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PRESENTATION

Operator

Good morning, and welcome to the Olin Corporation Fourth Quarter 2019 Earnings Conference Call. (Operator Instructions) Please note, this event is being recorded. I'd now like to turn the conference over to Logan Bonacorsi, Olin's Director of Investor Relations. Please go ahead, Miss.

Logan L. Bonacorsi ***Olin Corporation - Director of IR***

Good morning, everyone, and thank you for joining us today. Before we begin, let me remind you that this presentation, along with the associated slides and the question-and-answer session following our prepared remarks, will include statements regarding estimates of future performance. Please note that these are forward-looking statements and that actual result could differ materially from those projected. Some of the factors that could cause actual results to differ from our projections are described without limitations in the Risk Factors section of our most recent Form 10-K and in yesterday's fourth quarter earnings press release. A copy of today's transcript and slides will be available on our website in the Investors section under past events. The earnings press release and other financial data and information are available under press releases.

With me this morning are John Fischer, Olin's Chairman, President and Chief Executive Officer; Pat Dawson, Executive Vice President and President of Epoxy International; Jim Varilek, Executive Vice President and Chief Operating Officer; and Todd Slater, Vice President and Chief Financial Officer. We will begin with our prepared remarks and thereafter, we'll be happy to take your questions.

I will now turn the call over to John Fischer. John?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

Thank you, Logan, and good morning, everyone. I will begin today by reviewing Olin's full year 2019 results. Then I will provide an overview of each of our business segments and conclude with some comments on our near-term and long-term outlooks for Olin and the markets in which we participate.

With that, let's turn to Slide 3. During the fourth quarter of 2019, Olin reported adjusted EBITDA of approximately $173 million, which resulted in full year 2019 adjusted EBITDA of $941 million. This level of adjusted EBITDA reflects the challenging macroeconomic environment that developed during the year and worsened during the fourth quarter. In particular, the Chlor Alkali Products and Vinyls business experienced a broad-based weakness in demand from urethane, agricultural, refrigerant, alumina and pulp and paper customers. The Epoxy business also faced weaker demand from automotive, electrical laminate and industrial coatings customers. As you can see from the chart, the lower product demand put downward pressure on pricing, which was the driver of the lower year-over-year adjusted EBITDA. The deterioration of pricing during 2019 in our Chlor Alkali Products and Vinyls business was approximately $450 million from 2018 levels and the deterioration in our Epoxy business was approximately $260 million.

There were a number of factors that help partially offset these price declines. Lower raw material costs of approximately $130 million in our chlor alkali products and vinyl segment, primarily related to lower electricity and ethylene costs. We realized lower raw material costs in the Epoxy business of approximately $215 million, primarily benzene and propylene. Olin accelerated its ongoing activities to lower our cost structure and to improve our efficiency. Operating and administrative costs in 2019 were approximately $90 million lower than 2018 levels. As a point of reference, since late 2018, Olin's total employee and contractor headcount was reduced by approximately 6% and an additional reduction of approximately 4% is to incur in 2020.

Now we'd like to take a more detailed look quarterly results for each of our business segments, starting with Chlor Alkali Products and Vinyls, which is shown on Slide 4. Fourth quarter 2019 adjusted EBITDA for the chlor alkali products and vinyl segment was $142.5 million, representing a 46% year-over-year decline. As previously discussed, this decline was driven chiefly by the declines in product pricing. For the fourth quarter, caustic soda pricing, in Olin system, declined approximately 24%, when compared to the fourth quarter of 2018. At the same time, year-over-year ethylene dichloride experienced power -- lower pricing of approximately 23% and hydrochloric acid pricing declined approximately 40%. Partially offsetting this year-over-year pricing pressure was the improved performance as well as the lower raw material cost, that I just discussed.

Now let's take a closer look at caustic soda pricing, which is on Slide 5. During the fourth quarter and into January 2020, caustic soda prices continued to move lower as demand weakness in the manufacturing sector persisted. At the same time, chlorine operating rates have remained relatively steady primarily due to strength in the vinyl sector, which increased the supply-demand imbalance that has existed for much of the past 15 months. The caustic soda price decline has been particularly pronounced in the export market where pricing indices were down more than $80 per ton since the beginning of October and approximately, $200 per ton since the end of 2018. Export caustic soda pricing has declined to levels last seen in 2010. Domestic pricing, while lower, was more resilient due to support from a relatively stronger domestic demand environment and the overall cost-to-service market. A portion of the fourth quarter and January declines in the price indices will be experienced in our system as we progress through the early months of 2020.

Let's now talk about our Epoxy segment, which is shown on Slide 6. Epoxy's -- Olin's Epoxy business generated adjusted EBITDA of $36.2 million in the fourth quarter of 2019, which represented an 18% decline from the level achieved in the prior year period. The year-over-year decrease primarily reflects lower resin pricing due to lower demand in our key markets, a trend that has challenged the business for the last 15 months. Partially offsetting these market conditions during the period were lower raw material costs, primarily benzene and propylene, and lower operating costs driven by our ongoing productivity efforts. That said, price declines outpaced lower raw material costs, resulting in further margin compression for Olin as we close the year. The Epoxy segment generated $154 million of -- in adjusted EBITDA for the full year 2019. While not the year-over-year improvement that was originally anticipated, it was a strong performance in the face of a challenging market landscape, we -- and we continue to believe that the strength of the Epoxy business's chlorine integration and potential -- and in the potential earnings power for this part of our business.

Looking now at Global Epoxy resin prices, which is shown on Slide 8. During the fourth quarter, liquid epoxy resin pricing continued to decline in all regions. The average Global Epoxy resin pricing declined 20% over the course of 2019. Ongoing demand weakness from global automotive, global electrical laminate and industrial coatings customers has led to global price erosion. We also believe economic deceleration in multiple geographic regions has led to cautious buying behavior inventory managements by customers during the period.

Now let's turn to our Winchester segment on Slide 8. The Winchester business continued on a positive trend, posting its second consecutive quarterly year-over-year increase. Fourth quarter of 2019 adjusted EBITDA was $12.5 million, which represents a 33% improvement. This was a result of higher commercial, military and law enforcement volumes and favorable commodity and operating costs. Lower year-over-year pricing partially offset these improvements. 2019 also marked the first year-over-year increase in annual adjusted EBITDA since 2016, which was the last year of surge buying in the industry. This improvement was driven primarily by a reduction in commodity and operating costs. The lower operating costs are a result of ongoing cost reduction efforts in the business.

Moving now to our outlook for the full year 2020, which is on Slide 9. As you all know, Olin is primarily a commodity chemical producer with limited ability to influence pricing in large global commodity markets. Given the uncertainty surrounding pricing for our chlor alkali and Epoxy products and the significant and rapid impact that price changes can have on our earnings, Olin will no longer provide annual adjusted EBITDA guidance. We will continue to provide our planned maintenance turnaround cost schedule, pricing sensitivities for certain commodity products and other key metrics, which are included in the appendix section of our slide presentation.

We do expect the weak underlying demand fundamentals in our chemical businesses to persist through at least the first quarter of 2020. We are entering the year challenged by lower chemical pricing. January 2020 pricing for caustic soda, ethylene dichloride and other chlorine derivatives as well as epoxy resins are below 2019 full year averages. If these levels of prices are maintained throughout 2020, the impact of pricing on 2020 results compared to 2019 would be in the $250 million range. During January, we have seen demand across our chemicals portfolio consistent with fourth quarter levels. We expect lower raw materials in both our Chlor Alkali Products and Vinyls and the Epoxy segments to be in 2020 compared to 2019. The lower costs are related to electricity, ethylene, benzene and propylene. We will continue to focus on the variables within our control by working to reduce operational and administrative costs and expect them to decline in 2020 compared to 2019.

We are also anticipating an increased contribution from our Winchester segment, primarily driven by the uplift from the Lake City U.S. Army ammunition contract, beginning in the fourth quarter of this year. As we have previously discussed, our Winchester business secured a multiyear contract with the U.S. Army to operate the Lake City army ammunition plant in Independence, Missouri. Upon completion of the 1-year transition period, we expect this multiyear contract will drive a significant increase in annual profitability for Winchester, starting the fourth quarter of this year. We estimate increased annual revenue of between $450 million and $550 million and corresponding increase in annual adjusted EBITDA of $40 million to $50 million.

I would like to underscore the long-term out -- now would like to underscore the long-term outlook for our chemical businesses, which is on Slide 10. In spite of the weaknesses we're currently experiencing, we continue to believe that market fundamentals will be supported and bolstered by long-term structural forces in the chlor alkali supply and demand. In fact, we continue to believe that there will be demand growth for the chlor alkali sector on both sides of the ECU. Today there have been minimal global capacity additions and announcements of additions to meet this projected demand growth. And as a reminder, in December, Olin announced chlor alkali products capacity reductions. The U.S. will continue to enjoy a sustained energy and feedstock advantage over the rest of the world. Current industry economics do not support world-scale chlor alkali capital investments. And ultimately, over the long term, supply and demand balances will tighten, resulting in upward pricing momentum for Olin's caustic soda, chlorine and chlorine-derivative products.

Similarly, in the Epoxy business, we see global demand growth and minimal capacity additions.

Before I turn the call over to Todd, I'd like to emphasize that Olin remains on very solid financial footing. In 2020, Olin expects to generate positive cash flows after the payment of the normal quarterly dividend and before the one-time investments, that Todd will discuss. And this assumes the full year negative impact of no change in the current product pricing and no positive cost offsets.

And with that, I'll turn it over to Todd.

Todd A. Slater ***Olin Corporation - VP & CFO***

Thanks, John, and good morning, everyone. Let's turn to our full year 2019 cash flow detail, which is on Slide 11.

We generated approximately $252 million of free cash flow in 2019. Starting with our adjusted EBITDA of $941 million, which is in the far left of the waterfall chart, we deduct $36 million in cash tax payments, which are almost all attributable to earnings in foreign jurisdictions. Column 3 reflects our capital spending of $386 million, which includes annual maintenance capital spending and the investment associated with our multiyear information technology integration project of approximately $56 million. As we've previously discussed, in 2017, we began a multiyear project to implement new enterprise resource planning, manufacturing and engineering systems across the chemical businesses. The project includes the required information technology infrastructure.

Now turning to the fourth column. One-time items include information technology integration costs and cash restructuring costs of approximately $100 million. This includes approximately $49 million of IT integration project costs, that I just spoke about, and approximately, $28 million of duplicate IT costs being incurred during the transition. These costs were partially offset by $20 million of pretax proceeds from the sale of an investment in a nonconsolidated affiliate during the first quarter.

The next column represents our cash interest expense for 2019. As of December 31, we had approximately 5% of our debt at variable interest rates. In the next column, we had an $11 million decrease in working capital in 2019, primarily as a result of lower accounts receivable attributed to lower level of sales in the fourth quarter of 2014, which was offset by a reduction in the sale of receivables under our factoring program. In the far-right column, we had $252 million of free cash flow.

Now I'd like to move to Olin's investment requirements in 2020, which we'll review on Slide 12.

In order to complete several initiatives to improve long-term cash flow for Olin, 2020 will include investments that are outlined on this slide. The final ethylene tranche payment of approximately $493 million at year-end, this will provide ethylene at producer-based economics needed to supply the new VCM contract, which will commence at the beginning of 2021. A total of approximately $110 million for the capital, project cost and duplicate IT cost being incurred during the transition of our multiyear information technology integration project. This project is winding down. By the end of 2019, approximately 35% of Olin's chemical users were successfully converted to the new systems. During 2020, most of the remaining chemical users will be converted to the new systems. Olin expects to refinance the high-cost bonds which were assumed during the 2015 Dow acquisition and will become callable in the fourth quarter of 2020 with a call premium of approximately $42 million. Finally, Olin will incur transition costs and working capital investments required for the new Lake City U.S. Army ammunition contract. When finalized, these necessary and value-creating investments will be a catalyst for improved cash generation beginning in late 2020 and fully in 2021 and beyond, regardless of the market environment. The cash flow benefits are highlighted on Slide 13.

In 2021, we expect incremental annual cash generation of approximately $250 million from the initiatives that I just discussed. The refinancing of the high-cost bonds are expected to reduce interest expense by $50 million to $70 million annually. Winding down of the multiyear information technology project will save approximately $110 million between capital and expense. The vinyl chloride monomer contract, which is transitioning from a toll-manufacturing arrangement, that's been in place since the acquisition, to a direct-customer sale agreement beginning on January 1, 2021. The VCM facility is 1 of 2 operations that has the most significant impact on our Chlor Alkali Products and Vinyls' results. The full year effect of the new Lake City U.S. Army ammunition contract. And finally, one initiative announced in December and was not discussed on the previous slide, is the expected $75 million (sic) [$35 million] reduction in operating costs from the permanent shutdown of a chlor alkali plant, with a capacity of 230,000 tons, at Olin's Vinylidene Chloride production facility in Freeport, Texas. These closures are expected to be completed before the end of 2020. That -- these closures will allow Olin to optimize its chlor alkali operations and cost structure in Freeport, Texas. $35 million, not $75 million.

These cash flow enhancements of approximately $250 million provide significant incremental cash flow to Olin, independent of industry conditions.

Now I'd like to conclude with Olin's priorities for free cash flow, which is on Slide 14. During 2020, our priorities for free cash flow will be returning capital to our shareholders through our quarterly dividend, refinancing the high-cost debt in late 2020 and funding the essential investments required to enhance our businesses that we just reviewed. Finally, on Friday, January 24, Olin's Board of Directors declared a dividend of $0.20 on each share of Olin common stock. The dividend is payable on March 10, 2020, to shareholders of record at the close of business on February 10, 2020. This is the 373rd consecutive quarterly dividend to be paid by the company.

Operator, we are now ready to take questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question will come from Neel Kumar of Morgan Stanley.

Neel Kumar ***Morgan Stanley, Research Division - Equity Analyst***

I know you mentioned that January costs and EDC prices are approximately 15% below the average 2019 price. Can you just give me the sense of what type of EBITDA headwind that could translate to, assuming prices remain at January levels?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

We made a comment and -- just made a comment in the remarks that said, "If all prices that we discussed, which was caustic, EDC, HCl and then epoxy resins remained at current levels throughout the year, the negative impact would be approximately $250 million".

Neel Kumar ***Morgan Stanley, Research Division - Equity Analyst***

And then you talked about some cost containment and productivity initiatives in 2019 to offset the cost of pricing initiatives. Can you just give us a sense of some examples of this? And what initiatives you have in place for 2020, in addition to the plant closure that should reduce your cost by $35 million?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

Well we talked about pretty significantly lower raw material costs, both in the chlor alkali sector from electricity and ethylene and in the Epoxy sector from benzene and propylene. And we also talked about a 6% reduction in our employee and head -- contractor headcount and that occurred in 2019. And I would tell you, there's an added benefit just from that because that was not in place all year in 2019, and we expect to reduce that headcount an additional 4% in 2020. And we also expect, again, to benefit from lower raw material costs, both on the electricity and ethylene side as well as benzene and propylene.

Operator

And our next question will come from Kevin McCarthy of Vertical Research Partners.

Kevin William McCarthy ***Vertical Research Partners, LLC - Partner***

On Slide 12, you show an expected payment of $493 million to procure more ethylene. My recollection is that you had an option to do so. And so my question is, if we fast forward to December and it turns out that ethylene prices are quite low for whatever reason, do you have the ability to defer that payment? Would that be feasible or impractical?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

I think that is totally impractical. It allows us access to cost-based ethylene for 20 years. It matches up with the new vinyls contract, we've already negotiated. So I would say that -- and as Todd mentioned in his remarks, vinyls is 1 of the 2 -- that plant is 1 of the 2 most important plants in our system, and we're not going to do anything to jeopardize that. So that's, in our mind, not practical.

Kevin William McCarthy ***Vertical Research Partners, LLC - Partner***

Understood. Second, I wanted to ask about working capital. Todd, if we look at the balance sheet, accounts receivable, for example, declined $16 million year-over-year or about 2%. It looks like payables were up. Can you speak to those line items in the context of the relatively large price declines that you quantified in the prepared remarks, why did we not see more of a change there?

Todd A. Slater ***Olin Corporation - VP & CFO***

Yes, Kevin, good question. In receivables -- we do factor our receivables, so some are sold. So year-end to year-end, directionally, you're looking at about $70 million in less receivables sold. So when you factor that in to the equation, receivables was actually down fairly consistent with the sales change and in accounts payable and you see inventory is down as well. Those are much more in line.

Operator

And our next question will come from Don Carson of Susquehanna Financial.

Donald David Carson ***Susquehanna Financial Group, LLLP, Research Division - Senior Analyst***

John, it seems you're kind of in a situation where chlorine demand is stronger than caustic demand. So with early restocking in PVC, domestically, boosting chlorine demand, how do you see industry operating rates and Olin operating rates in chlor alkali for the first and second quarters, not a year-over-year basis?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

What I'd like to do is answer that historically. We believe from the time we made the Dow acquisition through the end of 2018, Olin's operating rates were actually slightly better than the industry. In 2019, we believe that reversed. We have a significantly larger exposure to the urethanes chain, both MDI and propylene oxide producers, than we do to the vinyls chain. So I believe, in 2019, our operating rate was probably a little bit lower than the industry, and I would suggest that based on what we've seen so far in January, that will continue early in 2020.

Donald David Carson ***Susquehanna Financial Group, LLLP, Research Division - Senior Analyst***

Okay. And then just switching to Epoxy. So given the level of demand and where raws are, is the fourth quarter EBITDA -- of roughly $36 million, is that kind of a good run rate for each quarter as we go through 2020 or do you see any potential upside?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

Well, the run rate is heavily influenced by turnaround schedules. I would suggest, based on the turnaround schedule, we forecast that you're going to see a weaker level in Q2. And then seasonally, we typically see Q3 be stronger. And I would say, if you looked at the pattern we saw in 2019, that's a good pattern.

Donald David Carson ***Susquehanna Financial Group, LLLP, Research Division - Senior Analyst***

Okay. And final question, just on Winchester. You've talked in the past about a lot of channel inventory and customer inventory, where do you think we are in that right now? Is the -- do you think we're at the point where industry small caliber shipments can actually equal final ultimate demand?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

I think we saw that developing as we move through 2019. I think the one wildcard that the industry has faced is the withdrawal of Walmart from certain industry categories, specifically pistol ammunition and hunter's sporting rifle ammunition, which they essentially exited the business by December 1 and sold out their entire inventory. So I actually think we saw some purchasing at the end of the year in excess of what we would normally see. And we're going to see inventory replenishment, but it's not at Walmart. So the -- what I'll say is, the view is a little muddled at the moment.

Operator

And our next question will come from Frank Mitsch of Fermium Research.

Frank Joseph Mitsch ***Fermium Research, LLC - Senior MD***

Listen, regarding the chlor alkali shutdown announced in December, so I was hoping you might talk a little bit more about the thought process behind it. And I, again, am assuming that was on the higher end of your cost curve. Do you anticipate other shutdowns, either by yourselves or by the competition?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

Well, Frank, we announced that as part -- in concert with the shutdown of a chlorine derivative, which we've seen just declining demand to the point where it doesn't make sense to run the plant and that just gave us the opportunity to shut down the chlor alkali plant that feeds it or on the site it actually creates less demand. I'm not sure I want to comment on what other people are going to do. We're going to manage our system to optimize our costs. And if we get in a place where a plant makes no sense from an economic perspective, we will take action.

Frank Joseph Mitsch ***Fermium Research, LLC - Senior MD***

Got you. Got you. And just curious, I mean, I know it's very early days with respect to the coronavirus, but it seems to be a topic that comes up everywhere. And just my gut would suggest that Olin might be a beneficiary in terms of disinfectants, et cetera. Are you seeing any change in purchasing patterns due to -- with respect to the coronavirus?

Pat D. Dawson ***Olin Corporation - Executive VP and President of Epoxy & International***

Yes, Frank, this is Pat. Listen, first of all, I think it's important to remember that our exposure as Olin is very, very small. China represents less than 5% of our overall revenues. We do have an epoxy plant over in China that serves mainly our downstream markets, and this facility is currently down as it normally is this time of the year, and it'll start back up next week. So really, at the moment, back to your question, we haven't really seen any direct impact to our businesses. But we're monitoring that and watching it very closely to see if it could benefit us on the chlorine side as this evolves.

Frank Joseph Mitsch ***Fermium Research, LLC - Senior MD***

Yes. No, I would have anticipated that you would have seen bleach sales and chlorine sales move up. But at this point, it's too early to make that call?

Pat D. Dawson ***Olin Corporation - Executive VP and President of Epoxy & International***

Yes.

Operator

Our next question will come from Mike Sison of Wells Fargo.

Michael Joseph Sison ***Wells Fargo Securities, LLC, Research Division - Senior Analyst***

When you talked about the $250 million negative for pricing in 2020, if prices remain at fourth quarter levels, is that more front-end loaded? Does it primarily hit you in the first, second quarter? Any thoughts on how that flushes through?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

Let me clarify something. That's based on the -- that $250 million is based on the pricing we saw in January, not for the quarter.

Michael Joseph Sison ***Wells Fargo Securities, LLC, Research Division - Senior Analyst***

Got it.

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

And obviously, if you're looking at year-over-year comparisons, the GAAP narrows as we move through the year.

Michael Joseph Sison ***Wells Fargo Securities, LLC, Research Division - Senior Analyst***

Okay. Great. And just -- I know it's tough to forecast and predict, but what do you think needs to happen to get some momentum in caustic prices as the year unfolds?

James A. Varilek ***Olin Corporation - Executive VP & COO***

Mike, this is Jim. What we really need is we need that -- the industrial production side of things to grow. We'd love to see a pickup in the automotive market, also the -- some of the aluminum markets like aerospace, aircraft-s, commercial aircraft-s and so forth. And if we saw those pick up, that would obviously start to rebalance things between chlorine and caustic side.

Operator

Our next question will come from Jim Sheehan of SunTrust.

James Michael Sheehan ***SunTrust Robinson Humphrey, Inc., Research Division - Research Analyst***

A question on your earnings power. If we look back at 2014, your pro forma EBITDA was $1 billion. Since then, the caustic soda index prices are up a bit and chlorine and EDC prices are down, but natural gas prices have dropped from around $4 to $2.50. That should have given you a net EBITDA tailwind. And then when you consider cost synergies of $250 million and revenue synergies on top of that, you should have been able to generate about $1.3 billion or $1.4 billion of EBITDA in 2019, based on your sensitivities. But you did $941 million in 2019, that's about $60 million below the level of pro forma 5 years ago. How do you explain not being able to grow EBITDA over 2014 pro forma?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

I would say, I think you've thrown a lot of things at us there. And I would prefer to write down what you said and get back to you on that point because we're not going to pound through the pro forma and all the differences -- and I'm not saying you're wrong, I'm not sure exactly of the veracity of everything you said.

James Michael Sheehan ***SunTrust Robinson Humphrey, Inc., Research Division - Research Analyst***

Okay. Fair enough. Now it looks like your EBITDA is declining in 2020 at the current price levels, which means your net debt-to-EBITDA ratio might be rising. If pricing continues to erode, are you in any danger of tripping debt covenants this year?

Todd A. Slater ***Olin Corporation - VP & CFO***

Jim, as you know, in December, we redid our bank agreements that expands our leverage ratio for the next 2.5 years to -- which should enable us to ensure a level of compliance. And so we would expect that we will be fully compliant, including the investment outflows in 2020 with our bank agreements. And don't forget about the $250 million of incremental cash flow that starts in late '20 and is full bore in 2021.

Operator

And our next question will come from Matthew Blair of Tudor, Pickering and Holt.

Matthew Robert Lovseth Blair ***Tudor, Pickering, Holt & Co. Securities, Inc., Research Division - MD of Refining and Chemicals Research***

John, you mentioned the pricing environment was clearly pretty tough in Q4. Could you just provide some commentary on just overall volumes and just overall demand trends as you progressed throughout the quarter? Would you say that December was either stronger or weaker from a volume standpoint compared to October?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

Well, in October, we had some turnarounds, so that's not a valid comparison. I would say that what we saw in December, in the fourth quarter, generally, was quite a bit weaker than what we saw in the third quarter, and that was across the spectrum of chemical products.

Matthew Robert Lovseth Blair ***Tudor, Pickering, Holt & Co. Securities, Inc., Research Division - MD of Refining and Chemicals Research***

Got it. And then any thoughts on EDC's supply-demand? It looks like several new EDC plants in South Korea and China this year could raise global capacity by over 3%. What do you project for demand? And is there a concern that EDC might weaken as you progress through the year?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

I don't know -- I'm not going to forecast what it's going to do. What I would say is we've actually seen EDC in January and February and as we look at March, tends to pick up in terms of demand and pick up a little bit in terms of pricing.

Operator

Our next question will come from Eric Petrie of Citi.

Eric B Petrie ***Citigroup Inc, Research Division - Senior Associate***

So U.S. export prices for caustic soda have declined to $200 to $250 per ton. Can you just talk about the arbitrage windows that are still existent for you? And talk on how you're seeing transport costs develop?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

Obviously, the best arbitrage for Olin is to stay out of the straight export market. And I would say when you look at those prices, those are not prices that Olin sold at. Our best situation is to continue to export, if you will, into Latin America, where we continue to build out a distribution system and where we get prices significantly higher than what you see in the export market.

Eric B Petrie ***Citigroup Inc, Research Division - Senior Associate***

Okay. For my second question, a competitor recently announced pocket price initiatives. Have you done the same? And then broadly, could you change your strategy to go more downstream to support that near-term earnings target of $250 million EBITDA?

Pat D. Dawson ***Olin Corporation - Executive VP and President of Epoxy & International***

Yes, Eric, just a couple of comments. First of all, we had increases out there in January. We had very modest success with that. We do have increases out there for February as well. And your last point, we do continue to build our downstream businesses around formulated products, around wind and a few other areas. So that is a part of our strategic thrust as well.

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

But I want to emphasize, we are, at our core, a chlor alkali producer, which means we are going to stay in the upstream of the epoxy chain. That's where our strength is, and that's what we're trying to leverage.

Operator

Our next question will come from Mike Leithead of Barclays.

Michael James Leithead ***Barclays Bank PLC, Research Division - Research Analyst***

Just 2 quick ones on the input side of the equation. First, on your chlor alkali EBITDA sensitivity table. I noticed you added a little asterisk where you mentioned there might be some impact to the sensitivity because of your hedging activities for inputs. So I guess, can you just give us a sense of the level of input cost benefit you expect to realize in 2020? Since my guess is it's probably less than what the sensitivity would imply, given where natural gas prices are today.

Todd A. Slater ***Olin Corporation - VP & CFO***

Yes. This is Todd. If you -- as everyone on the call knows, we're a hedger. We do hedge gas and ethane for ethylene needs on a rolling 4-quarter basis. If you look today at where our hedge position is for natural gas and ethylene -- ethane for 2020 as well as a current futures' number for 2020, you're probably looking at good news year-over-year '20 versus '19, in the $40-plus million range.

Michael James Leithead ***Barclays Bank PLC, Research Division - Research Analyst***

Got it. Okay. That's helpful. And then to tie in with that, you mentioned earlier kind of the rough $250 million headwind number on pricing, if we run rate January numbers. Is that net of this benefit from cost reduction or is that just purely run rating gross pricing?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

That is run rating gross pricing.

Operator

And our next question will come from Steven Byrne of Bank of America.

Steve Byrne ***BofA Merrill Lynch, Research Division - Director of Equity Research***

You made some comments about the supply and demand imbalance on the chlor alkali chain that's leading to the lower pricing in caustic, but yet pricing on the chlorine derivatives are not very favorable either. Is it your view that the chlor alkali industry is too fragmented for there to be any idling of capacity to tighten this market up and drive pricing up?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

No, I don't believe that at all. I think if you looked at the industry operating rates, they're in the mid-80s. So we're just -- we're suffering from 2 things. We're suffering from lack of overall demand and then the imbalance between chlorine and caustic capacity at less than optimal levels.

Steve Byrne ***BofA Merrill Lynch, Research Division - Director of Equity Research***

Well, maybe an extension of this. Then on the Epoxy side, you commented about some of the end markets being weak and yet your volumes went up. Is that logical to push more volume in a declining price environment? Or would -- do you have the ability to tighten that by cutting back on production rates?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

Yes. The thing I would point out is that in 2018, we had 2 very significant 60-day turnarounds, one at our plant in Europe, one at our plant in the United States. So the 2019 volume increase would have been expected under all circumstances.

Steve Byrne ***BofA Merrill Lynch, Research Division - Director of Equity Research***

And then I have one question on your SG&A expense. It looks like you trimmed it in 2019 versus 2018. And perhaps, that is a reflection of the headcount reduction that you mentioned earlier. But if you go back to a few years post the acquisition from Dow, the SG&A expense was lower. What has been driving that up to more than offset the cost synergies from that acquisition?

Todd A. Slater ***Olin Corporation - VP & CFO***

Steve, this is Todd. One of the big items that runs through SG&A that has gone up from, I'll say, 2016, early 2017 levels, are the costs associated with this IT integration project, and that number was about $77 million in 2019. So that's the big driver from what you referenced, several years ago. But today, SG&A was down in '19 versus '18 in spite of $40 million of higher IT integration costs year-over-year. It was legal, consulting, incentive, stock-based compensation. I mean it was lower cost generally across the board.

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

And again, we keep emphasizing, that project is scheduled to conclude at the end of 2020. And we talked about $100 million of less spending in 2021, split between capital and expense. The expense piece of that is part of the G&A.

Operator

And our next question will come from Hassan Ahmed of Alembic Global.

Hassan Ijaz Ahmed ***Alembic Global Advisors - Partner & Head of Research***

You guys were kind enough to share with us that if we were to mark to market pricing at January levels, it would be around a $250 million EBITDA hit. Now obviously, we've seen crude oil prices and crude-linked sort of raw material prices come down a fair bit. We've seen similar sort of dynamics happen on the nat gas side of things. So what would that number EBITDA sort of benefit wise look like if you were to mark-to-market raws where they are currently in January? Obviously, taking into account the hedging activities and the likes you mentioned.

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

Well, we said in the remarks, qualitatively, we expected raw material costs in both chlor alkali and Epoxy to be down. Todd just gave a number associated with natural gas and ethane of $40 million to $50 million. And I can tell you on the Epoxy side, it's a similar number to that, and there are some other benefits coming from that.

Hassan Ijaz Ahmed ***Alembic Global Advisors - Partner & Head of Research***

Understood. Understood. Very helpful. Now moving on, in Q3, during the conference call, you guys talked about sort of continued destocking in caustic. I mean with pricing sort of sliding more, I would imagine that sort of destocking continue through Q4 as well. So where do you see sort of industry inventory levels right now?

James A. Varilek ***Olin Corporation - Executive VP & COO***

This is Jim. I think you're correct. From a customer standpoint, within a declining price environment, it's natural for them to run inventories down, and that started as early as the third quarter and moved through the end of the year. So we believe that customer inventories have moved down. I can't really speak to producer inventories. All I can say is that Olin's inventories are lower at the end of the year than they were in the third quarter.

Operator

[Operator Instruction] And our next question will come from Jeff Zekauskas of JP Morgan.

Jeffrey John Zekauskas ***JP Morgan Chase & Co, Research Division - Senior Analyst***

You're shutting down a chlor-alkali plant, another VDC plant, you talk about the chlor-alkali plant being 230,000 tonnes maybe the VDC plant by some caustic soda. And maybe you're not running at a high rate of the plants you're going to shut down. So what's the net capacity closure really for the industry and the shutting down of those units? And do you plan to shut them down in the first half or the second half?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

The capacity around chlorine and caustic soda, as we stated, 230,000 tons. We plan to shut these down in the second half of the year. We have contracts on the BDC side to run out, and that's then we'll be shutting them down.

Jeffrey John Zekauskas ***JP Morgan Chase & Co, Research Division - Senior Analyst***

Okay. And when you totaled up your -- I think it's $105 million in transition costs and additional working capital for Lake city and

in 2020. Would there be more in 2021 in terms of building capital? Or would we be done?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

Assuming that the business level at Lake City from the Army remains at a constant level, we would be done.

Operator

And our next question will come from Arun Viswanathan of RBC Capital Markets.

Arun Shankar Viswanathan ***RBC Capital Markets, Research Division - Senior Equity Analyst***

You guys delineated the price impact around $250 million, but just curious on the volume side. Last year, when you provided guidance in Q2 and Q3, you thought volumes had provided over $100 million uplift in the second half. I guess, did that materialize? And if not, is that something that we could look forward to when markets recover?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

That did not materialize. We said that the economic climate for us weakened throughout the year and that weakness accelerated in the fourth quarter. So I think from our perspective, especially if you look at some of the chains we serve on the chlorine side, urethanes, we would hope very much that there's a potential uptick in 2020 on a volume and a price perspective.

Arun Shankar Viswanathan ***RBC Capital Markets, Research Division - Senior Equity Analyst***

Great. So just going with that, I guess, in the past, you've provided a different walk through mid-cycle EBITDA in $1.3 billion to $1.5 billion range of $1 billion of annual EBITDA. Is that, I guess, still within the realm of possibility? And what would it really take? It seems like there's been not a large amount of capacity additions in chlor alkali. You guys are potentially shutting down a facility -- or are. I guess, are you surprised at all that pricing has been so difficult in many of the products? Especially since if supply is tight right now, and you're still not able to achieve some pricing, and I know that demand has obviously been weak, but is there anything other than weak demand that's realizing or resulting on this weak price factor?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

I -- from our perspective, we believe it is weak demand that is driving the prices down. You asked what it would take to get back up into the $1 billion or $1.2 billion. We talked about we experienced $450 million of negative price on caustic soda, plus the epoxy resin chain in 2019 versus 2018. And if I add that back to the EBITDA of 2019, we actually exceeded 2018's EBITDA. All the other things being equal, obviously, they're not, but...

Arun Shankar Viswanathan ***RBC Capital Markets, Research Division - Senior Equity Analyst***

Right. And then just lastly, just going back to the industry structure question. I guess, why wouldn't there be any further transactions? When I look at operating rates, I guess, in the mid-80s and then the potential for a relatively attractive North American production base, it would seem that some players may want to [add] from an international standpoint or whatever it is in the caustic because there could be more consolidation. Do you expect more consolidation in this space? And would you be in a position to drive that?

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

I think it is, from our perspective, highly unlikely that Olin, given its current market share in North America, could participate in the consolidation.

Operator

And our next question will come from John Roberts of UBS.

John Ezekiel E. Roberts ***UBS Investment Bank, Research Division - Executive Director and Equity Research Analyst, Chemicals***

Back to Frank's original question on China. Would you hazard a guess as to how much of the caustic capacity and Epoxy capacity in China is operating at below normal rates right now?

James A. Varilek ***Olin Corporation - Executive VP & COO***

This is Jim. That's a pretty tough call to make. I would say that there's a -- they did extend the Chinese New Year, they extended that and they do have plants -- their plants down. I can't give you a number on that. But I would just say that there's obviously more shutdown than there traditionally is, even though you're in the winter time period. That's about as good as I can do, John.

John Ezekiel E. Roberts ***UBS Investment Bank, Research Division - Executive Director and Equity Research Analyst, Chemicals***

Okay. And then just an accounting question here, Todd. On the $75 million for the VCM contract change, I assume that's primarily the expected margin on the ethylene that you're going to get. What's the revenue change associated with going to consolidating the VCM sales? And how much depreciation do we put against that $75 million? Can we just take the $493 million and straight line it over 20 years.

Todd A. Slater ***Olin Corporation - VP & CFO***

I'll start with the back and work my way forward. Yes. The $493 divided by 20 will be the amortization, that's right. We've not given a guide on revenue, but the revenue effect will be higher than the $75 million. That is clearly a net number.

Operator

As there are no further questions, this concludes our question-and-answer session. I would like to turn the conference back over to John Fischer for closing remarks. Please go ahead.

John E. Fischer ***Olin Corporation - Chairman, President & CEO***

I'd like to thank you all for participating in our call today, and we look forward to talking to you at the end of the first quarter. Thank you.

Operator

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