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# EDITED TRANSCRIPT

OLN - Olin Corp Second Quarter And Full Year 2016 Guidance Call

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**OVERVIEW:**

OLN updated its 2Q16 and full-year 2016 outlook.



## CORPORATE PARTICIPANTS

**Larry Kromidas** *Olin Corporation - Director, IR*

**John Fischer** *Olin Corporation - President & CEO*

## CONFERENCE CALL PARTICIPANTS

**Frank Mitsch** *Wells Fargo Securities, LLC - Analyst*

**Jason Freuchtel** *SunTrust Robinson Humphrey - Analyst*

**John Roberts** *UBS - Analyst*

**Aleksey Yefremov** *Nomura Securities Company, Ltd. - Analyst*

**Arun Viswanathan** *RBC Capital Markets - Analyst*

**Karl Blunden** *Goldman Sachs - Analyst*

## PRESENTATION

### Operator

Good morning and welcome to the Olin earnings update conference call.

(Operator Instructions)

Please note, this event is being recorded. I would now like to turn the conference over to Larry Kromidas. Please go ahead.

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### Larry Kromidas - Olin Corporation - Director, IR

Good morning, everyone. Before we begin our discussion this morning, I want to remind everyone that this presentation, along with the associated slides and the question and answer session that will follow our prepared remarks, will include statements regarding estimates of future performance. Please note that these are forward-looking statements and those results could differ materially from those projected. Some of the factors that could cause actual results to differ are described without limitation in our Risk Factors section of our most recent 10-K, and in our latest press release.

A copy of today's transcript and slides will be available on our website in the Investor section under Calendar of Events. The press release and other financial information are available under Press Releases.

Our expectation during our 30 minute call this morning is to provide you with some details on what changes occurred between our second quarter guidance and our preliminary second quarter results concerning caustic soda, ethylene dichloride and our chlorinated organics business.

Now I'd like to turn the call over to John Fischer, President and Chief Executive Officer. John?

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### John Fischer - Olin Corporation - President & CEO

Thank you for joining us today. This morning we provided detailed slides covering some specifics regarding caustic soda, EDC and the chlorinated organics business and I will refer to these slides this morning as I go through my presentation.

On slide 2 we provide a bridge from the second quarter guidance that we provided to our revised outlook. A couple of comments. We did experience a rapid run-up in the cost of both natural gas and ethylene from late May through June, and this negatively impacted our second quarter costs compared to our second quarter forecast. Natural gas prices in June were approximately \$1 per MBtu higher than the April and May average and



those were the basis of our forecast. Ethane prices increased approximately 40% in June compared to the April-May levels which our forecast was based on.

The third slide covers caustic soda. On caustic soda, first let me discuss the second quarter. Olin had forecasted its second quarter caustic soda price would be similar to the first quarter and instead experienced a sequential decline. This price decline compared to the first quarter reflects a less favorable mix between domestic and export sales, the first quarter index declines which impacted second quarter pricing and the normal contract lags that limited the realization of the second quarter price increases.

Domestic volume also declined as we saw weaker ordering patterns beginning in mid-May. The weaker domestic volumes were replaced by export volumes which increased 14% compared to first quarter levels. The export volumes carried a lower netback compared to the domestic volumes and as a result, the overall caustic soda price in Olin's system declined from the first quarter to the second quarter.

On caustic soda pricing in the third and fourth quarters of 2016, we see domestic prices increasing in both the third and fourth quarters by a total of between 5% and 7%. And we see export prices increasing in both the third and fourth quarters, by increasing between 20% and 25%. These caustic soda pricing forecasts reflect Olin's assessment of the price increases that have been announced in the market. Finally, as we said in the press release, we continue to expect to benefit over the next several years from favorable trends developing in the global caustic soda market.

The next slide covers ethylene dichloride. As a reminder, the EDC that Olin sells is sold into the export market. The key message is that while we have seen EDC prices recover from the low levels we saw in the fourth quarter of 2015 and early in 2016, they have not recovered to the level we had forecast and they remain well below historic levels.

The lower level recovery has been reflected in the IHS indices which are shown on this slide. These compare the IHS forecast used when our initial full-year 2016 guidance was created and the current IHS forecast. We believe this reduction in the forecasted price is due to low oil prices which has made Naphtha-based ethylene less expensive and pressured global PVC pricing and therefore exported EDC pricing. I do want to remind everyone that there is significant leverage in the Olin system from EDC pricing, a \$0.01 per pound change equates to a \$20 million impact on a full-year basis.

On the next slide we address chlorinated organics. As we discussed during our Investors' Day in February, the largest source of demand for this business is refrigerants and that is an end-use market that has struggled in both Europe and North America during 2016, from the combination of softer demand and an increased level of imports from China. This has created a negative impact on both volumes and pricing.

In addition, we have seen weaker-than-expected demand in North America from both packaging and agriculture customers. As a result, we expect total Olin chlorinated organic volumes in 2016 to fall short of our forecast by between 10% and 15%.

The final slide in the deck reiterates our long-term outlook and the key variables for profit improvement. All of these variables remain intact. The trends in the caustic soda market are favorable. EDC continues to trade well below its historic level and Olin has significant leverage to price increases. We continue to be optimistic about growth in the epoxy business and the business is on track to achieve meaningful year-over-year EBITDA growth in 2016 compared to 2015. And we continue to have significant synergy and cost reduction opportunities that have yet to be realized.

And with that, we'd be happy to take questions.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions)



Frank Mitsch, Wells Fargo Securities.

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**Frank Mitsch** - Wells Fargo Securities, LLC - Analyst

Good morning, gentlemen.

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**John Fischer** - Olin Corporation - President & CEO

Good morning, Frank.

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**Frank Mitsch** - Wells Fargo Securities, LLC - Analyst

Hey, John, I wanted to try to delve into -- obviously Olin is a commodity-oriented business with a lot of cyclicality. But there are parts of the business that we thought had some more stable characteristics, chlorinated organics being one, and let's start there.

You talked about the reasons why refrigerants were weak here in 2016 and part of that might be Chinese imports. Is this something that might be broken forever? Or is there an expectation that it will come back to what we thought was a more stable business?

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**John Fischer** - Olin Corporation - President & CEO

I think, Frank, right now, our view is that it is not broken forever. There is a cycle to refrigerant demand as regulation drives an old refrigerant out and a new refrigerant in. There is some peaks and valleys in terms of demand. I think, especially in Europe, we're in a transition phase and we don't think the business is permanently broken.

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**Frank Mitsch** - Wells Fargo Securities, LLC - Analyst

So as you would characterize it, that is this 2016 setting a new normal? Or was 2015 the normal and 2016 is merely the valley?

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**John Fischer** - Olin Corporation - President & CEO

I would say 2016 is closer to the valley.

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**Frank Mitsch** - Wells Fargo Securities, LLC - Analyst

All right. And I wanted to spend a moment or two on obviously raw material inflation. You could see nat gas moving up from the end of May through Fourth of July. Now it's come back down.

But, I guess, my expectation, particularly as it pertained to the Dow business which is a material part of your overall business, is that there was some stability there in terms of margins. I had been thinking that it was almost akin to a tolling relationship, that the higher cost would be passed through as part of the business.

Is that not the way to think about it? Are there lags associated with what you are seeing on the raw material front and maybe it evens out over time? Any clarity there would be extremely helpful.

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**John Fischer** - *Olin Corporation - President & CEO*

There is a piece of the business that we acquired from Dow that, on a long-term basis, is sold to Dow and that piece of the business is protected from gas price moves. Just gas prices.

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**Frank Mitsch** - *Wells Fargo Securities, LLC - Analyst*

A piece of that \$1 billion in sales going to Dow on an annual basis. How big --

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**John Fischer** - *Olin Corporation - President & CEO*

No, Frank, a piece of the total sales that come out of the heritage Dow business for Olin, that piece which goes to Dow is protected. So your \$1 billion, roughly, is protected. But the rest of the sales are not.

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**Frank Mitsch** - *Wells Fargo Securities, LLC - Analyst*

Yes, okay. So the \$5 billion is to the market, \$1 billion is protected.

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**John Fischer** - *Olin Corporation - President & CEO*

That's correct.

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**Frank Mitsch** - *Wells Fargo Securities, LLC - Analyst*

All right. And then lastly, obviously you outlined the issues with lower domestic caustic and higher export caustic. And clearly export pricing was lower than domestic. But I wanted to try and understand the 3- to 6-month lag in your pricing. Because clearly the indices have been doing quite well in Q2 and look to be the same here in Q3.

Is there any help that you could give us in terms of X percent of your merchant caustic sales are 90-day price protected and Y percent are 180-days price protected. How should we think about your slate of merchant caustic soda sales in terms of the lag?

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**John Fischer** - *Olin Corporation - President & CEO*

I'll start with -- and we gave you some statistics -- about 20% of the sales in the second quarter were export, so 80% was domestic. Virtually all of the domestic sales are done under contract. In the Heritage Olin, which accounts for about half of that today, those contracts typically you lag between one and two quarters. And it's probably a mix balance between the two.

The balance of the domestic which is the Heritage Dow, is a shorter lag but it's typically about one quarter. And then an element of the export business is spot, the balance of that is contract. And the contract tends to lag one to two quarters just because of the duration of the shipment itself.

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**Frank Mitsch** - *Wells Fargo Securities, LLC - Analyst*

I see. Okay, thank you.

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**Operator**

Jason Freuchtel, SunTrust.

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**Jason Freuchtel** - *SunTrust Robinson Humphrey - Analyst*

Hey, good morning. Previously you estimated a \$10 change in caustic pricing would impact EBITDA by about \$30 million. Does that sensitivity still hold? Or do you have a new estimate for the impact of caustic pricing on EBITDA, given the larger exposure to the export market that you saw?

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**John Fischer** - *Olin Corporation - President & CEO*

No, that still holds.

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**Jason Freuchtel** - *SunTrust Robinson Humphrey - Analyst*

Okay. And then, trying to clarify the comments that you just made on the contract situation. What was the difference in what you saw in 2Q versus 1Q? Because I believe in 1Q, you indicated the change in the caustic pricing in February ended up impacting the price that you ended up realizing for that quarter.

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**John Fischer** - *Olin Corporation - President & CEO*

I think what we said in the first quarter was that the indexes had declined and that would normally -- the full effect of that would be felt in the second quarter. But that we had seen index increases starting in April and that we were hopeful that those would offset the first quarter declines and we would end up flat.

What happened was, I think, on the domestic side that occurred. What happened was we had a mix problem. So we sold more at lower export prices than we did domestically. So I don't think what we told you from moving from Q1 to Q2 about the index actually -- in actuality was any different than what we said. The big issue was the mix.

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**Jason Freuchtel** - *SunTrust Robinson Humphrey - Analyst*

Okay. And will the contracts that Dow put on, are they expected to roll off sometime this year, next year? And will that change the lag that you expect once they do essentially roll off?

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**John Fischer** - *Olin Corporation - President & CEO*

When we are talking about the caustic soda pricing, we are excluding that which is being sold to Dow. So these are just contracts that Dow had selling caustic into either the domestic market or the export market and those renew on a regular basis just like the Olin contracts do. The contract specifically with Dow is a 10-year contract.

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**Jason Freuchtel** - *SunTrust Robinson Humphrey - Analyst*

Right, okay. So the contracts that renew on a regular basis that Dow put on, those are continuously rolling off and have likely already rolled off to some degree and may continue to roll off throughout 2016? Is that accurate?

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**John Fischer** - *Olin Corporation - President & CEO*

I think the way to think about that is that those that were annual contracts will roll off sometime in the fourth quarter of this year. Contracts are typically renewed in the back half of the year for the following year if they're annual contracts. Based on when we acquired the Dow business, a lot of the 2016 contracts were in place.

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**Jason Freuchtel** - *SunTrust Robinson Humphrey - Analyst*

Okay. And roughly what percentage were annual contracts?

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**John Fischer** - *Olin Corporation - President & CEO*

Jason, we've not disclosed that.

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**Jason Freuchtel** - *SunTrust Robinson Humphrey - Analyst*

Okay, understood. Lastly, how much of the 125 to 150 of procurement and maintenance synergies is baked into your 2016 guidance? And was the \$20 million of administrative synergies already achieved?

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**John Fischer** - *Olin Corporation - President & CEO*

I would say the majority of the synergies and the majority of the \$20 million of administrative savings are reflected in the future.

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**Jason Freuchtel** - *SunTrust Robinson Humphrey - Analyst*

Okay. So a portion of that will occur in 2016 but --

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**John Fischer** - *Olin Corporation - President & CEO*

The majority will occur in 2017 and beyond.

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**Jason Freuchtel** - *SunTrust Robinson Humphrey - Analyst*

Okay, great. Thank you.

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**Operator**

John Roberts, UBS.

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**John Roberts** - *UBS - Analyst*

Thank you. Just when you think it can't get hotter in St. Louis, I guess it does.

John, when you talk about caustic being done under contract, I believe when you say that, it means contracts are done at varying discounts to the posted price and those discounts can be up to about 50%, I guess? Is that about right?



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**John Fischer** - *Olin Corporation - President & CEO*

That's correct.

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**John Roberts** - *UBS - Analyst*

Okay, so it's not at the posted contract prices. And then, how do you reconcile -- so caustic is used in pretty broad end markets and chlorinated organics are also pretty diversified, blowing agents for foam packaging, solvents, et cetera. So the US weakness in May and June doesn't seem to reconcile with broad macroeconomic data. How do you reconcile the dip you saw?

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**John Fischer** - *Olin Corporation - President & CEO*

I can only look at the product portfolio and the customer portfolio that we have. And we might have had the disadvantage of having some customers that were going through outages, et cetera. I don't know that I can specifically reconcile that.

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**John Roberts** - *UBS - Analyst*

Okay. I was just trying to figure out --

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**John Fischer** - *Olin Corporation - President & CEO*

I would say that, as we exited the second quarter, the demand weakness that we saw beginning in May had corrected itself.

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**John Roberts** - *UBS - Analyst*

Did that coincide with key customers restarting?

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**John Fischer** - *Olin Corporation - President & CEO*

I can't address specific customers. I think we saw a period of about 45 days where the overall portfolio was yielding lesser demand and that started to turn around early in July.

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**John Roberts** - *UBS - Analyst*

Okay, great. Thank you very much.

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**Operator**

Aleksey Yefremov, Nomura Securities.

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**Aleksey Yefremov** - *Nomura Securities Company, Ltd. - Analyst*

Good morning, thank you. What was domestic price realization for you in the second quarter? In terms of sequential change, how much did it go up or down for caustic? And secondly, is your caustic soda price forecast on page 3 for your realized price or for the benchmark?



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**John Fischer** - *Olin Corporation - President & CEO*

The forecast on page 3 is for our realized price. We have not disclosed, and I don't think we're going to disclose, what the absolute change in our caustic soda price was.

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**Aleksey Yefremov** - *Nomura Securities Company, Ltd. - Analyst*

Okay. And as a follow-up, in your guidance of 5% to 7% increase in the second half, what do you assume for price increase nominations, what kind of success rate? In other words, do you assume only what's already in the index, actually reported by IHS? Or do you assume that there will be success to some pending price nominations as well?

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**John Fischer** - *Olin Corporation - President & CEO*

I would say typically -- and this has been true with the Olin and we have talked about this forever -- typically you yield -- if you see an IHS index increase, the yield to a seller is between 40% and 60%. What we said in the remarks is that if the caustic soda pricing that is embedded in our back-end forecast reflects our assessment of the price increases that have been announced and what impact they are going to have and what the yield's going to be out of the IHS.

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**Aleksey Yefremov** - *Nomura Securities Company, Ltd. - Analyst*

Just to make sure, you assume some success in July and August price increases that are currently on the table.

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**John Fischer** - *Olin Corporation - President & CEO*

We are saying that prices are going to go up, so inherently, yes, we're assuming some success.

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**Aleksey Yefremov** - *Nomura Securities Company, Ltd. - Analyst*

But you will also get some realization of lag price increases from April through June, right? So that 5% to 7% reflects both?

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**John Fischer** - *Olin Corporation - President & CEO*

That's correct.

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**Aleksey Yefremov** - *Nomura Securities Company, Ltd. - Analyst*

Okay, thank you for going through this. And stepping back, if domestic market was tight and prices are going up, why is it not possible to sell more in the domestic market and you were forced to sell more in the export markets?

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**John Fischer** - *Olin Corporation - President & CEO*

I think that could be, as I said to the previous questioner, I think a lot of that could have been unique to the Olin system in terms of where we had contracts. We try very hard not to sell caustic soda in the spot market domestically because that is what drives prices down.



**Aleksey Yefremov** - *Nomura Securities Company, Ltd. - Analyst*

Understood. And last question, if I may, what is your assumption for natural gas in the second half of the year? (multiple speakers)

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**John Fischer** - *Olin Corporation - President & CEO*

I think we said in the press release that the full-year forecast reflects current market prices, or current market conditions. I think it was actually increased raw material costs reflecting second quarter levels, is what's in the full-year guidance. That's what we said in the press release.

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**Aleksey Yefremov** - *Nomura Securities Company, Ltd. - Analyst*

Okay, thank you very much.

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**Operator**

Arun Viswanathan, RBC Capital Markets.

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**Arun Viswanathan** - *RBC Capital Markets - Analyst*

Thank you. Just wanted to understand the opportunity as we look ahead here. If we do look at the 840 to 900 and we assume the 5% to 7% increase for this year in the second half on caustic and then the 20% to 25% on export, do you expect that you will continue to ship at the same level on export for the remainder of the year?

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**John Fischer** - *Olin Corporation - President & CEO*

No, we do not. We would expect our shipments to be more in line with what we've seen over the first two quarters that we owned Dow which would have suggested exports would have been more like 10% of total caustic sales, not 20%.

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**Arun Viswanathan** - *RBC Capital Markets - Analyst*

Okay. And then, if we translated that 5% to 7% to a dollar level, and then put that on the \$30 a ton -- sorry -- multiplied that and got to \$30 million EBITDA, I'm coming out with a change for next year that's on the order of about a \$100 million improvement in EBITDA. Is that a fair characterization of where you're coming out?

Because when you started this discussion, you're coming out at about a 2016 EBITDA level of around \$1 billion. We're just trying to understand if that opportunity is still there for 2017.

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**John Fischer** - *Olin Corporation - President & CEO*

We clearly believe that the opportunity in 2017 to earn \$1 billion is there.

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**Arun Viswanathan** - *RBC Capital Markets - Analyst*

That's excellent. And then that would also be the case on the EDC side. Is the opportunity to export EDC also there, given that the Naphtha-based production is less favorable?



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**John Fischer** - *Olin Corporation - President & CEO*

The opportunity remains there. The historic average price of EDC in the export market is between \$0.13 and \$0.14 if you look over the last, say, 15 years. If you followed it this year, it started as low as \$0.06, it's been up between \$0.09 and \$0.10. We had some expectations that it might be a little higher than that, hence the revisions to our guidance. If oil were to jump up and/or other factors in the market made the export price higher, the opportunity is clearly there.

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**Arun Viswanathan** - *RBC Capital Markets - Analyst*

I guess my question is, do you expect that we will get back to that level even with the oncoming capacity in North America?

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**John Fischer** - *Olin Corporation - President & CEO*

I'm not sure that the EDC capacity in North America has anything to do with the export market.

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**Arun Viswanathan** - *RBC Capital Markets - Analyst*

Well, no, I'm just saying there's oncoming capacity in ethylene that could depress ethylene prices globally. Would that depress ethylene dichloride prices and therefore decrease the opportunity?

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**John Fischer** - *Olin Corporation - President & CEO*

In the export market, the pricing of EDC is really based upon Asian ethylene, not US ethylene.

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**Arun Viswanathan** - *RBC Capital Markets - Analyst*

Okay, that's helpful. And then lastly on chlorinated organics, do you expect the shift to the new refrigerants ultimately -- so you do expect this to return to a normal market. When do you expect that ultimately to happen?

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**John Fischer** - *Olin Corporation - President & CEO*

That is typically one- to three-year transition.

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**Arun Viswanathan** - *RBC Capital Markets - Analyst*

Got it, thank you.

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**Operator**

Karl Blunden, Goldman Sachs.

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**Karl Blunden** - *Goldman Sachs - Analyst*

Hi, good morning. Thanks for taking my questions. I was just looking out how this guidance cut impacts your deleveraging plans and potentially how the ratings agencies would view the credit going forward here. Anything that you could share about your debt reduction goals in light of this?



And any conversations you've had with the rating agencies? They seem to have given you some credit for the deleveraging contemplated in your prior guidance.

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**John Fischer** - *Olin Corporation - President & CEO*

Karl, I would prefer to deal with that question in a couple weeks when we have a balance sheet and we give a revised cash forecast.

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**Karl Blunden** - *Goldman Sachs - Analyst*

Good, that's helpful. And then on the cash side, sounds like it's a couple weeks from now we'll have that. But are there offsets there? We're seeing \$80 million EBITDA reduction. Are there reasons to believe that should be similar on the cash flow front?

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**John Fischer** - *Olin Corporation - President & CEO*

Again, I would prefer to discuss that in a couple weeks when we have all the balance sheet and cash flow information available.

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**Karl Blunden** - *Goldman Sachs - Analyst*

Thanks very much.

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**Operator**

There are no additional questions at this time. This concludes our question-and-answer session. I would like to turn the conference back over to John Fischer for closing remarks.

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**John Fischer** - *Olin Corporation - President & CEO*

I'd like to thank everybody for participating today and we look forward to talking to you on August 2. Thank you.

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**Operator**

The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.

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