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MPMQ - Q2 2018 MPM Holdings Inc Earnings Call

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CONFERENCE CALL PARTICIPANTS

Nathan Edward Schubert *JP Morgan Chase & Co, Research Division - Research Analyst*

PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Second Quarter 2018 Momentive Performance Materials' Earnings Conference Call. (Operator Instructions) As a reminder, this conference is being recorded.

I would now like to introduce your host for today's conference, John Kompa, Investor Relations for Momentive. Please begin.

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

Thank you, Norma. Good morning, and welcome to Momentive's Second Quarter 2018 Earnings Conference Call. Leading today's call will be John 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 one week, and the replay dial-in information is contained in our latest earnings release. A replay of this call will be also 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. Please note, our results are unaudited and the final unaudited financials will be included in our quarterly report on Form 10-Q. Our earnings release and our SEC filings are also available on the Internet at momentive.com.

With that, I will now turn the call over to Jack Boss to discuss our latest results.

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

Well, thanks, John, and good morning, everyone. I am pleased to report another quarter of strong financial performance. We continue to deliver year-over-year gains, reflecting organic growth, contributions from our multi-year capital investments and our efforts to optimize our basics



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portfolio. Our results also reflect our strategic alignment with secular mega trends and continued market penetration into auto, consumer goods, electronics, construction and personal care.

With the strong first half of the year, we remain well positioned for long-term growth and continued margin expansion. In the second quarter, revenue grew 19%, driven by improved market dynamics in our basics end markets and gains in our specialty portfolio. We drove a 53% increase in segment EBITDA for the quarter, reflecting improved market dynamics in our basics end markets, volume growth throughout nearly all the portfolio and contributions from our recent strategic growth capital investments. These factors also drove a 360 basis point increase in our segment EBITDA margins. We began the third quarter of 2018 with a robust order book across all business units.

Turning to Slide 5. We'll now look at the individual segment results. In our Performance Additives segment, we continue to focus on providing value-added differentiated solutions for our global specialty fluids, silanes and urethane additives customers. We drove strong sales and volume growth across the portfolio, as second quarter sales increased 10%, reflecting positive demand in the automotive, agricultural and personal care end markets.

Performance Additives segment EBITDA was \$50 million, an increase of 4% over the prior-year period, reflecting volume growth and contributions from our strategic growth investments, partially offset by NXT start-up costs from our new facility in Leverkusen, Germany, and a temporary impact of higher input costs in our urethane additives end markets.

On Slide 6, I'll discuss our Formulated and Basic Silicones segment. Our earnings more than doubled in our Formulated and Basic Silicones segment in the second quarter. This segment contains both very high-end specialty products, such as our coatings and electronics, as well as our basic silicone products. We strategically focused on increasing our specialty product sales to improve our overall product mix. This strategy continues to pay dividends, as sales in the second quarter were up 27%, reflecting improved dynamics in our basic end markets and volume gains across the electronics, coatings and industrial end markets.

Segment EBITDA for the second quarter was up 133% or \$36 million year-over-year as a result of volume growth and the successful implementation of pricing actions in both the specialty and the basic portions of our portfolio. Segment EBITDA margins rose sharply, increasing 720 basis points in the quarter.

Turning to Slide 7, I'll discuss our Quartz Technologies segment. Quartz Technologies sales increased 6% in the quarter, driven by continued positive semiconductor demand. Quartz Technologies segment EBITDA increased 20%, driven by higher sales and increased operating leverage. Specifically, we benefited from our lean and continuous improvement initiatives, which resulted in improved yields in our Quartz production sites. The outlook for Quartz Technologies remains positive for the remainder of 2018, based in our -- based on our leading technologies and continued positive market outlook.

Before turning it over to Erick to discuss our balance sheet, I want to update you on the progress of our strategic growth programs.

Turning to Slide 8. Our clearly defined growth strategy is focused on specialties, and this slide highlights a few key investments. First, one of our largest strategic investments is our NXT product line, which is key to expanding our already significant presence in the auto industry. Our NXT silanes help global tire producers enhance product performance. For example, Momentive NXT silanes improve the rolling resistance of tires without the loss of wet traction. I'm pleased to report that the NXT plant commissioning process is proceeding as planned and production is expected to steadily ramp up throughout 2018.

We're also investing in key strategic geographic regions, in Latin America, which remains a key growth region for us. We've recently added capacity in Itatiba, Brazil for our specialty fluids business. This investment supports our local customers in Brazil and throughout Latin America, particularly in the fast-growing agricultural, personal care and textile end markets.

In the Asia Pacific region, we're strengthening our already significant presence by expanding our manufacturing and R&D capabilities in Seoul for our electronic materials business. This positions us closer to key customers and at the epicenter of the electronics industry, which will allow us to further capitalize on growth opportunities within the emerging display and integrated electronics material space.



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And finally, we're expanding our Ohta, Japan site to meet the growing demand for silane products. This expansion, which we expect to be completed by the end of 2018, will support growth in our industrial coatings business, specifically high-temperature resistant coating applications.

I'll now turn the call over to Erick, who will summarize our balance sheet on Slide 9.

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

Thanks, Jack. We continue to maintain a strong balance sheet with significant liquidity. Our net debt-to-EBITDA ratio now stands at 3.2x. Our strong earnings momentum drove free cash flow of \$28 million in the quarter, and at the end of the second quarter, we had cash plus borrowing availability of \$448 million compared with \$417 million at the end of the first quarter of 2018. Finally, we are maintaining significant financial flexibility, while we drive our growth investments, and we expect to invest approximately \$125 million in total capital expenditures in 2018.

Now I'll turn the call back over to Jack to close.

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

Thanks, Erick. To sum up, we continue to drive strong results, with second quarter revenue gains of 19%, segment EBITDA increase of 53% and EBITDA margin improvement of 360 basis points.

We remain focused on executing our strategy of growing our higher-margin specialty applications, while optimizing the basics business and improving our overall cost structure. Our previously announced restructuring program is expected to deliver approximately \$8 million in savings this year, which will support continued earnings growth and margin expansion.

We have a robust order book, strong demand and a favorable outlook for the balance of the year due to positive industry fundamentals and upside from our key growth investments.

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

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

QUESTIONS AND ANSWERS

Operator

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

Nathan Edward Schubert - *JP Morgan Chase & Co, Research Division - Research Analyst*

So my first question is just kind of generally -- general silicone market fundamentals. It sounds -- one of your competitors was out there saying that there's a significant imbalance between supply and demand and that debottlenecking isn't -- alone is not going to be sufficient to bridge the supply gap. So just what are your thoughts on significant new capacity? What does that take? When will we see that, obviously, with that?

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

No, it's a great question, because -- I would concur. The operating rates in the industry right now are about as good as they've been. The good news is, the silicone industry, as you probably know, has grown historically at above GDP and is expected to continue even at a faster clip. So there

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will need to be new capacity come online at some point. As we look out at least for the next couple of years, we don't see any new significant capacity coming online globally. So we expect the dynamics and the operating rates that exist today to continue at least for the next couple of years, and beyond that, it's kind of hard to predict, if any new capacity will come on, and if so, where and how much. So at least as we look out through 2020 and into 2021, we don't see a lot changing in the dynamics that we're seeing today in the industry.

Nathan Edward Schubert - *JP Morgan Chase & Co, Research Division - Research Analyst*

Okay. Great. And then just to follow up on that is, can you just kind of maybe ballpark how much it would cost for 1 ton of additional capacity as you think about like a greenfield and also a brownfield plant? Like, how should we think about total cost in terms of new capacity?

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

Yes. I can't specifically -- we haven't made a large investment in new site. I think, you're referring to siloxane capacity. Obviously, we put a lot of investments in our growth programs for finishing and specialty capacity, but I think you're referencing, really, the siloxane, the key building block for the industry. And you can go back on one end of the spectrum, Dow Corning was \$2-plus billion in 4 years, when the WACKER-Dow Corning joint venture went in back several years ago. We don't see anything of that magnitude coming back into play. It'd be more sort of incremental investments, 50 KMT, 100 KMT. I don't have any good numbers to be honest. Obviously, brownfield is less than a greenfield, but don't have great numbers around what that would require, other than it's big numbers. They're typically not tens of millions, they're more like hundreds of millions to put in a siloxane facility anywhere in the world.

Operator

(Operator Instructions) Our next question comes from Roger Spitz of Bank of America Merrill Lynch. At this time, I would like to turn the call back over to Mr. Jack Boss, CEO, for closing remarks.

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

Okay. Thanks, operator, and thanks to everyone for joining our call today. We had a strong second quarter and a strong first half of the year. And we remain enthusiastic about the full year outlook for the company. I look forward to updating you on our next earnings call. Thanks.

Operator

Ladies and gentlemen, thank you for your participation in today's conference. You may disconnect. Have a wonderful day.

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