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OLN - Q2 2016 Olin Corp Earnings Call

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OVERVIEW:

OLN reported 2Q16 results. Expects 3Q16 reported diluted EPS to be \$0.10-0.20.



CORPORATE PARTICIPANTS

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

John Fischer *Olin Corporation - President, CEO*

Todd Slater *Olin Corporation - VP, CFO*

Jim Varilek *Olin Corporation - EVP, President Chlor Alkali Products and Vinyls*

Pat Dawson *Olin Corporation - EVP, President Epoxy and International*

CONFERENCE CALL PARTICIPANTS

Frank Mitsch *Wells Fargo Securities, LLC - Analyst*

Jason Freuchtel *SunTrust Robinson Humphrey - Analyst*

Arun Viswanathan *RBC Capital Markets - Analyst*

Herb Hardt *Monness, Crespi, Hardt & Co. - Analyst*

Edlain Rodriguez *UBS - Analyst*

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

Dmitry Silverstejn *Longbow Research - Analyst*

Chris Ryan *BofA Merrill Lynch - Analyst*

Owen Douglas *Robert W. Baird & Company, Inc. - Analyst*

Don Carson *Susquehanna Financial Group/SIG - Analyst*

PRESENTATION

Operator

Good morning and welcome to the Olin Corporation's second-quarter 2016 earnings conference call. Please note that this event is being recorded.

I would now like to turn the conference over to Larry Kromidas, Director of Investor Relations. Please go ahead.

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

Thank you, Ed, and good morning, everyone.

Before we begin, I want to remind everyone that this presentation, along with the associated slides and the following question and answer session, will include statements regarding estimates of future performance. Please note that these are forward-looking statements and that results could differ materially from those projected. Some of the factors that could cause actual results to differ are described without limitations in the risk factors section of our most recent Form 10-K and in our second quarter earnings release.

Also, please note that during today's call we will reference quarter-over-quarter comparisons, as the prior year results do not reflect the contribution of the acquired chlorine products businesses.

Finally, a copy of today's transcript and slides will be available on our website in the investors section under calendar of events. The earnings press release and other financial data and information are available under press releases.



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

John Fischer - *Olin Corporation - President, CEO*

Thank you, Larry, and good morning and thank you all for joining us today.

In addition to Larry, with me this morning are Pat Dawson, Executive Vice President and President of Epoxy and International; John McIntosh, Executive Vice President, Chemicals and Ammunition; Jim Varilek, Executive Vice President and President Chlor Alkali Products and Vinyls; and Todd Slater, Vice President and Chief Financial Officer.

I will begin with a few highlights and then review our adjusted EBITDA forecast for the third quarter and full year before going into some details on the businesses. Todd will then provide an update on our cash flow before we open the call to questions.

On slide 3 are some of the highlights for the quarter and our full year expectations. Last night, we announced second quarter 2016 adjusted EBITDA of \$180.4 million, which reflects depreciation and amortization expense of \$132.4 million, restructuring charges of \$8.2 million, and acquisition-related integration costs of \$16.3 million.

The second quarter was negatively impacted by lower caustic soda pricing, primarily driven by exports comprising a higher-than-normal percentage of total caustic soda sales. On July 22, we talked about the lower-than-expected domestic caustic soda demand in the Olin system during the second quarter. This was the result of unplanned outages at two large pulp and paper customers, as well as a large multi-plant industrial customer in June. Third quarter demand from these customers is expected to reflect normal operations.

Other factors contributing to weaker-than-expected performance this quarter include higher natural gas and ethylene costs and softer chlorinator organics demand from refrigerant, packaging, and agricultural customers.

Second quarter synergy realization met our expectations. Our synergy teams continue to build positive momentum, particularly in the maintenance and procurement areas. We now expect to achieve \$60 million of total synergies in 2016 and exit the year with an \$80 million annualized run rate.

We are forecasting full year 2016 adjusted EBITDA to be in the \$840 million to \$900 million range. This guidance reflects our expectation that earnings in the second half of the year should benefit from higher domestic and export caustic soda pricing, partially offset by higher costs for raw materials, including natural gas and ethylene, compared to the first half of 2016.

Additionally, softness in chlorinator organics demand is expected to continue, negatively impacting our volumes and pricing in the second half of 2016.

We continue to forecast profitability improvement for the Epoxy business during the second half, compared to the first half of 2016, due to higher expected volumes, expected improvement in productivity, and lower planned maintenance outage costs. We also continue to expect Winchester's 2016 results to improve compared to 2015 levels.

Before I turn to the segment-by-segment performance, I would like to present some slides that should provide more clarity into our outlook and business dynamics. For the third quarter, we are forecasting adjusted EBITDA to be in the \$220 million to \$250 million range and reported net income to be in the \$0.10 to \$0.20 per diluted share range.

We expect sequential caustic soda pricing improvement in the third quarter, due to higher domestic and export pricing. Epoxy earnings are expected to benefit from higher volumes and lower scheduled maintenance outage costs. Winchester should benefit from its normal seasonal peak earnings quarter and we expect incremental synergy capture in the third quarter above second quarter levels.

Higher natural gas and ethylene prices will partially offset these positive factors, as we expect third quarter input prices to continue at June levels.



Turning to slide 5, I would like to take a moment to describe the new Olin's caustic soda business and the dynamics of caustic soda price realization in our system. First and foremost, as a reminder, a \$10 per ton change in Olin's caustic soda price equates to an annual \$30 million change in adjusted EBITDA.

Unlike heritage Olin, in the new Olin caustic soda is exported and represents a meaningful component of the total caustic soda business. The majority of Olin's export sales are made using either negotiated or index prices. For Olin's index-based export pricing, Olin will typically realize the index change 30 to 90 days after it occurs, and Olin should receive approximately 80% to 100% of the index price change.

Similarly, a significant portion of Olin's domestic caustic soda sales are linked to index pricing, with Olin's pricing typically reflecting index changes on a 30- to 120-day lag. Depending on the domestic market conditions, Olin should realize 30% to 70% of the index price change.

On a positive note, July's \$20 per ton domestic contract index increase and a \$20 per ton average export spot increase should have a favorable impact on our business during the latter part of the third quarter and into the fourth quarter of 2016.

Now turning to slide 6, I would like to reiterate our long-term views on caustic soda. Olin believes several favorable trends are developing in the global caustic soda market. Olin has reduced capacity by 433,000 tons, and in North America we believe there is a bias towards further capacity reductions. Additionally, no major chlor alkali capacity increases have been announced in North America.

Outside of North America, we have seen caustic soda exports from China decline by approximately 30% since 2012, with these declines expected to continue. We believe this reflects the combination of reduced supply driven by lower chlorine production and increased internal consumption.

Finally, the mandated elimination of European mercury-based chlor alkali production by the end of 2017 should result in chlor alkali capacity reductions of 1 million to 1.5 million tons. Some of these reductions have already occurred. We believe that, as a result, Europe should become a net importer of caustic soda, rather than a net exporter, during 2017.

The long-term view of caustic soda is supported by the fact that caustic soda export sales from North America reached a record quarterly level in the first quarter and caustic soda exports reached a record monthly level in April. Because of these factors, Olin believes we are entering into a favorable multi-year caustic soda pricing environment.

Now turning to segment performance, on slide 7 you can see Chlor Alkali Products and Vinyls performance in the second quarter. We covered the majority of these points in our prior discussion on July 22, so let's move to the performance of the Epoxy segment on slide 8.

For the second quarter, Epoxy sales were \$450 million, declining \$10 million sequentially, and adjusted EBITDA was also lower versus first quarter levels. These declines came as a result of planned maintenance outages.

For the third quarter, we expect sequential improvement in Epoxy sales and adjusted EBITDA, due to the absence of any significant planned maintenance-related outage costs, combined with expected improvement in volumes and productivity.

We expect sequential demand improvement in North America, as well as Europe, which is expected to benefit from continued strength in midstream and downstream products, including differentiated and wind energy resins. In North America, we expect increased sales of upstream and midstream products, which improve the productivity and utilization of our Freeport, Texas, facility. And as a reminder, increased upstream production also increases the quantity of caustic soda Olin has to sell.

I would now like to turn to Winchester performance, which we summarize on slide 9. Sales were \$181 million, a slight decrease compared to the first quarter, with demand for seasonal items, such as shotshell and hunting rifle ammunition, shifting to a more traditional pattern versus what we have seen in recent years.

Adjusted EBITDA was \$35.7 million, a \$2.4 million increase sequentially. Improved results reflect lower commodity, other material, and manufacturing costs, partially offset by slightly lower commercial sales.

In the second quarter, Winchester completed the relocation of substantially all of the centerfire operations from East Alton, Illinois, to Oxford, Mississippi. We continue to believe cost savings from this five-year project should be \$40 million annually.

We are forecasting sequential adjusted EBITDA improvement in the third quarter for Winchester as the business enters its seasonally strongest quarter. We continue to believe full-year 2016 Winchester earnings should improve compared to 2015, primarily as a result of expected incremental savings from the Oxford relocation, expected decreases in commodity and material costs, and expected improvement in volumes, partially offset by lower prices.

Earlier on the call, I said we expect full-year adjusted EBITDA to be in the \$840 million to \$900 million range. On slide 10, I want to reiterate our long-term view of the business and highlight that the opportunities for Olin are unchanged. As I said earlier, the near-term outlook for caustic soda supply and demand is favorable, which bodes well for pricing. In fact, in July the domestic caustic soda price indices increased \$20 per ton, which should have a favorable impact on our business during the latter part of the third quarter and into the fourth quarter of 2016.

The Epoxy business is on track to deliver improved profitability in 2016 and beyond, through volume growth and mix enhancement. Our synergy capture efforts are moving forward at a pace that has allowed us to increase the 2016 realization estimate to the top end of our range.

In a few minutes, Todd will present our free cash flow forecast, which will illustrate the cash generation power of the business.

I would like to remind everyone that one of the key factors for Olin in the business combination with Dow was the power of the expanded chlorine envelope. Expanding the outlets from three to 19 products has increased the operating flexibility for Olin.

One of the new products in Olin's chlorine envelope is EDC, which we review on slide 11. EDC is produced by the reaction of Olin-produced chlorine and ethylene, while also liberating caustic soda for sale. Ethylene dichloride is an export product for Olin, sold primarily in Asia. As demonstrated by the IHS spot EDC pricing data, EDC export pricing improved during the first half of 2016, rising to approximately \$0.08 to \$0.09 per pound from lows of approximately \$0.06 per pound in the fourth quarter of 2015. Despite this improvement, EDC has not recovered to the levels we originally forecasted in our full-year 2016 outlook.

As you can see from the chart on the right, which shows the EDC export market from 2000 to present, it illustrates both the price volatility and the fact that we are currently in an historically low pricing range for EDC. For nearly 80% of the months during this period, EDC pricing has surpassed the levels we have seen over the first half of 2016.

And as a reminder, Olin has significant financial leverage to EDC pricing. An annual \$0.01 improvement in EDC pricing equates to an expected improvement in EBITDA of approximately \$20 million. That said, at this point we believe EDC represents upside potential with relatively limited downside. Additionally, we have recently made investments to enhance the profitability of EDC in our system, which is expected to improve full-year adjusted EBITDA.

On slide 12, we review chlorinated organics, another new product that has a unique value proposition for the operation and integration of our chlorine envelope. We take low-cost EDCs and combine them with internally and third-party produced chlorinated byproducts to produce a variety of chlorinated organics products.

Third parties pay us to dispose of their chlorinated organic byproducts, which results in negative raw material costs for a portion of our usage. The pullthrough of chlorine in production of chlorinated organics products then also liberates caustic soda for sale.

During the second quarter, demand from refrigerants customers in both Europe and North America was softer than expected, as was demand from packaging and agricultural customers in North America. In addition, refrigerants imported from China to North America and Europe increased. These headwinds resulted in volumes and pricing lower than we initially anticipated in our full-year 2016 guidance.



Before I turn the call over to Todd, I want to update everyone on our synergy efforts. As we continue to exceed expectation on our synergy capture efforts, we now expect 80 million -- \$60 million in total synergies for 2016 and an expected \$80 million annual run rate for the year. The other significant change relates to the synergy forecast for capital spending and investments, which Todd will talk about.

Now I would like to turn the call over to Todd Slater. Todd?

Todd Slater - *Olin Corporation - VP, CFO*

Thanks, John.

Before I review our cash flow forecast for 2016, I will comment on the book income tax rate. The second quarter tax rate was a tax benefit of 95.7% of the pretax loss. This reflects a combination of a taxable loss, favorable permanent book to tax differences, and return to provision adjustments.

As you are aware, in periods of low taxable income, these items have a disproportionate impact on our income tax rate. We would expect this non-traditional relationship between income tax expense and booked pretax income for the full-year 2016 as well.

Now turning to our 2016 cash flow forecast, which is on slide 14, we are forecasting to generate \$391 million of free cash flow before dividend payments in 2016. Walking from left to right on the waterfall chart, starting with the midpoint of our full-year adjusted EBITDA guidance of \$870 million, based on this new adjusted EBITDA guidance we now forecast cash taxes to provide approximately 25% of positive cash flow in 2016. This reflects the expected benefit from the utilization of net operating loss carryforwards created by the acquisition costs incurred last year and income tax refunds from prior years, primarily resulting from the ability to utilize net operating loss carrybacks.

The capital spending and investments include the midpoint of our current forecasts for capital spending of \$300 million, which is a decrease -- which has decreased by 6% from prior estimates. The remaining \$175 million represents investments made in the second and third quarters for additional low cost electrical power for the next 20 years at the Freeport, Texas, and Plaquemine, Louisiana, facilities. These investments should increase our manufacturing flexibility at both facilities, reduce overall electricity costs, and accelerate the realization of cost synergies.

We are now forecasting working capital should generate \$175 million of cash flow in 2016. We entered into a program to accelerate the collection of receivables, which should create a permanent working capital reduction. The one-time items include integration, cash restructuring costs, and asset sales.

The next column represents interest expense. We have approximately 75 -- approximately 65% variable rate debt in our debt profile. As a result, we're estimating the third quarter 2016 interest rate to be approximately 5%.

During the second quarter, we repaid \$17 million of term loan debt and the \$125 million 6-3/4% notes originally issued in 2001. For the full-year 2016, approximately \$205 million of debt will mature, all of which is expected to be repaid using available cash. As you can see, for 2016 we are forecasting to generate \$259 million of free cash flow after paying our normal quarterly dividend.

One comment on 2017 cash taxes, based on our forecast of net operating loss carryforwards for 2016, we are expecting lower-than-normal cash tax rate in 2017.

Finally, on July 28, Olin's Board of Directors declared a dividend of \$0.20 on each share of Olin common stock. The dividend is payable on September 9, 2016, to shareholders of record at the close of business on August 10, 2016. This is the 359th consecutive quarterly dividend to be paid by the Company.

Operator, we are now ready to take questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Frank Mitsch, Wells Fargo.

Frank Mitsch - Wells Fargo Securities, LLC - Analyst

John, you mentioned that the \$70 -- I'm sorry, July \$20 increase in caustic soda price in the index will be realized later in Q3 and into Q4, and you also gave some guidance in terms of the terms -- in terms of the time lag, so I was glad to see that it wasn't 180 days, because I think on the last conference call you guys talked about one to two quarters, so it was on the lower side there.

But can you give us some greater granularity in terms of the increases in Q2 that are going to be realized in Q3, and how much of a bump we should be expecting in your caustic soda price realizations in Q3 and Q4, based on where the indices stood in Q2 and Q3?

John Fischer - Olin Corporation - President, CEO

Frank, last -- or on July 22 when we last spoke, we talked about domestic prices increasing 5% to 7% compared to second quarter levels over the third and fourth quarter, and that export prices, we believe, will increase between 20% and 25% from second quarter levels over the third and fourth quarters.

Frank Mitsch - Wells Fargo Securities, LLC - Analyst

Is the \$20 July increase embedded in that 5% to 7% number?

John Fischer - Olin Corporation - President, CEO

Yes, we had baked into that what our assessment was of the success of the price increases that had been announced.

Frank Mitsch - Wells Fargo Securities, LLC - Analyst

All right, and then you outlined that EDC is on a low point relative to the past 15 years. Now given that so much of it is Asia related and given that the Chinese construction markets have slowed down, the expectation for a recovery there, is that predicated on a recovery in the Chinese construction market? What exactly are we looking for in terms of seeing that pick up to more normal historical levels?

John Fischer - Olin Corporation - President, CEO

I don't know that we necessarily said we were expecting a recovery there, because we talked about that that would be one of the reasons -- that was one of the two primary reasons we had to reduce our full-year 2016 guidance.

I think what we were looking for overall is the strength of construction in Asia more broadly than China, so places like Thailand, India, et cetera.

Frank Mitsch - Wells Fargo Securities, LLC - Analyst

All right, so at this point there is not reason for optimism for the balance of 2016 there, correct?



John Fischer - *Olin Corporation - President, CEO*

What we have essentially said is we expect where we are today to continue from a pricing perspective for the balance of 2016.

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

Terrific. And then, lastly, in the release I thought I read something about the guidance for Epoxy in 2016 is still intact with prior guidance, and just to confirm, we are talking about an EBITDA level for the year in the \$130 million to \$140 million range? Is that correct?

John Fischer - *Olin Corporation - President, CEO*

That's a fair estimate, yes.

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

Thanks so much.

Operator

Jason Freuchtel, SunTrust.

Jason Freuchtel - *SunTrust Robinson Humphrey - Analyst*

Of the \$15 million impact to second quarter earnings from higher raw material prices, how much of the impact was driven by higher nat gas pricing compared to higher ethylene pricing?

John Fischer - *Olin Corporation - President, CEO*

They were about evenly split.

Jason Freuchtel - *SunTrust Robinson Humphrey - Analyst*

Okay, and then just to clarify in the revised guidance, did you extrapolate that one month surge in raw material prices that negatively impacted the results over the course of the 12 months adjusted for your utilization rates?

John Fischer - *Olin Corporation - President, CEO*

Yes, we did.

Jason Freuchtel - *SunTrust Robinson Humphrey - Analyst*

Okay, great. And can you expand on the investments you made to improve your EDC situation? What was the CapEx commitment and how quickly will that investment improve your EDC profitability?

John Fischer - *Olin Corporation - President, CEO*

I would prefer not to talk about the dollar value of the investment. I would say we expect to see benefits beginning in the fourth quarter.

Jason Freuchtel - *SunTrust Robinson Humphrey - Analyst*

Okay, great. And I guess, lastly, can you discuss the working capital initiative to accelerate collection of receivables? Will that benefit be complete in 2016 or will there be continued benefit in 2017?

Todd Slater - *Olin Corporation - VP, CFO*

Jason, this is Todd. We would expect that to occur all in 2016 and that would be more of a one-time permanent reduction. In essence, we entered into an agreement with a major financial institution to sell our receivables, in essence accelerating the collection.

Jason Freuchtel - *SunTrust Robinson Humphrey - Analyst*

Okay, great. Thanks, guys.

Operator

Arun Viswanathan, RBC Capital Markets.

Arun Viswanathan - *RBC Capital Markets - Analyst*

I guess first off, just on the export side, I guess I can appreciate that you had a couple customers down in the second quarter and that's what led to your own lower domestic demand within your own system and, of course, a little bit more export tonnage.

I just wanted to understand the 2017 situation, though. Is it safe to assume that you would have more exports in 2017 than you would have in 2016? Maybe you can just tell us your expectations on overall export tonnage, and does that lead to an overall lower price realization on an average basis?

John Fischer - *Olin Corporation - President, CEO*

We would not expect any significant change in 2017 versus 2016 in the mix between domestic caustic soda sales and export sales. And I (multiple speakers) would actually think if you look at where the pricing has moved, there has been a more dramatic move up in the export pricing. So export will actually contribute to, we hope, a higher netback in 2017.

Arun Viswanathan - *RBC Capital Markets - Analyst*

Great, that's helpful. And then, maybe, help us -- remind us, some of your assumptions embedded in the \$1.5 billion mid-cycle EBITDA statement, if we were to remove the \$250 million of synergies, that leaves us at about \$1.25 billion. Is that the right way to look at it? And what is the caustic soda price and the epoxy EBITDA that is embedded in that EBITDA?



John Fischer - *Olin Corporation - President, CEO*

If we start with caustic soda, we talked about mid-cycle, and I think if you went back and looked at 2011 through 2014, you could pick a mid-cycle point and I would suggest that was something like \$100 higher than what we have seen in the first half of 2016.

In the Epoxy, if you go back to the investors day presentation, we showed you where the business had been and that we expected it to get back to that level over a multi-year period. And then, the other element of it is EDC, and all we said was mid-cycle was the average that is on the chart that we put today, the 15-year average, which is something in the neighborhood of \$0.13 or \$0.14.

Arun Viswanathan - *RBC Capital Markets - Analyst*

And just to clarify, though, are there any impediments structurally, whether it be demand, given that there are some lower markets, i.e., alumina or pulp and paper, that would impede you from getting to those levels or costs, i.e., lower oil prices or anything like that, that would prevent you from getting back to those mid-cycle levels?

John Fischer - *Olin Corporation - President, CEO*

I think there is always the potential for market factors that could do that. I don't know what global demand, what the global economies are going to look like two years from now in terms of rates of growth or whether we might be in a less favorable growth scenario. But I think -- and we talked about this, I think clearly we believe on caustic the dynamics are setting up for that to happen. I would say in the short run we're a little less certain about EDC, which is why we have made some investments to get the costs down.

Arun Viswanathan - *RBC Capital Markets - Analyst*

Okay, thanks.

Operator

Herb Hardt, Monness.

Herb Hardt - *Monness, Crespi, Hardt & Co. - Analyst*

My question regards competition. With the various price increases that you see on the index, do you see your main competitors going along with you and not having any problems in meeting that?

Jim Varilek - *Olin Corporation - EVP, President Chlor Alkali Products and Vinyls*

This is Jim Varilek. I would just say from a competitive standpoint the indexes are representative of what is taking place in the industry, and there have been support for all the announcements that have been made out there and they are being implemented according to the index.

Herb Hardt - *Monness, Crespi, Hardt & Co. - Analyst*

Thank you.



Operator

Edlain Rodriguez, UBS.

Edlain Rodriguez - UBS - Analyst

Just one quick question on Epoxy. Outside of the maintenance outages you have had, is everything on track for you to get to your goals that you had during the investor day? And again, remind us again what is going to be the key drivers of that growth for you.

Pat Dawson - Olin Corporation - EVP, President Epoxy and International

Sure. This is Pat Dawson, and, yes, we are on track. We continue to take cost out of our entire supply chain in Epoxy, improving productivity, running our assets harder, and, obviously, continuing to use our low cost position that we have, starting with chlorine, to drive that low cost position and to increase our volumes and to fundamentally run our plants hard. So, the bottom line is we are on track and we will continue to improve the Epoxy business.

Edlain Rodriguez - UBS - Analyst

Okay, thank you.

Operator

Aleksey Yefremov, Nomura.

Aleksey Yefremov - Nomura Securities Co., Ltd. - Analyst

Turning to slide 13, if I look at capital investment to achieve synergies, if I add up all the -- last two rows in 2016 and 2017, it looks like your costs will come down by about \$210 million. Is it fair to assume that all of this accrues to your free cash flow growth next year, and if so, are there any offsetting factors if we try to build a bridge for 2017 free cash flow?

John Fischer - Olin Corporation - President, CEO

No, I think the way we were looking at it is that the total investment to capture synergies has actually gone up a little bit, but it is front-end loaded now. So there will be significantly lower capital outlay or cash outlays next year to capture -- and 2018 to capture synergies than we had been previously forecasting.

Aleksey Yefremov - Nomura Securities Co., Ltd. - Analyst

And I guess the total of those would be about \$210 million? Am I correct? I'm just subtracting the 2017 number from 2016.

John Fischer - Olin Corporation - President, CEO

That's correct. And we had previously been forecasting something in the neighborhood of \$150 million.



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

Okay, and for working capital, \$175 million benefit this year, how much of that would you estimate as one time in nature or non-recurring next year?

Todd Slater - *Olin Corporation - VP, CFO*

Yes, that's really a one-time -- that's the majority of it and it is a permanent reduction in working capital.

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

Thank you. And Todd, final question, if I may, on taxes. Would you expect cash taxes to be, all else equal, higher or lower, or maybe in terms of cash tax interest rate for 2017 versus 2016?

Todd Slater - *Olin Corporation - VP, CFO*

What we have said is we would expect -- what we had previously said is we think normalized cash tax rate is 25% to 30%, but with the carryforwards now from 2016, we are going to say that that is the low. I think you could potentially see a \$40 million to \$50 million cash tax reduction off of your modeling or off of a normalized rate in 2017.

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

Thank you very much.

Operator

Dmitry Silversteyn, Longbow Research.

Dmitry Silversteyn - *Longbow Research - Analyst*

Can you update us or give us an idea of how big the EDC and the chlor organics businesses are within the vinyls and the chlor organics division?

John Fischer - *Olin Corporation - President, CEO*

We have not provided that information.

Dmitry Silversteyn - *Longbow Research - Analyst*

Okay, so there is really no way for us to model that. Okay. Can you talk about what's going on in hydrochloric acid, the bleach and potassium hydroxide market, your legacy businesses as far as destination for the chlorine molecule is concerned?

Jim Varilek - *Olin Corporation - EVP, President Chlor Alkali Products and Vinyls*

This is Jim Varilek. I will comment on that. As you might imagine on the bleach side of things, we're entering into bleach season. The warm weather has been good for bleach, so the demand is strong there and pulling hard.



On the hydrochloric acid standpoint, we are still bumping -- kind of bumping along the bottom in terms of the demand and so forth. Pricing is stable, but not where we would like it to be, but it is moving along.

KOH is pretty stable. Raw material prices have been a benefit there, but prices are relatively stable, and so (technical difficulty).

Dmitry Silversteyn - Longbow Research - Analyst

So nothing in terms of hydrochloric acid market recovery that we can point to with expectations for that business to improve?

Jim Varilek - Olin Corporation - EVP, President Chlor Alkali Products and Vinyls

Not that we see at this point.

Dmitry Silversteyn - Longbow Research - Analyst

If you look at -- I want to make sure I understand the pricing commentary. So you got a 20% -- or a \$20 a ton price increase in July on the spot market, which you expect to get some of that in your third quarter results, and then more of that in the fourth quarter. Typically, your price increases have been about 50% effective versus spot, so should we be thinking about a \$10 a ton increase in the fourth quarter and something less than that in the third quarter?

John Fischer - Olin Corporation - President, CEO

That's probably the best way to think about it, yes.

Dmitry Silversteyn - Longbow Research - Analyst

Okay. And anything going on on the chlorine pricing right now or is it just maintaining them is basically the goal at this point?

Jim Varilek - Olin Corporation - EVP, President Chlor Alkali Products and Vinyls

The chlorine -- this is Jim Varilek -- chlorine has moved. The index moved \$5 in July.

John Fischer - Olin Corporation - President, CEO

Why don't you tell him what it has done all year?

Jim Varilek - Olin Corporation - EVP, President Chlor Alkali Products and Vinyls

And we have had --

Dmitry Silversteyn - Longbow Research - Analyst

Expect (technical difficulty) quarter.



John Fischer - *Olin Corporation - President, CEO*

I'm sorry. We didn't get that question.

Dmitry Silversteyn - *Longbow Research - Analyst*

I was going to say, so the \$5 increase that you have seen in the chlorine pricing here in July, we should be expecting somewhere in the \$2 to \$3 increase at all by the fourth quarter, correct?

Jim Varilek - *Olin Corporation - EVP, President Chlor Alkali Products and Vinyls*

That's correct.

Dmitry Silversteyn - *Longbow Research - Analyst*

Okay. All right, and then just final question on what's going on with the Epoxy market. Outside of the costs of plant maintenance shutdowns, what does demand and pricing and raw material environment look like both in the US and outside the US?

Pat Dawson - *Olin Corporation - EVP, President Epoxy and International*

This is Pat Dawson, and I would say that overall demand for epoxy typically is about 3% market growth. We are on the low side of that this year, especially in North America, where you look at industrial production being pretty anemic and really very low growth, combined with a tough oil and gas market that we all know about.

When you move to Europe, Europe grows about 4% or 5%. There is very different dynamics in the industrial coatings marketing in Europe, and we see Europe being very stable, with some slight improvements in pricing there.

We are very small in Asia-Pacific. We typically play in the downstream differentiated markets of wind energy electric laminates, where epoxy is used there, and those markets in Asia are actually stable, but the overall demand in Asia is significantly down, due to the slowing of the Chinese economy over the last couple years.

Latin America is a very small market, probably as much influenced by Mexico, which is doing just fine as compared to Brazil, which has been a very tough situation this year.

Dmitry Silversteyn - *Longbow Research - Analyst*

Okay, thank you. And so in that environment, how should we think about your ability to get pricing and your ability to grow volumes on a year-over-year basis? Is it basically a low single-digit volume environment and pricing flat to slightly negative?

Pat Dawson - *Olin Corporation - EVP, President Epoxy and International*

Yes, I would say pricing is stable, and I wouldn't look at -- we're not looking at any dramatic improvements in pricing. I think, as I said earlier, though, the overall market is about a 3% growth market. It varies in different areas. And so, year-on-year growth probably in the 2% to 3% range, but again when you look in our upstream part of the business, the upstream will continue to grow because we have a great cost position there. So, maybe a little bit better than 2%, 3% growth in the upstream.



The midstream, which is primarily the liquid epoxy resin market, is more in this -- probably on the lower end of 3%, as I said, more like the 2% to 3%.

Dmitry Silversteyn - *Longbow Research - Analyst*

Thank you very much.

Operator

Roger Spitz, Bank of America Merrill Lynch.

Chris Ryan - *BofA Merrill Lynch - Analyst*

This is Chris Ryan on for Roger. Thanks for taking my questions. The first question, the epoxy MD&A suggests that the underlying epoxy variable margins didn't materially change in Q2 2016 versus Q1 2016. Is that correct?

Pat Dawson - *Olin Corporation - EVP, President Epoxy and International*

That's correct.

Chris Ryan - *BofA Merrill Lynch - Analyst*

Okay, thank you. And did you see any change in your upstream or base epoxy business being the BPA at the LER business versus the downstream specialties business, which may have offset it, or were they constant?

Pat Dawson - *Olin Corporation - EVP, President Epoxy and International*

I would say that on the upstream, which we really define as our allylics, our allyl chloride, our epichlorohydrin, and then our integrated aromatics with our cumene phenol, that is an area that we have continued to make good progress in selling those assets out and running them harder.

The downstream growth has been primarily in Europe and also, to a degree, in Asia-Pacific in the wind and electrical laminate market. So, it is pretty -- it has been pretty balanced, quite frankly, on the margin contribution between the downstream and the upstream, upstream growing through our integrated cost positions, downstream growing mainly through our formulation know-how and adding value with our formulation expertise with specific end-use customers.

Chris Ryan - *BofA Merrill Lynch - Analyst*

Okay, thank you. And finally, Hexion is shutting down its Norco [epi] facility. Can you say if you're picking up that business?

Pat Dawson - *Olin Corporation - EVP, President Epoxy and International*

That was announced by Hexion here last quarter. We are picking up some of that business.

Chris Ryan - *BofA Merrill Lynch - Analyst*

That's all my questions. Thank you.

Operator

Owen Douglas, Baird.

Owen Douglas - *Robert W. Baird & Company, Inc. - Analyst*

Thanks so much for sharing some good information earlier. I wanted to dig in a little bit more on that capital investment. So just to make sure I have it right, so the investments are going to be made in Q2 and Q3 and cumulatively all of that spend relates to the power supply agreement?

John Fischer - *Olin Corporation - President, CEO*

It relates to power.

Owen Douglas - *Robert W. Baird & Company, Inc. - Analyst*

Okay, can you provide a little more color on that?

John Fischer - *Olin Corporation - President, CEO*

It gives us access to a greater quantity of power that allows us to more fully run our facilities at an attractive price.

Owen Douglas - *Robert W. Baird & Company, Inc. - Analyst*

So is this investment in a new facility that is coming up?

John Fischer - *Olin Corporation - President, CEO*

It is access.

Owen Douglas - *Robert W. Baird & Company, Inc. - Analyst*

Okay, I see. And you said that you expect to receive some of that benefit in 2016, I believe. Is that Q4? Is that correct?

John Fischer - *Olin Corporation - President, CEO*

I think we talked about that we had made an investment that was going to positively impact margins on our EDC business and we would see that in Q4.

Owen Douglas - *Robert W. Baird & Company, Inc. - Analyst*

Are those two separate things? Sorry, I am just having a hard time really understanding.

John Fischer - *Olin Corporation - President, CEO*

We describe them as separate things, yes.

Owen Douglas - *Robert W. Baird & Company, Inc. - Analyst*

Okay, I see. So as far as that power agreement, do you believe that that positive impact would be received any this year or is this really more in the future?

John Fischer - *Olin Corporation - President, CEO*

The vast majority of it, as Todd said, it is a 20-year agreement, is well in the future.

Owen Douglas - *Robert W. Baird & Company, Inc. - Analyst*

Okay, but it will be some agreement to -- there is some benefit in 2016?

John Fischer - *Olin Corporation - President, CEO*

Some benefit in the second half of 2016, yes.

Owen Douglas - *Robert W. Baird & Company, Inc. - Analyst*

Okay, so as we look to that bridge to the full-year EBITDA, that's already being factored in there, right?

John Fischer - *Olin Corporation - President, CEO*

That's correct.

Owen Douglas - *Robert W. Baird & Company, Inc. - Analyst*

Okay, great. Thank you.

Operator

Jason Freuchtel, SunTrust.

Jason Freuchtel - *SunTrust Robinson Humphrey - Analyst*

I just had a quick follow-up. Will there be any opportunities for further debt reduction in the back half of the year 2017?

Todd Slater - *Olin Corporation - VP, CFO*

At this point, we are committing to pay our \$205 million of maturing debt that occurs in 2016.



Jason Freuchtel - *SunTrust Robinson Humphrey - Analyst*

Okay, thank you.

Operator

Don Carson, Susquehanna Financial.

Don Carson - *Susquehanna Financial Group/SIG - Analyst*

John, I just want to go back to caustic soda. What is -- for the new Olin, what is your mix between export and domestic in terms of percentage that goes to each market? And why would the index realization be so much better in offshore than it is in domestic? Do you have contract limitations in the domestic market or is there more just the competitive nature of the domestic market?

Jim Varilek - *Olin Corporation - EVP, President Chlor Alkali Products and Vinyls*

This is Jim Varilek. From a split standpoint, exports are about 10% to 20% of our total business on the caustic side, and there are contractual differences between the domestic and the export markets, just by the nature of the dynamics.

Don Carson - *Susquehanna Financial Group/SIG - Analyst*

And then, looking at EDC, is that really a hedge to caustic soda? Obviously, the caustic soda market or the export market has improved because of reduced demand for chlorovinyls into Asian construction and hence less caustic production there. So, if EDC demand gets better, does that mean you're going to see higher chlor alkali operating rates in Asia and hence lower export pricing and demand? Do the two offset each other?

John Fischer - *Olin Corporation - President, CEO*

I think, Don, the way we as a producer look at it is we look at the value of EDC plus caustic to determine what we're going to do and how hard we operate.

Don Carson - *Susquehanna Financial Group/SIG - Analyst*

Okay. And then, finally, on Winchester, are you seeing a renewed demand surge such that -- you have always talked about 2016 being above 2015, but are you now more optimistic on the outlook based on some of the trends you are seeing in ammunition demand?

John Fischer - *Olin Corporation - President, CEO*

I don't think our story as it relates to 2016 and Winchester versus 2015 has changed.

Don Carson - *Susquehanna Financial Group/SIG - Analyst*

Okay, thank you.



Operator

This concludes our question-and-answer session. I would like to turn the conference back over to John Fischer for any closing remarks.

John Fischer - *Olin Corporation - President, CEO*

Thank you all for joining us today and we look forward to speaking to you about our third quarter earnings in October or early November. Thank you.

Operator

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

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