonization risk. We continue to work successfully with our customers on unique win-win margin stability initiatives that provide the predictability of price and the stability of supply that our customers are looking for and at the same time, the margin stability that will allow us to consistently reinvest in our business throughout the cycle. We're having success with these initiatives in both coatings and plastic markets.

Moving to zircon, sales of $89 million increased 7%. Sales volumes increased 8%, positively impacted by the timing of shipments, while selling prices were 1% lower due solely to mix. As we look forward into the second half of the year, we are seeing some softening in the demand for zircon due to the uncertain outlook in China, affected by the trade war, environmental regulations and generally slower growth.

We've seen an increase in sales of lower-grade zircon products which has put some pressure on price for premium grade zircon. As a result, we expect our zircon sales volumes in the second half to be similar to the sales volumes in the first half. This sales level is included in our full-year outlook that Jeff discussed. Our mid to long-term outlook on zircon is still positive based on supply/demand fundamentals.

Feedstock and other product sales of $81 million increased from $68 million in prior quarter. Higher CP slag volumes more than offset lower ilmenite sales as our ilmenite production now serves our expanded internal requirements.

And with that, I thank you and I'll now turn the call over to JF for a review of our operating performance and profitability in the quarter. JF?

Jean-François Turgeon

Chief Operating Officer & Executive Vice President, Tronox Holdings Plc

Thanks, John, and good morning, everyone. Moving to slide 6, I'm very pleased to speak with you today and report that our integration work is going very well across our global operation, the world largest vertically integrated TiO2 production network with nine pigment plant and eight mineral sands facility on six continent.

As John did, I'll briefly cover the year-on-year comparison, then move to the sequential comparison. The sequential comparison will give you a good sense of what we have accomplished since we took the key to Cristal on April 10 and where we're heading on our journey to improve our safety, lower our cost, increase our product quality and generating cash using our advantage global footprint and integrated position.

Second quarter 2019 pro forma adjust EBITDA of $200 million was 22% lower than the $257 million in the year-ago quarter. The primary driver to the lower year-on-year result are those we discussed at our Investor Day in May. They are lower year-on-year TiO2 selling price due to legacy Cristal commercial approach in 2018 that John cover, lower zircon sales and production volume in Cristal mining operation in Australia due to the operational downtime that limited sales volume, the associated higher production costs at Cristal Mining Australia also impacted the comparison.

As John said, the Ginkgo Mine concentrator has restarted. I also want to thanks my team and our employee in Australia led by Managing Director, Russ Austin, a job very well done. In fact, the picture on slide 6 show the dredge as of last weekend. As you can see, the dredge is [ph] floating and was restart (00:17:17) earlier this week.

Higher Cristal external feedstock costs that largely rolled off by the end of the year also impacted result in the quarter. A major contributor to adjust EBITDA in the quarter was the $28 million margin benefit from our shift to fully integrated operation.

As Jeff said, we move from a long position in feedstock to a short position upon closing. The action we took, our operation in the three to four quarter in advance of moving from a long to short position at closing are now bearing fruit. They were the same action that diminish our margin in those quarter, including the first quarter of this year that we discussed with you on last call.

We increased high-grade feedstock production and put the lower unit cost product into inventory. This lower cost inventory is now benefiting pigment margin as the pigment made from that feedstock is sold. Favorable foreign exchange, primarily the South African rand and the Aussie dollar, benefit adjust EBITDA by $30 million. And we're off to a good start to delivering our targeted synergy with $12 million realized in the second quarter, $11 million reflected in adjust EBITDA and $1 million of interest saving not in the adjust EBITDA bridge.

Let's move to slide 7 for a brief summary of the synergy delivered in the quarter. Here are the synergy target we share with you on Investor Day. The synergy in each year represent the saving we expect to achieve in that calendar year. Our 2019 target, as you can see, is $45 million. We realized $12 million in the second quarter compared to our range for the second quarter of $5 million to $10 million. The $12 million saving were generated in a number of area, SG&A reduction through organizational efficiency initiatives and lower indirect spending such as a reduction in overhead expense and professional service fee. Feedstock saving by optimizing our value in use, this is a great example of how having control over our own feedstock is so valuable to us strategically over the long term. We can optimize our use of different feedstock grade to minimize waste and maximize value creation.

Supply chain saving also contribute in the quarter with reduction in direct material purchasing and service contract as well as consolidation of contract and elimination of redundant service. In addition, reduced interest rate contribute $1 million that are not reflected in the adjust EBITDA bridge.

Let's move to the sequential adjust EBITDA bridge to give you a sense of the movement we're generating in our operation. Moving to slide 8, adjust EBITDA of $200 million increased 42% from $141 million in the first quarter 2019. Higher TiO2, zircon, feedstock and co-product sales volume combine contribute $34 million to the increase; favorable foreign exchange on cost of $7 million, again primarily the South African rand; $28 million of the increase came from the margin benefit from our shift to fully integrated operation; and synergy saving raised EBITDA by an additional $11 million.

As you can see, we are executing our [ph] plant (00:22:11) and generating significant momentum. Yes, global macroeconomic condition are uncertain. However, as Jeff said, many of the key drivers to increase our profitability are in our control, delivering the synergy and optimizing our global operating footprint. We are fully intend to meet our commitment to lower our costs, improve our product quality and generated cash using our advantage and integrated position.

With that, I thank you. I look forward to continuing to report on our progress and I'll turn the call over to Tim Carlson for a review of our financial position. Tim?

Timothy Craig Carlson

Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

Thanks, JF. Moving to slide 9 and starting with our balance sheet. On June 30, 2019, debt was $3.2 billion and debt net of cash and cash equivalents was $2.8 billion. Our liquidity was $798 million, comprised of cash and cash equivalents of $397 million and $401 million available under revolving credit agreements. And our net leverage on a trailing 12-month basis was 3.7 times. We continue to expect our net leverage to be under 3 times in 2020.

Regarding the legacy Cristal reporting concern, we identified following closing in April, it has been resolved. The pro forma adjusted EBITDA that Cristal generated in the first quarter was $61 million. The concern regarding non-current liabilities had offsetting adjustments to other balance sheet accounts and other comprehensive income. The concern regarding working capital was within accounting guidelines.

Our capital allocation policy is unchanged with the priority given to deleveraging and disciplined capital spending on high-return organic projects. As we said, share repurchase will be done solely on an opportunistic basis. Our capital spending in the second quarter was $56 million, well below our depreciation, depletion and amortization expense of $84 million. As you know, we did undertake significant share repurchases since closing the acquisition. We returned approximately $263 million to shareholders in the second quarter by repurchasing approximately 19 million shares and making our regular dividend payment.

On May 9 of this year, we repurchased 14 million Tronox shares from Exxaro for an aggregate purchase price of approximately $200 million or $14.32 per share. The share price was based upon a 5% discount to the 10-day volume weighted average share price as of the day that Exxaro exercised their sales notice to us.

On June 3, our board authorized the repurchase of up $100 million of Tronox shares. During the second quarter 2019, we repurchased 5 million shares under the repurchase program at an average price of $11.26 per share and at a cost of approximately $56 million. We continue to purchase in the third quarter. As of August 6, we have repurchased 7.5 million shares under the authorization at an average price of $11.59 per share and at a cost of approximately $86 million.

As a result, we've returned $294 million to shareowners from the start of our second quarter to August 6 by the repurchase of approximately 21.5 million shares and with our regular dividend payments.

Regarding our forecast for the second half 2019, as Jeff stated, we are maintaining our outlook for full year 2019 on a reported basis within the previously-provided ranges in narrowing guidance to the lower half of previous provided ranges for revenue of $2.83 billion to $2.98 billion and adjusted EBITDA of $635 million to $740 million respectively, to the high-end of previously provided range for adjusted diluted EPS of a negative $0.17 to $0.43 and within the previously-provided range for free cash flow of $130 million to $160 million.

With that, I thank you. I'll turn the call back over to Jeff for closing comments Jeff.

Jeffry N. Quinn
Chairman & Chief Executive Officer, Tronox Holdings Plc

Thanks, Tim. As you can see, we are executing well and have generated significant momentum. Despite a lot of noise in the general economic landscape is a good time for us at Tronox and we're bullish about the future both the long-term future and the near term. We are well-positioned relative to others in our space to deliver significant profitability and cash flow across varying macroeconomic conditions.

Many of the key drivers to increase our profitability are within our control such as delivering the synergies from the acquisition, optimizing our global operating footprint, taking advantage of our vertical integration, managing our overhead and wisely allocating our capital. We are indeed moving forward together as one New Tronox. We have a clear vision of what success looks like and clarity as to how we're going to get there.

As we've said, our mission is to be the TiO2 equity offering of choice, displaying greater stability, financial performance and cash generation across cycles, by utilizing our vertical integration and margins stabilizing commercial approach. We believe that the second quarter has been a very clear first step toward achieving that goal.

With that, I thank you. And, now, we'd like it – to open it up for your questions. Chris?

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] And our first question comes from the line of Duffy Fischer with Barclays. Your line is now open.

Patrick Fischer
Analyst, Barclays Capital, Inc.

Q

Yeah. Good morning. First question is just around the guidance. So, you did about $341 million in the first half, low-end of the guidance is, call it, $640 million. So, you've got about $300 million in the back half. That'd be $150 million a quarter and you're coming off a quarter where just did $200 million of EBITDA. So, that step-down of 25% on a quarterly run rate seems pretty large, given the synergies running through. Can you just walk through what drives that step-down?

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

A

Duffy, the number that you quoted for the first half was what, I'm sorry?

Patrick Fischer
Analyst, Barclays Capital, Inc.

Q

$341 million is your pro forma, right? The $200 million in the second quarter and the $141 million in the first quarter?

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

A

Yeah. And the guidance that we reported is on a reported basis. So, the $61 million that you've included in the first half is not in our full year number, because it's a reported basis number, not a pro forma number.

Patrick Fischer
Analyst, Barclays Capital, Inc.

Q

Okay. Okay. Well, okay. So, it still then would be about a $30 million step-down quarter-over-quarter. I mean, so, again, I guess just if you were to walk through kind of – if you start with the second quarter, we've got more synergies coming in quarterly, but there does definitely seem to be a step-down in run rate profitability. How much of that is zirconium and how – zircon and how much is TiO2?

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

A

So, the two components for it, we will see some additional synergies as we go through the back half of the year. As we go through the back half of the year, we'll also see the TiO2 seasonality with Q4 revenues coming down from Q3. And then, the zircon market, we've built in into our forecast a little bit of softness, but it is relatively flat.

And if you look at the guidance that we provided or the full-year guidance of the $635 million to the $740 million, thus guiding to the lower half of that, it really equates to a relatively level EBITDA performance Q2 to Q3 and then a slight $20 million to $30 million step-down in Q4 just given the nature of our business.

Patrick Fischer
Analyst, Barclays Capital, Inc.

Q

Okay. And then, second one, just on raw materials. Now, again, it doesn't affect you directly as much anymore since you're integrated. Obviously, it'll affect your competitors. How do you see kind of low-end and high-end ore prices moving over the next year?

Jean-François Turgeon
Chief Operating Officer & Executive Vice President, Tronox Holdings Plc

A

Well, maybe, Duffy, I can answer this one. It's JF. We see a very tight market in the high-grade feedstock side of the business. So, for everything that you can call, slag or natural rutile, synthetic rutile, it's a very tight supply demand market. In the ilmenite market, we see a balance supply/demand situation and with that a more homogeneous price for those product.

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc

A

Yeah. The price for ilmenite hasn't moved much since the numbers we kind of reported on Investor Day. So, it's been relatively stable.

Patrick Fischer
Analyst, Barclays Capital, Inc.

Q

Great. Thank you, guys.

Operator: Thank you. And our next question comes from the line of John McNulty with BMO Capital [ph] Group (00:32:12). Your line is now open.

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

Q

Yeah. Good morning. Thanks for taking my question. So, I guess, the first one, on the synergies that you realize, I mean you're clearly at least a little bit ahead of schedule, which is great. I guess can you give us an update as to how you're thinking about the yearend run rate and if that's going to also continue to stay ahead of schedule or if you kind of settle in more toward your original plan?

Jean-François Turgeon
Chief Operating Officer & Executive Vice President, Tronox Holdings Plc

A

Look, I'd say that it's good to be ahead and obviously we're working hard to try to remain ahead, but the guidance that we gave you in May at our Investor Day are still, I mean, our best guess of where we are. So, we forecast to be at $45 million deliver at the end of 2019. And obviously the run rate will be higher. So, we can hit the $120 million for the full year of 2020.

But look, what – as Jeff mentioned in his comment, every day, we found new project and new initiative that we didn't thought were there and that helped making sure that we will maintain this slightly ahead of where we want to be on the synergy.

Jeffry N. Quinn
Chairman & Chief Executive Officer, Tronox Holdings Plc

A

Yeah. And, John, obviously, one of the ways we realize we can create significant value is pulling forward that synergy capture and that's a focus that we have each and every day. And as we progress through the year, we'll continue to update on that. And certainly, once we get towards the end of the year, we'll provide even a more detailed reconciliation of all the various buckets in terms of where we are.

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

Q

Got it. Okay. And then, just as a follow-up, I guess you had a lot of optimism around interest in your kind of margin stabilization program post the close of the transaction, I guess, can you give us an update as to where you stand there and how much in terms of incremental interest you've been seeing since the close?

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc

A

Yeah. So, this is John Romano. As we've mentioned briefly on the call, we are getting traction on these margin stability initiatives. I'd say more so than we reported on Investor Day. Again, it's something that's going to take time. It's not going to happen overnight, but we're getting traction in both plastics and coatings markets. And that's not just in the Americas. So, it's in other regions of the world as well.

And when we think about how we're going about that, we're actually targeting strategic accounts where our intent is to grow there and to the extent we have offerings on our margin stability that is more attractive than our competitors, we are actually picking up business on long-term contracts. So, that's kind of the summary on that.

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

Great. Thanks very much for the update.

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc
A

Thanks, John.

Operator: Thank you. And our next question comes from the line of Frank Mitsch with Fermium Research. Your line is now open.

Frank J. Mitsch
Analyst, Fermium Research LLC
Q

Thank you so much and congratulations on the Ginkgo restart. I know that, that was a source of some consternation in the investment community. So, good to have that out of the way. We're seeing that, out of China, some price increases announced on TiO2. I think it's $50 a ton across the board. Where do you stand on price increases and just in general what is your expectations on TiO2 prices in the back half of this year?

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc
A

Hey, Frank. It's John Romano So, yeah, as recently as this weekend, there has been some movement with regards to people talking about price increases in China. That's on the back of what we saw in the last couple of months with some downward movement on pricing. It's one of the things, as a new company, we now have a much better visibility into the China market, because we have an asset over there.

So, I think [ph] sum (00:36:22) of what's driving the price increase announcements more recently is that China's golden year, which is their 70th anniversary of the founding of the People's Republic of China starts in October, that's the first full week of October. And there's a lot of prep going on in front of that and that preparation is slated to start as early as September. So, as you start creeping into the end of the year where the environmental regulations tighten up any way, there are planned outages that are going to take place. And I think that's putting some pressure on lower inventories and ultimately a drive to try to get additional pricing.

As far as the balance of our market, we have been working to increase prices. I'm not going to give a whole lot of color on exactly how we've done on that, but what I can say is that in the third quarter, we did have some success on pricing in Asia and Europe and we're continuing to focus on improving pricing as we move forward. That being said, just like pricing hasn't been moving down significantly over the last four quarters, we don't expect significant price movement up on pricing either and that's in line with our margin stability initiatives.

Frank J. Mitsch
Analyst, Fermium Research LLC
Q

So, John, so I should take that to mean that prices in 3Q are going to be flat to possibly up slightly sequentially from 2Q?

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc
A

That's a good assessment.

Frank J. Mitsch
Analyst, Fermium Research LLC

Q

All right. Terrific. And then, you characterized some of the softness on the zircon market and – owing to some of the macroeconomic softness in China I guess. So, what percent of China is your zircon sales?

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc

A

Well, demand for China is about – for zircon is about half on ceramics. So, it's a big part of it. And it's not only in China, that's the biggest area where we're seeing kind of a slowdown, but it's in Europe as well. So, as Jeff said and I think I've referenced, our sales moving into the second half is going to be around the same kind of profile we had in the first half, maybe slightly higher, where we would have previously forecasted a little bit stronger volume in that second half.

The second quarter was also – normally, I'm making comments about shipment timing having a negative impact on our quarterly volume. In Q2, it actually had a positive impact on our volume based off a roll-off from the previous quarter. So, we still are very optimistic about zircon moving forward in the mid to long term, but in the short term, I think China is driving a lot of trepidation in some of our customers minds around what might happen.

Frank J. Mitsch
Analyst, Fermium Research LLC

Q

All right. Fair enough. So, the way I should think about it is volumes maybe on the weak side, but pricing still stable on the zircon side.

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc

A

Yeah. We don't see a lot of movement on pricing and I would say volume is relatively stable.

Frank J. Mitsch
Analyst, Fermium Research LLC

Q

All right. Terrific. Thanks so much.

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc

A

Thanks, Frank.

Operator: Thank you. And our next question comes from the line of Hassan Ahmed with Alembic Global. Your line is now open.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC

Q

Good morning, guys.

Jeffry N. Quinn
Chairman & Chief Executive Officer, Tronox Holdings Plc

A

Hi, Hassan.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC

Q

Hi, there. Really a good volume growth sequentially on the pigment side, up 17%, but sort of more or less normal-ish year-over-year growth. So, I'm just trying to figure out this sequential uptick you guys saw in TiO2 volumes, was that primarily a result of, like you guys sort of alluded to in the release, the de-stocking phase being behind us. I mean was that where the bulk of that volume growth came from or was there some element of market share gains baked in there as well?

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc

A

Yeah. Thanks for that. Look, there were a variety reasons for that uptick. First, as I mentioned, the seasonal uptick in demand that always occurs in Q2 compared to Q1, although that was a bit muted this year due to the slower start to the coatings season, there was also the pickup in demand that we saw in Q2, reflecting the completion of the destocking in Europe and Asia. And as a combined company, that was a bit more significant due to our larger footprint in Europe.

And then, the impact of the legacy Cristal market adjustments to regain share that started in the second half of 2018, which had an impact on our volume moving into the first half of the year. And lastly, as I mentioned just a minute ago, our margin stability initiatives. Again, we're targeting customers with these unique initiatives, in some instances, our value proposition is more attractive than our competition and we are securing contracts for larger volume, but not on the back of price.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC

Q

Understood. Understood. Now, on the on the feedstock side, again, sequentially pro forma revenue is up 19%. It seems to me that the bulk of that sort of uptick came from high-grade ore pricing improvements, because obviously you guys talked about the sort of volume increment on the CP slag side being offset by volume declines in the ilmenite side. And obviously, you pointed out why those volumes declined in ilmenite, obviously using it for internal sort of purposes and the like.

And it also seems that you sounded quite positive about a continuation of pricing increments on the high-grade ore side. So, a two-part question. One is do you continue to see even in this sort of erratic macro-environment supply/demand tightness in high-grade ore 2019 into 2020? And the second part of that is that obviously you guys must have between yourself and legacy Cristal some legacy contracts in place. Have most of those legacy contracts expired? I mean, if you could just give me a sense of what percentage of business is being done sort of at market price.

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc

A

So, as far as legacy contracts, we only have one contract on high-grade feedstock and that is with the company that acquired Ashtabula. That's by contract and the agreement we had with them. So, that volume is actually lower than what we have sold historically. Timing of shipments had something to do with the uptick, but ultimately, we will be consuming, long term, all the feedstock internally.

So, the contracts that we have right now, I wouldn't say are old legacy, they're relatively new, but there's only one of them.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC

Q

Understood. And just about pricing prospects just for high-grade ore 2019 into 2020, even in this sort of uncertain macro.

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc

A

Yeah. Look, at this particular stage, we would continue to see upward movement on pricing for high-grade feedstock. We're in the market also for high-grade feedstock and we're continuing to see pressure on the upside.

Jeffry N. Quinn
Chairman & Chief Executive Officer, Tronox Holdings Plc

A

Yeah. The tightness in the market as JF said earlier.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC

Q

Very helpful, guys. Thank you so much.

Operator: Thank you. And our next question comes from the line of Jeffrey Zekauskas with JPMorgan. Your line is now open.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Thanks very much. What were operating rates at Yanbu a month ago and what are they now? And can you talk about the changes that are going on at that facility?

Jean-François Turgeon
Chief Operating Officer & Executive Vice President, Tronox Holdings Plc

A

So, Jeff, it's JF here. Look, Yanbu, at the moment, is the asset where we want to increase the quality. So, our focus has not been on volume, but our focus has been on quality to really change the perception of our customer of what can be produced in Yanbu.

And remember at Investor Day, I made that comment that with the last 20 year we have improved significantly Hamilton product and Yanbu is a copy of Hamilton and we have very easy change that we have put in place to significantly lift the quality out of Yanbu. Well, we will obviously adjust the volume based on the demand and based on John possibility of selling more material and that's always been our strategy to adjust our production to the market demand.

And I think I'd like to make the comment, because I heard that comments from some of our competitor, I believe that we probably have the best capability to increase production as needed with no capital requirement, because what we have done in our legacy Tronox [ph] Plan (00:45:49) by what I call delivering the hidden factory, well, that's why we did that deal to be able to deliver the hidden factory out of the legacy Cristal asset, but we'll do that as the market requests this new tonnage.

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc

A

Jeff, remember at our Investor Day, we talked a lot about the unified commercial approach being such a critical part of our strategy going forward. And we talked about how we would feather into the market as the market demanded it, incremental production that we have from the legacy Cristal operations. And that's exactly what we're doing. And because it is a commercial-driven strategy, that quality need in the market and the market being receptive to a higher-quality product coming out of the Yanbu has been a very early focus of ours and we've made progress in that regard.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

So, maybe just to re-ask it, how long do you think it will take you to get the Yanbu quality up to standard if you can forecast that? Will you have that done by the end of the year or it's too hard to know?

Jean-François Turgeon
Chief Operating Officer & Executive Vice President, Tronox Holdings Plc

A

Well, it's a range of change. And I can tell you that there is some action that we have took that already have increased some of the product out of Yanbu. There is grade that are legacy Tronox grade that we want to start producing in Yanbu, that we expect to produce in 2020.

So, I'd say that it's hard to answer with a very fixed number of month, but I can tell you that there is already product that is better than it was out of Yanbu after three months. And I'd say within the next year, we'll continue to have new grade and new product.

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc

A

Yeah. And, Jeff, there's no silver bullet there in Yanbu as we knew. It's the combination of dozens of projects and initiatives that will improve the quality and liberate the incremental volume over time and we are systematically and thoughtfully pursuing those and the team there, now that we've put in place with some of the help and expertise from our global operations and the energized team there at Yanbu, we feel really good about the path there and the progress we've made.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Okay. Just a financial question, what's your share count after you factor in all of the repurchases that you've made thus far? And I realize that there's a difference between the average share count and the actual share count. But if you made no more share repurchases, what would your share count be either in the third quarter or in the fourth quarter?

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

A

About 142 million, Jeff.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

142 million. And are there further share repurchases that you expect to make to the end of the year?

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

A

The $100 million that the board authorized back in June, that authorization was within the 10% limitation permitted under Section 382 of the Code. So, we can't go above that without jeopardizing 382. That obviously resets again next year. So, as of now, there's no anticipated repurchases beyond what we've already announced.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Okay good. All right. Thank you so much.

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

A

Thanks, Jeff.

Operator: Thank you. And our next question comes from the line of Jim Sheehan with SunTrust. Your line is now open.

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Thank you. Good morning. So, TiO2 prices have stabilized at a higher level in this cycle than in previous troughs. Do you credit your margin stability discipline for that and how sustainable might that pricing stability be? Do you have any concern that competitors will reverse their stability strategies and disrupt the market in order to regain market share?

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc

A

Yeah. Look, so I do and I think we mentioned this previously, I do think that the initiatives on margin stability have had an impact on this last mini cycle, because volume – typically, you'll get pricing that will drop quarter-to-quarter far in excess of 1% in a down-cycle. And over the last several quarters, we've had 1%-ish price decline. And in this particular quarter, pricing stabilized.

So, I do believe that margin stability initiatives have had a positive impact. And I also believe that, as we move forward, I can't predict or understand exactly what my competitors are going to do, but I do believe that there's enough momentum with margin stability out there that as we move forward, it's our expectation that this will continue and that's going to drive positive results for Tronox.

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Great. And could you give some more color on the Cristal reporting issue? So, is it true that inventory was not actually overstated and therefore we should not expect a true-up?

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

A

The inventory balance was within the accounting guidelines. The EBITDA that we talked about has been reported on Investor Day was $63 million. The pro forma adjusted EBITDA was $61 million. So, the concerns that we had on working capital ended up all being within the accounting guidance.

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.
Q

Thank you.

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc
A

Thanks, Jim.

Operator: Thank you. And our next question comes from the line of Vincent Andrews with Morgan Stanley. Your line is now open.

Steven Haynes
Analyst, Morgan Stanley & Co. LLC
Q

Hi. This is actually Steve Haynes on for Vincent. Maybe just at the industry level, on the demand side, what kind of underlying volume assumptions are baked into the back half guidance for 2019 and then kind of going into 2020? And maybe any changes to that outlook given the macro uncertainty you guys are setting? Thanks.

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc
A

Yeah. So, as we look into the back half of the year, our forecast has the second half looking very similar to the first half. There might be a little upside. And moving into 2020, as our position hasn't really changed much, it's in the 3%-ish range 2019 to 2020 on growth.

Steven Haynes
Analyst, Morgan Stanley & Co. LLC
Q

Thank you.

John D. Romano
Executive Vice President & Chief Commercial and Strategy Officer, Tronox Holdings Plc
A

Thank you.

Steven Haynes
Analyst, Morgan Stanley & Co. LLC
Q

Thank you.

Operator: Thank you. And our next question comes from the line of Roger Spitz with Bank of America. Your line is now open.

Roger Spitz
Analyst, Bank of America Merrill Lynch
Q

Thank you and good morning. Can you provide Cristal's Q3 2018 pro forma without Ashtabula sales and EBITDA and that of Q4? We have the 2H 2018 numbers, but want to see if we can get a quarterly breakdown of the sales and pro forma EBITDA.

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

A

Hey, Roger, I don't have that handy. My apologies, but we'll make sure we can get that out at some point.

Roger Spitz
Analyst, Bank of America Merrill Lynch

Q

Thank you. So, you lowered your EBITDA guidance a bit lower half of the range, but kept the free cash flow the same. Can you just comment on that and perhaps update us on the other items that you provide on the Investor Day for the cash flow items between EBITDA and free cash flow, CapEx, cash interest, et cetera, whatever might have changed?

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

A

Yeah. We'd be happy to, Roger. The – these have – favorability on the free cash flow line, slightly lower capital expenditures, slightly lower cash taxes, a little bit of improvement in the working capital. As you look at the full year, as it relates to our free cash as reported, our capital is probably going to be in the $230 million to $250 million range. Cash taxes in the $25 million to $40 million range. And then, the working capital, we expect a little bit of a continued improvement as we drive some of our working capital initiatives with the combined company.

Roger Spitz
Analyst, Bank of America Merrill Lynch

Q

Thank you. And lastly, what is the timing of the additional 14.7 million Tronox shares as well as the 7 million Tronox South African shares that you might, at some point, be – plan to acquire from Exxaro Resources.

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

A

Yeah. So, Exxaro has, obviously, the right to sell those shares whenever they should desire to sell those shares. Based upon the discussions we had with them with the last marketing request, I anticipate that they would sell around the $14 and $15 range. I don't think they're a seller at the current prices. If the stock does recover, I would anticipate that we would get a marketing notice that gives us 60 days to prepare.

As it relates to 7.2 million share flip-in, Exxaro has the right as well to not accept our offer to flip those shares in. And given the indications that they're looking at a $14 to $15 stock price, even if we requested to flip that in, they wouldn't accepted it. So, I would expect no activity until we see a recovery in the market.

Roger Spitz
Analyst, Bank of America Merrill Lynch

Q

Thank you very much.

Operator: Thank you. And I'm not showing any further questions at this time. I would now like to turn the call back to Jeff Quinn for any closing remarks.

Jeffry N. Quinn

Chairman & Chief Executive Officer, Tronox Holdings Plc

Thank you, Chris. In summary, we're off to a good start for the New Tronox. We are well positioned. We are bullish about the future. We are focused and locked in on execution. And that's achieving results that are reflected in our results for the second quarter.

We look forward to continue to dialogue with you as we move forward about the value we're creating, the capture of synergies and building the world's greatest TiO2 organization. We look forward to submitting our position as the TiO2 equity of choice and dialoguing with you about that as we move forward. So, have a good day. Thank you for your time this morning and thank you for your continued interest in our company.

Operator: Ladies and gentlemen, thank you for participating in today's conference. This does conclude today's program. You may all disconnect. Everyone, have a great day.