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MPMQ - Q3 2017 MPM Holdings Inc Earnings Call

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CORPORATE PARTICIPANTS

Erick R. Asmussen *MPM Holdings Inc. - Senior VP & CFO*

John G. Boss *MPM Holdings Inc. - CEO, President & Director*

John Kompa *Hexion Inc. - VP of IR & Public Affairs*

CONFERENCE CALL PARTICIPANTS

Alex Kayvanfar

Christopher Anthony Ryan

Nathan E. Schubert

PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Momentive Performance Materials' Third Quarter 2017 Earnings Call. (Operator Instructions) As a reminder, this conference call is being recorded. I'd now like to introduce your host for today's conference, Mr. John Kompa, Investor Relations. Sir, you may begin.

John Kompa - *Hexion Inc. - VP of IR & Public Affairs*

Thank you, Jimmy. Good morning, and welcome to Momentive's Third Quarter 2017 Earnings Conference Call. Leading today's call will be Jack Boss, Chief Executive Officer and President; and Erick Asmussen, Senior Vice President and Chief Financial Officer. As a reminder, this call is also being webcast, and the slides referenced in today's conference call are available through the momentive.com website under the Investor Relations section. A replay of this call will be available by telephone for 1 week, and the replay dial-in information is contained in our latest earnings release. A replay of this call will also be posted on our website.

Before we start, I'd like to read information about forward-looking statements and the use of non-GAAP information as part of this call, as highlighted on Page 2.

As you know, some of our comments today may include statements about our expectations for the future. Those expectations are subject to known and unknown risk, uncertainties and other factors that may cause the company's actual results and performance to be materially different from any future results or performance suggested by these expectations.

The slide you now see gives you more information on the assumptions and factors we consider in making those forward-looking statements. We can't guarantee the accuracy of any forecast or estimates, and we undertake no obligation to update any forward-looking statements during the quarter, except as otherwise required by law.

For more information on our risk factors, please see our earnings press release and our SEC filings. In addition, some of our comments may reference non-GAAP financial measures, including EBITDA. The most directly comparable GAAP measures are set forth in our presentation, and reconciliations to such GAAP financial measures and other associated disclosures are contained in our earnings release and on our website. Our earnings release and our recent SEC filings are available on the Internet at momentive.com. With that, I'll now turn the call over to Jack Boss to discuss our latest results.



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John G. Boss - MPM Holdings Inc. - CEO, President & Director

Thanks, John, and good morning, everyone. I'm pleased to report another solid quarter as we continue to execute our long-term strategic growth plan and drive profitable growth and year-over-year EBITDA gains.

In the third quarter, we posted strong net sales growth of 5% from the prior year, primarily reflecting gains across the specialty portfolio. In the third quarter, segment EBITDA increased 2% year-over-year, reflecting an increase in net sales, partially offset by the timing of production facility turnarounds. On a year-to-date basis, segment EBITDA and margins increased 21% and 190 basis points, respectively. The timing of our turnarounds year-over-year had a \$7 million impact on EBITDA in the quarter. Our facilities have all started up in normal course, we are now at full production and our strategic capital management program remains on track. In addition, we recently raised prices across our silicones portfolio, and we expect that the financial impact will be realized in the fourth quarter of 2017 and first quarter of 2018, which will drive improved margins.

Moving into the fourth quarter. Our order book is strong across all business units with expected year-over-year improvement in EBITDA in the fourth quarter. In the third quarter of 2017, we reorganized our segment structure to better reflect our specialty chemical portfolio and the related performance.

Turning to our new segments. Slide 5 presents our quarterly performance additives segment results. We were pleased to post continued strong growth across our Performance Additives portfolio, which includes specialty fluids, urethane additives and silanes.

Performance Additives' net sales increased 4% in the quarter and 5% on a year-to-date basis. Our Performance Additives segment EBITDA was impacted by the onetime effects of Hurricane Harvey, plant turnaround expenses and temporary lead-lag on raw material pricing. Again, our operations have since started up in normal course and we are at full production. In addition, price increases have been implemented and will be realized in Q4 of '17 and early Q1 of 2018.

Looking ahead, our order book is strong along all business units, and construction of our NXT expansion in Germany remains on track to be completed by year-end and to start up in the first quarter of 2018.

Now turning to our Formulated And Basic Silicones segment on Slide 6. Third quarter net sales were up 4%, reflecting growth in specialty formulated products, partially offset by an intentional reduction in our Basic Silicones business. Specially formulated growth was driven by strong demand in electronic materials, elastomers and sealants and coatings markets. We are continuing to see the benefits from the transformation of our Germany site that began in Q4 2016. This strategic initiative reduced our Basic Silicones portfolio and is part of a broader focus on optimizing assets and expanding downstream specialties.

Segment EBITDA was flat, reflecting growth in specialties and a reduction in basic silicones, offset by facility turnaround expenses and temporary raw material lead-lag.

As I mentioned a minute ago, our operations have started up in normal course and we are now at full production. We also remain vigilant in realizing appropriate value for our products in the market, and we've implemented price increases, which we expect to be realized in Q4 '17 and early Q1 of '18.

Year-to-date segment EBITDA and margins were up 39% and 230 basis points, respectively, due to our multiyear growth investments, restructuring benefits and improved mix.

Looking ahead, our order book and outlook for Formulated and Basic Silicones remains strong, driven by demand in automotive, consumer products and industrial end markets.

Turning to our Quartz Technologies segment on Slide 7. Quartz Technologies' net sales increased 19% in the quarter and 21% on a year-to-date basis, driven by improved demand in semiconductor and aerospace markets. Our Quartz Technologies segment EBITDA increased 117% in the quarter and 131% year-to-date, driven by higher net sales, operating leverage and substantially improved manufacturing efficiencies. The outlook



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for Quartz Technologies heading into Q4 and full year '18 remains strong due to continued strong volumes from semiconductor and our aerospace markets.

Now let's turn to our company-wide strategic investments on Slide 8. We continue to make targeted investments throughout our global operations to transform our assets. The most recent example is the installation of a state-of-the-art extruder at Waterford to increase our silicone sealant coatings and roof coat capacity to support the growing building solutions market. The new manufacturing design and robotics technology improves process automation and increases site productivity. We're also pleased to serve as the exclusive global licensee of GE-branded silicone products.

In addition, we steadily work to create a globally competitive cost structure. As previously announced, our global restructuring program and our Leverkusen, Germany siloxane production transformation is complete, and these programs are expected to generate approximately \$48 million in annual savings.

As of September 30, Momentive had \$6 million of pro forma cost savings under these programs yet to flow to our financial results. We continue to evaluate additional structural cost-saving opportunities focused on asset optimization and expanding our downstream specialties. Now let me turn the call over to Erick Asmussen, our CFO, to discuss our balance sheet.

Erick R. Asmussen - MPM Holdings Inc. - Senior VP & CFO

Thanks, Jack. We continue to maintain a strong balance sheet with significant liquidity, and we have steadily delevered from 5.9x in 2015 to 4.3x. At the end of the third quarter, we had cash plus borrowing availability of \$358 million, and we have no significant debt maturities until 2021. We continue to invest in areas where we have a strategic advantage, and in the first 9 months of 2017, capital expenditures totaled \$123 million. We now expect to invest approximately \$160 million in capital expenditures during 2017 as we deploy increased amounts of growth capital to take advantage of opportunities we see in the market. Net working capital was \$485 million at the end of the third quarter, and we remain focused on optimizing our net working capital. Now I'll turn the call back over to Jack.

John G. Boss - MPM Holdings Inc. - CEO, President & Director

Thanks, Erick. We're pleased with our continued strong financial and operational performance as we continue to execute our strategy. Our third quarter net sales and segment EBITDA increased 5% and 2%, respectively. Our segment EBITDA and related comparability was impacted by facility turnarounds in the third quarter. On a year-to-date basis, sales and segment EBITDA grew 3% and 21%, respectively. Our order book and outlook remains strong across all business units. And as I mentioned, we recently raised prices across our silicones portfolio. As a result, we expect year-over-year improvement in EBITDA in the fourth quarter. Our growth investments remain on track to drive growth in 2018 and beyond. Our NXT expansion will be complete by year-end, and is scheduled to come online in the first quarter of next year.

In closing, you can see we're excited about our performance, we're excited about our fourth quarter outlook and our growth trajectory as we head into 2018.

John Kompa - Hexion Inc. - VP of IR & Public Affairs

Thanks, Jack. Operator, we'd now like to open the line for questions. If you could please remind callers of those instructions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Nathan Schubert from JPMorgan.



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Nathan E. Schubert

So first just on the NXT expansion. Can you talk about your expectations, once completed, as far as the ramp up and full year 2018 contributions? And then also, how we should think about the CapEx impact step down from the completion?

John G. Boss - MPM Holdings Inc. - CEO, President & Director

Yes. So as we've talked about many times, the market continues to grow at double digits. And so we expect to continue to fill up our Texas City plant as well begin to fill up the NXT plant in Germany. I mean, Q1, we'll be starting up and qualifying customers, so we really won't launch into commercial sales until the back half of the year, second quarter leading into the third quarter. As we've always talk about, good investment, strategic business for us, 20% IRR minimum is always our target. And so we expect that to accrue next year to our both sales and EBITDA.

Erick R. Asmussen - MPM Holdings Inc. - Senior VP & CFO

And, Nathan, look at the -- about \$30 million of the capital program would be NXT. So that would be sort of your step down related to that project.

Nathan E. Schubert

Okay. And then moving onto the bankruptcy court ruling. I know you're probably limited on what you can talk about, so to the extent you are able to, can you just discuss your expectations around the time line? And then what you're thinking in terms of the potential outcome?

John G. Boss - MPM Holdings Inc. - CEO, President & Director

Yes, sure. I'll start and Erick, you can follow on. But -- they rule on 2 of the 3, as we see it in our favor once again for the make whole and subordinated debt we were happy with. On the interest rate formulation, we're still evaluating our options on how we manage that going forward. So that's about, I guess, all we can say, Erick. And if you have any further comments. But we're still evaluating next steps there, and 2 of the 3 we felt really good about.

Nathan E. Schubert

Okay. So no really commentary on, sort of, time line?

John G. Boss - MPM Holdings Inc. - CEO, President & Director

No. We can't really comment too much -- in any more detail.

Operator

(Operator Instructions) Our next question comes from the Roger Spitz from Bank of America.

Christopher Anthony Ryan

This is Chris Ryan on for Roger. My first question is, for the turnarounds, can you say which facilities had turnarounds in Q3 '17? And was there one that represented the bulk of the \$7 million in turnaround costs?



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John G. Boss - MPM Holdings Inc. - CEO, President & Director

Erick, you want to give the highlights on that one?

Erick R. Asmussen - MPM Holdings Inc. - Senior VP & CFO

Yes. If you look, we had -- the major turnarounds were Waterford and our Japan facility, the largest of which was the Waterford facility, which had a larger turnaround effect because last year, we had a much shortened process because of the strike.

Christopher Anthony Ryan

Okay. And then what was the split from the lead-lag on raw material prices between Performance Additives, Formulated and Basic Silicones and Quartz?

John G. Boss - MPM Holdings Inc. - CEO, President & Director

Yes, I don't know that I have this -- the total breakdown, but I can say that most of it was in our was in our performance additives business. I think it's -- and it's fair to say that most of the lead-lag impacts around some of our nonkey raw materials that were flowing through our Performance Additives segment, which we've since raised prices on, and we'll see that margin improve in Q4 and beyond.

Christopher Anthony Ryan

Okay. And finally, is there any consideration of repurchasing or refinancing the bonds in the near term?

John G. Boss - MPM Holdings Inc. - CEO, President & Director

Erick, do you want to?

Erick R. Asmussen - MPM Holdings Inc. - Senior VP & CFO

As you can appreciate the company evaluates all capital strategic options. And while we can't comment, we assess all opportunities appropriately using, sort of, the capital alternatives for growth as a threshold.

Operator

And our next question comes from Alex Kayvanfar from Redwood Capital.

Alex Kayvanfar

Just a quick one on the unrestricted subsidiary that was designated restricted. Just wanted to see if you could provide any color on that and why that was the case.



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Erick R. Asmussen - *MPM Holdings Inc. - Senior VP & CFO*

Yes, that was more, I think, of a legacy, yes. It was -- it created some optics issues, frankly, as it relates to the bank EBITDA, adjusted EBITDA and segment EBITDA. And frankly, there -- if you look at the amount of leverage in China, it's well below the basket. We didn't have some of the cross default issues that existed preemergence. So at this juncture, it's one that we made the decision to change that to allows for better clarity and better alignment between adjusted EBITDA and our segment EBITDA.

Operator

And we have one follow-up question from Roger Spitz (sic) [Christopher Ryan] from Bank of America.

Christopher Anthony Ryan

Just to get clarity on the resegmentation. Is the -- is basic silicones, siloxanes and some other basics? And what's the difference between formulated siloxanes and Performance Additives, presumably the latter is more specialty products?

John G. Boss - *MPM Holdings Inc. - CEO, President & Director*

Yes. We -- so we change just to get better clarity on our specialty portfolio and how each one performs. I mean, the specialty additives, the Performance Additives segment is truly additive specialties. You can see the margins are different in that segment than on the other ones. So I really wanted to highlight that as a key business we have. And the other one is -- Formulating basics has both our Basics business and our old Formulated Products business in there. So it's a mix of some high-end specialties as well as some of our basic siloxane products.

Operator

And as I see no further questions, I'd like to turn the back -- call back over to Jack Boss, CEO.

John G. Boss - *MPM Holdings Inc. - CEO, President & Director*

Well, thanks. And thanks for joining our call today. We continue to execute, like I said, on our strategy of accelerating profitable growth, transforming our global operations and evolving our culture. We remain on track to continue to deliver sustainable EBITDA growth, and we look forward to updating you on our fourth quarter call. Thanks, everyone.

Operator

Ladies and gentlemen, this does conclude your program for today. And you may all disconnect. Everyone, have a great day.



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