Q2 2017 Results Conference Call (Script)

Mark Davis

Good morning, ladies and gentlemen. Thank you for joining us for our conference call and webcast today.

As usual, joining me today is Rohit Bhardwaj, our Chief Financial Officer.

Before I commence the review, I would remind you that our presentation contains certain forward-looking statements that are based on current expectations, and are subject to a number of uncertainties and risks, and actual results may differ materially. Further information identifying risks, uncertainties and assumptions, and additional information on certain non-IFRS measures referred to in this call can be found in the disclosure documents filed by Chemtrade with the securities regulatory authorities, available at sedar.com.

One of the non-IFRS measures that we will refer to in this call is Adjusted EBITDA, which is EBITDA modified to exclude only non-cash items such as unrealized foreign exchange gains and losses. For simplicity, we will just refer to it as EBITDA as opposed to Adjusted EBITDA. Both these terms are fully defined in our MD&A.

I want to start by making a few contextual comments which will be detailed more fully during the rest of the call.

1. Generally all of our businesses performed well during the quarter with our Vancouver chlor- alkali operation performing extremely well;
2. There are a lot of unique financial positives and negatives reflected in the results for the quarter but these items essentially net off financially. Accordingly, the aggregate reported EBITDA numbers are a pretty fair representation of our operating performance despite the moving parts that we will highlight below;
3. The integration of our new assets and personnel is well advanced and unfolding as we had planned;
4. We took some steps and continue taking steps to simplify and optimize our balance sheet; and
5. Two of the items mentioned above involve the continued optimization of our asset portfolio. We closed the transaction selling our International segment (the results of which are treated as discontinued operations) and incurred costs in the quarter to cease production this fall at our small sodium chlorate plant in Nanaimo, BC, which is an immaterial contributor to our financial results.

Turning now to our actual results, the second quarter shows the early benefits of the Canexus acquisition that we completed in early March. As you know, the Canexus businesses, together with our legacy sodium chlorate facility in Prince George, now comprise our Electrochemicals, or EC, segment.

It was another very busy quarter for Chemtrade. We made significant progress integrating the acquired businesses, completed several initiatives simplifying our balance sheet from its composition immediately following the closing of the Canexus acquisition and closed the sale of our International business. Rohit will have more details later.

Our strategy of enhancing size, scale and diversity of earnings took a large step forward with the acquisition of Canexus. The new businesses significantly increased our EBITDA and distributable cash. EBITDA from continuing operations in the second quarter was $95.0 million compared to $56.8 million last year, an increase of 67%. Distributable cash after maintenance capital expenditures from continuing operations for the quarter was $58.7 million, an increase of 56%, or 9 cents per unit from the same period last year.

We are very pleased with performance of our new segment, EC. The integration of the Canexus businesses into Chemtrade has been smooth, and their contribution to Chemtrade is quite evident as they represent the majority of the EC segment results. The chlor-alkali business, which was an entirely new product group for Chemtrade, is performing very strongly. As noted on our last call, caustic prices are significantly higher than they were when we did our run rate calculations for the acquisition, and our hydrochloric acid volume is also stronger.

As mentioned above, we are making one change to the asset portfolio we acquired on the Canexus acquisition. We acquired three sodium chlorate plants in North America — Brandon, Manitoba; Beauharnois, Quebec and Nanaimo, British Columbia. The Nanaimo plant was small, high cost and had only one customer. Since we can supply that customer from our other sodium chlorate facilities, we made the decision to close Nanaimo, effective September 1 this year. There will be some closure costs, but the closure will not have a material impact on EBITDA. We want to thank the Nanaimo employees for their contributions. It is an unfortunate fact that this plant is not economically viable, which has led to this action in spite of the excellent efforts of our Nanaimo employees.

Results in our Sulphur Products and Specialty Chemicals (or SPPC) segment were lower than last year but higher than our Q1 results as our plant operations improved. Recall that last year's results included our Augusta plant's normal sales to the across-the-fence customer Fibrant who ceased operations later in 2016. As we noted on our last call, we have re-started the Augusta plant selling to a new across-the-fence operation, but that plant is unlikely to generate the same level of EBITDA as before the Fibrant shutdown.

Our Water Solutions and Specialty Chemicals (or WSSC) segment is doing well. We continue to see stability in the water business and the first phase of our potassium chloride expansion at our Midlothian, Texas plant is already delivering positive results.

Rohit will now provide you with some more details on the second quarter results.

Rohit Bhardwaj

Thank you, Mark and good morning everyone.

As Mark indicated, it was a very strong quarter for Chemtrade, with solid contributions from the new businesses. As noted, Aglobis, our former International business, has been treated as discontinued operations since entering into an agreement on February 24 to sell the business to Mitsui. That sale, for €36.8 million (subject to a working capital adjustment), was completed on May 31. We realized an after tax gain of $15.3 million on that sale.

Revenue from continuing operations for the second quarter of 2017 was $407.4 million, an increase of $145.3 million from 2016. This increase was primarily due to revenues generated by the newly acquired businesses, partially offset by lower revenues in the SPPC segment due to lower sales volumes and selling prices for sulphuric acid.

Aggregate EBITDA from continuing operations for the second quarter of 2017 was $95.0 million compared with $56.8 million in the second quarter of 2016. The increase is mainly attributable to the contribution of approximately $39.3 million from the new business in our Electrochem (or EC) segment. As Mark mentioned there were a few large atypical items in the quarter that essentially offset each other. On the positive side, we settled an insurance claim related to a pre-acquisition incident at the North Vancouver chlor-alkali facility, resulting in a gain of $8.2 million.

On the other side, more than offsetting the insurance recovery were $8.7 million of atypical expenses related to the Electrochem business. These were a $5.4 million charge for severances and a realized foreign exchange loss of $3.3 million. This related to the unwinding of a cross-currency interest rate swap. Accordingly, as Mark mentioned, EBITDA of $95 million is reflective of this quarter's performance. There was one additional item in the quarter which did not affect EBITDA but reduced Distributable cash. We paid a premium of approximately $3.0 million to redeem 35% of Electrochem's high yield notes.

For the three months ended June 30, 2017, Distributable cash after maintenance capital expenditures from continuing operations was $58.7 million, or 63-cents per unit compared with $37.6 million or 54-cents per unit in 2016. The per unit amounts are based on a weighted average number of units outstanding of 92.6 million units in the second quarter this year, versus 69.1 million units outstanding last year.

Turning to segmented results for the quarter, SPPC generated revenue of $127.0 million compared to $144.6 million in 2016. EBITDA for the quarter was $32.8 million, which was $6.1 million lower than 2016. From a revenue perspective, the main reason for the year-over-year decrease was $10 million of lower revenues for sulphuric acid due to the effect of the Fibrant shut down, and due to lower selling prices. We also had $8.0 million of lower revenue due to reduced volumes of liquid sulphur dioxide or SO_2 as a result of exiting manufacturing and selling SO_2 in eastern Canada towards the end of 2016. EBITDA was lower due to the impact of the Fibrant closure and its effect on our Augusta plant, as the plant was running at full rates during the second quarter of 2016. We also had lower volumes of sulphuric acid and some additional costs due to unfavourable sourcing mix for sulphuric acid.

Our WSSC segment reported second quarter revenue of $115.7 million compared with $107.3 million in 2016. As noted earlier, the sodium chlorate business in Prince George, which was formerly part of the WSSC segment, is now part of EC, and all amounts for this year and prior periods have been adjusted to reflect that change. EBITDA was $32.4 million compared with $29.5 million generated in 2016. The increase is due to higher volumes and prices of water products and of potassium chloride or KCl following the first stage of our expansion at that site.

Our EC segment reported revenue of $164.7 million, $153.8 million of which is attributable to the newly acquired business. EBITDA was $41.7 million, with $39.3 million contributed by the new business. It should be noted that results include severance costs of roughly $4.0 million incurred during the quarter.

Excluding unrealized foreign exchange gains, Corporate costs during the second quarter of 2017 were $11.8 million, compared with $13.7 million in the second quarter of 2016. Corporate costs for the second quarter of 2017 include the $8.2 million insurance recovery discussed previously. It also includes the realized foreign exchange loss of $3.3 million I'd mentioned and corporate costs for the acquired business of $2.5 million, including $1.4 million of severance costs.

Maintenance capital expenditures in the second quarter were $12.9 million. We expect maintenance capex in 2017 to be approximately $80.0 million, which includes the newly acquired business at an annual run rate of $30.0 million. Non-maintenance, or growth, capex in the second quarter was $2.8 million. As we have noted in the recent past, we are spending some small amounts of growth capex on the new polyaluminum chloride or PACl and aluminum chlorohydrate or ACH plants, and the adjuvants facility in New Jersey.

In addition to the $30.0 million sustenance run rate for our new assets, as we announced last quarter, we intend to spend about $50.0 million over the next 5 years to restore Brandon to the state required to ensure it remains a long-term, reliable, low cost supplier of sodium chlorate. There was no significant spending on these items in Q2.

Finally, some comments on our balance sheet.

Following the Canexus acquisition, we initiated a number of actions to simplify our balance sheet.

First, we made mandatory change of control offers for all outstanding unsecured Chemtrade Electrochem (formerly Canexus) Debentures and high yield notes. We also announced that we would redeem any of the Electrochem 5.75% Debentures that didn't accept the offer to purchase and Chemtrade's 5.75% legacy convertible debentures that were maturing at the end of 2018.

In May we issued $201.3 million 4.75% unsecured debentures, and used part of the net proceeds to fund the change of control offers for the Electrochem debentures, the redemption of our legacy debentures, and the remaining 5.75% Electrochem debentures which didn't tender to our offer.

As a result

- we acquired a total of $80.3 million principal amount of the debentures tendered under the change of control offers;
- completed the redemption of the remaining Electrochem 5.75% debentures that hadn't accepted the offer; and

- redeemed the remaining $79.6 million aggregate principal amount of the Chemtrade 5.75% debentures.

None of the high yield notes were tendered into the change of control offer, and on June 26 we redeemed $38.5 million aggregate principal amount, representing 35% of the $110.0 million principal amount outstanding.

Following the completion of the change of control offers and the redemption of the remaining outstanding 5.75% Electrochem debentures, from an Electrochem (or former Canexus) perspective there were approximately $84.0 million of the 6% debentures, $74.6 million of the 6.5% debentures and $71.5 million of the Electrochem high yield debt outstanding.

Earlier this quarter we announced an offer to exchange the outstanding Electrochem 6% and 6.5% debentures for Chemtrade new convertible debentures with coupon rates of 5.5% and 5.75% respectively.

This morning we extended the offer period from August 10^{th} to August 23^{rd} in order to allow additional debenture holders to respond.

I'll now hand the call back to Mark.

Mark Davis

Thank you, Rohit.

The primary focus of our efforts in the second quarter was the integration of the Canexus businesses while also moving our legacy businesses forward. As I said in my opening remarks, integration is going well and we're very pleased with the contribution the businesses and our new employees are making to Chemtrade.

We are well on track to achieving the synergies we expected. As we have said before, we hoped to achieve about $10.0 million of synergies, and all the indications are that we will do that. Most of that should be evident by the end of next quarter.

Two specific comments that relate to the EC segment.

First, I wanted to briefly discuss hydro rates in Manitoba. Our Brandon, Manitoba facility accounts for over 70% of our North American chlorate supply (once Nanaimo has ceased production). You may have seen that Manitoba Hydro was seeking to increase hydro rates by almost 8% this year and a similar amount next year. As power represents about 75% of our cost to produce, an increase of this magnitude would have been detrimental unless it could be recovered in price. Recently the Public Utility Board rejected Manitoba Hydro's request for such a large increase and instead ordered an interim increase of 3.6%. This increase is more in line with our expectation of power increases in Manitoba and more reflective of histirical increases. We will continue to work with the PUB to ensure that only price increases that are fact-based and are not harmful to the Manitoba economy are approved.

Secondly, I mentioned that we are benefitting from high caustic prices. Caustic prices continue to run at a rate more than $90 per tonne higher than the price we used to calculate the acquisition run rate. While historically chlor-alkali earnings are cyclical and we expect that at some time they will cycle again, we currently see no signs that caustic pricing is going to abate. Although we do not generally forecast price movements, industry publications are indicating that the outlook is for continued strength in caustic pricing as global demand stays healthy. Further, our hydrochloric acid demand has significantly increased as fracking activity has picked up. We can't forecast how long these dynamics will persist but don't see anything in the near term or well into 2018 that should change this. As noted in our last call, if prices retreat and we return to the $6.0 million run rate we bought off, our thesis for buying Canexus remains intact.

Finally, as you would have noted, capex was lower in Q2 than our run rate for the year, but it is ramping up. Also, the 5-year $50.0 million capital spending program at Brandon which we had previously mentioned is being planned so it can be implemented efficiently and effectively. Just to reiterate some comments from our last call, this work will not expand capacity, but it will ensure that Brandon remains the long-term, reliable, lowest cost producer of sodium chlorate in North America. As we also noted, we do not expect any interruptions to production while this work is underway.

So, in summary we are well positioned to continue delivering value to our unitholders. In the first full quarter following the Electrochem acquisition we generated EBITDA of $95 million, substantially advanced our integration efforts, and simplified both our business portfolio and balance sheet. Looking forward, demand for most of our products remains strong and we are well positioned to continue taking advantage of opportunities as they arise.

Thank you for your attention. Rohit and I would now be pleased to answer questions.

Operator: Thank you. Ladies and gentlemen, we will now begin the question and answer session. Should you have a question, please press star, followed by one on your touch-tone phone. You will hear a three-tone prompt acknowledging your request, and your questions are polled in the order they are received. If you are using a speaker phone, please lift the handset before pressing any keys. Your first question comes from Jacob Bout from CIBC. Jacob, please go ahead.

Jacob Bout: Good morning.

Mark Davis: Hey Jacob.

Rohit Bhardwaj: Morning.

Jacob Bout: I had a few questions on the electrochemical business. I guess first off the chlor alkali volumes of the 62,000 tonnes in the quarter, that was a little bit higher run rate than what they have done historically. Is that kind of a run rate that we should be thinking about longer term?

Mark Davis: Yes. Yes to both questions.

Jacob Bout: Okay. Why the higher rates?

Mark Davis: As you all have followed Canexus previously, you would have noted is they had a number of teething problems for a number of years post their technology conversion at Vancouver, and had spent money, time and effort actually trying to rectify the issues as they arose. So the first thing is that the plant is in better reliable operating shape now than it was a couple of years ago.

Secondly, as we mentioned, increased demand for hydrochloric and chlorine let us take advantage of the enhanced reliability and actually operate the plant harder because as you know we need an outlet for chlorine and hydrochloric as well as the caustic to actually run at full rates.

Jacob Bout: You made some comments about when you were looking at Canexus, you were thinking it was a lowered valued—North Vancouver was a lower valued asset. Was that like a $10 million EBITDA business and would be now a $20 million EBITDA business? Is that how we should think about it?

Mark Davis: Yes. I guess we do it this way. If you want to keep it on an apples-to-apples basis, their SG&A allocation to the plant is the last reported number that we would have had to—when we did the deal was it reported about a $6 million EBITDA run rate. Right? Now, included in that $6 million was a bunch of production interruptions, so, again, on an apples-to-apples basis that $6 million was probably $10 million even at historical pricing and historical volumes. So you take that $10 million number and then you take extra production and increased pricing in particular for caustic but also on hydrochloric and that 10 number grows substantially. One of the numbers we gave in here is if you make 220,000 tonnes of caustic and pricing is up $100 from what it was what we bought off of, that's 10 plus 22, right? We've indicated we think caustic still has room to run and hydrochloric pricing is also increasing.

Rohit Bhardwaj: I just want to clarify one thing. The 62,000 tonne volume you talked about, just to remind you that actually includes Brazil so it's not North America, and so there may be a bit of confusion if people are just comparing it to what Canexus used to report as North American chlor alkali volume. Having said that, that is higher than in North America as well, but just to clarify that.

Jacob Bout: What were the volumes out of Brazil roughly?

Rohit Bhardwaj: We haven't really broken that out because in our kind of world order we don't want to segment it too much, but we've said in the past that our North American chlor alkali volume should be in 200,000 tonne annual kind of range, so you can assume that's a good guide for what it would have been in this quarter.

Jacob Bout: Okay, that's helpful. Then what's the increase with the electricity rates at Brandon? How are your—are your contracts structured in such a way that any price increase in electricity prices will be automatically reflected?

Mark Davis: As a general answer, no. Some are but most of the industry actually does not have power passthrough provisions in their contract. On the other hand — I'm going to get my number wrong but 25% or 30% of the industry capacity is located in Manitoba. The industry is running at very high rates. If there's cost escalation, it will get reflected in price at some point in time.

Jacob Bout: How about the Canadian dollar?

Rohit Bhardwaj: I think same response to that, although two-thirds of chloride production is Canadian based and two-thirds roughly of demand is U.S. based, so the same dynamic should play out as product does move across the border. Not contractually but through market conditions.

Mark Davis: And on both of those comments is over time.

Jacob Bout: Okay, I'll leave it there. Thank you.

Operator: Thank you. Your next question is from Nelson Ng from RBC Capital Markets. Nelson, please go ahead.

Nelson Ng: Great, thanks. Hi, just a quick question on Canexus. You mentioned that there were some severance costs and you're looking to kind of simplify the debt structure. Then also the Nanaimo facility closures. Are you expecting to see any other charge-off, one-off charges or any other things for the rest of the year? You mentioned that Nanaimo was not going to be material but should we expect to see any other charges in the second half?

Rohit Bhardwaj: The severances we incurred were partially, mainly for the head office people. There's a million dollars for Nanaimo, so we don't expect any more severances for Nanaimo. There may be some costs as we wind that down but they should not be material. There is a little bit of severances later in the year, but again, not material. I think most of it is now behind us so you shouldn't be expecting anything material for the back half of this year.

Nelson Ng: Okay, got it. Then just one quick question on Augusta, the facility. You mentioned that it's selling to another customer. Could you give a rough indication of what the cash flow reduction is relative to the previous contract?

Rohit Bhardwaj: What we have said was that in our contract that we had with Fibrant, with the customer there, we had contractual protection for a few years at about 50% of what they were contributing, and then what we had said was as we get into this new relationship, the new contribution from this business should be around the same, so you can expect that more than—about a 50% reduction in current terms and so it's roughly a million dollars a quarter or $4 million a year, and that's based on current run rates. The hope is that this is kind of a longer term operation that has some legs to it and some potential upside, but I think for our purposes for now let's just assume that's a $4 million run rate which is roughly half of what it used to be.

Nelson Ng: Okay, so just to clarify, so I guess near term because you're getting 50% protection from Fibrant and the new contract is about 50%.

Mark Davis: No, no.

Rohit Bhardwaj: No, no. No.

Mark Davis: It is that you have an obligation to mitigate under the Fibrant contract, so the new earnings essentially replace the Fibrant contractual payment. From our perspective there's potential upside if actually the new guy actually runs harder and better, and certainly it should last for a longer duration because the Fibrant contract ended 2021, I think, right? So we hope there’s upside from where we are in both profitability and term. This year actually is one basically replaces the other.

Rohit Bhardwaj: Yes.

Nelson Ng: Okay, got it. Thanks.

Mark Davis: Thanks.

Operator: Thank you. Your next question is from Joel Jackson from BMO Capital Markets. Joel, please go ahead.

Joel Jackson: Hi. Good morning guys.

Mark Davis: Hi.

Rohit Bhardwaj: Good morning.

Joel Jackson: Could you maybe walk us through for each segment SPPC, WSSC, ElectroChem, how you see earnings developing in the second half of the year versus the first half of the year, and maybe you can talk about utilization, is this in plan? Pricing? Outages? Volumes and whatever you can to help us figure out how the second half earnings are going to develop for the different segments versus first half?

Mark Davis: I thought you would just come and actually take our internal budget, Joel. We actually don’t give that kind of specificity of our forecast. What we could say is that—I’ll tell you certain things and we’ll see where we get to, right?

Similar to other years is our second and third quarters should be stronger than our first and fourth. Our fourth quarter obviously it should be stronger this year than it was last year with the Canexus addition and actually fewer operating issues.

Rohit Bhardwaj: I think SPPC last year’s Q4 was very weak so we should be better than that.

Mark Davis: That’s right. Right? So there’s those few general statements. A few more specific statements is that we see our Electrochemical segment continuing to perform well and hopefully continuing to strengthen as we’ve seen no signs of those key products I mentioned actually lessening. We see SPPC again should continue to be good. Regen continues to run strong. Our Ultrapure business is good, so we continue to see actually now more strength and consistency in that segment than we actually saw I guess in the fourth quarter/first quarter last year and this year, respectively. In our WSSC segment, again, with the exception of that little seasonality in the water business, third quarter versus fourth, we think that segment’s on track to continue generating relatively consistent earnings going forward.

Joel Jackson: You had a large dropoff in WSSC in Q4 because of some operational issues and expansions and plant issues. You had a much smaller drop-off in Q4 ’15 versus Q3. So would that—should we expect.

Mark Davis: ’17 should look more like-

Rohit Bhardwaj: Fifteen, yes.

Mark Davis: Fifteen. It’s that we had specific plant issues at the end of the year last year.

Joel Jackson: Okay. Then finally in SPPC we’ve seen sulfur and sulfuric acid prices in the North America tick up a little bit the last little while. We’ve had a lot of different outages at different plants and smelters in North America in the middle of the year. How do you see pricing sort of developing for sulfur/sulfuric acid second half of the year? What are you seeing in the market? What’s the Copper Cliff impact? What should we think for all of that?

Mark Davis: I think it goes like this, is remember—and in our world actually, in the acid world our big driver is really the regen markets, then we talk about the ultrapure market, and last we talk about merchant sulfuric acid. So, again, as we see continued strength in actually the regen and ultrapure markets for, I guess, frankly, I think you all know, is in the merchant market it’s our view that supply/demand dynamics are—I don’t want to say strong but are definitely firm, right? We’re hopeful that actually pricing starts to follow our belief of dynamics and we’ll know for sure whether or not that happens during the year-end contract season, but for the reasons that you mentioned, a bunch of supply reductions and some ticking up in the activity in certain industries is, we think that actually there’s room to move and we’ll see how successful we all are come 2018.

Rohit Bhardwaj: I guess just keep in mind that as usual we’ll spend more cap ex in the back half of the year.

Joel Jackson: Thank you very much.

Mark Davis: Sorry, I’ll give you one more, even though you didn’t ask for it. Remember, actually, on merchant acid pricing is even if it moves we give away a bunch of that to actually our byproduct suppliers under our risk shared contracts, right?

Joel Jackson: Yes, thank you.

Mark Davis: Thanks.

Rohit Bhardwaj: Thank you.

Operator: Thank you. Your next question comes from Benoit Leprade from Scotiabank. Benoit, please go ahead.

Benoit Leprade: Thank you. Good morning gentlemen.

Rohit Bhardwaj: Good morning.

Benoit Leprade: A few questions. First going back to the Nanaimo closure, just curious. So the severance costs are pretty much behind you. I was wondering if on one hand you would have more site remediation costs, or alternatively would that site have some potential for real estate and ultimately could be a cash benefit?

Rohit Bhardwaj: I guess from a remediation perspective, we still have to evaluate all our options there, but for accounting rules you're required to have asset retirement obligations on the books, which we do. We have asset retirement obligations for all of our sites, but having said that we have to evaluate a plan of whether there's some useful life to that site, whether it's, like you said, redevelop for different use. So those are things that are going to develop but we don't expect any unfavorability coming out of that.

Benoit Leprade: Will you be serving the customer from Brandon or Prince George?

Mark Davis: We'll be serving them in the most expeditious, cost effective way that actually satisfies his requirement.

Benoit Leprade: Okay. Second, on the corporate costs side there was a few puts and takes but what would be—assuming no big change in LTIP, what would be a normal run rate for corporate costs on a quarterly basis?

Rohit Bhardwaj: I think what we—in the current structure, probably in the $55 million to $60 million range.

Benoit Leprade: Okay, and is it too early to get a sense of how much capex we should expect for 2018, both maintenance and growth? How much of the 50 for Brandon should we expect to be spent in '18?

Rohit Bhardwaj: I think probably $90 million to $100 million for next year, and we are, as Mark said, we are still working on the Brandon plan because it is a longer term plan to see what's the most efficient way to deploy the capital there. We can give more clarity on that as we get into the third quarter and we have done more of our planning cycle.

Benoit Leprade: The 90 to 100, that's all maintenance or all-in including growth?

Rohit Bhardwaj: That's all maintenance and we don't at this stage have a lot of additional growth slotted for 2018.

Benoit Leprade: Okay. Lastly for me, Fibria is reported to be taking significant downtime at their plant in Barra do Riacho in Brazil in Q4 making room for their new plant in Três Lagoas and there's discussion or speculation how much longer that downtime could be taking. Could you remind us exactly what are the impact of the fixed margin contract you have down there is Fibria would produce more or less in the future?

Rohit Bhardwaj: We do have our contract is a fixed margin contract but it is subject to volume risk. So to the extent they take volume we get a fixed margin, so we do have exposure. Now, having said that, we aren't sure whether—how much downtime they actually are going to take and there is some merchant opportunity there to the extent they take some lower volume of product from us. So, at this stage, we are not expecting it to be material in 2017, and we don't expect that this is going to be a long-term thing. As well as we can see the pulp market needs supply and this is a large operation that they have, so we aren't expecting to be anything permanent or long term, and in the short term we don't expect a material impact out of it.

Benoit Leprade: Well, thank you very much.

Mark Davis: Thanks, Benoit.

Operator: Thank you. Your next question is from Anoop Prihar from JMP Securities. Anoop, please go ahead

Anoop Prihar: Good morning. Just one question for me. Of the $95 million of EBITDA that you guys just reported, on a year-over-year basis can you quantify what the impact is from just better pricing on hydrochloric and caustic?

Rohit Bhardwaj: I guess what's interesting is clearly our comparative numbers don't have anything for those items in 2016, so on the—so really you're looking at what would have happened in the ElectroChem standalone world, correct?

Anoop Prihar: Yes.

Rohit Bhardwaj: I think the best thing for that, I mean what you can do quite easily is look at what was reported by Canexus in Q2 of last year because they were a public company and you should be able to get those comparative numbers there. As Mark had mentioned, a lot of that uptick is coming from chlor alkali because caustic—chlor alkali tends to be more stable.

Mark Davis: If you want a simple way of doing it, if you assume we make 200,000 tonnes of caustic in Vancouver, so assume we make 50,000 a quarter, price is up 100 bucks, right? So there's $5 million of that there and there's more with hydrochloric, too.

Rohit Bhardwaj: So for perspective, last year in Q2 the North American chlor alkali segment for ElectroChem actually lost money or kind of broke even you can call it. This year that is obviously a lot higher so a lot of that upgrade is coming from there.

Anoop Prihar: Okay. Thank you.

Mark Davis: Thanks.

Operator: Thank you. Your next question is from Steve Hansen from Raymond James. Steve, please go ahead.

Steve Hansen: Yes, hey guys. Just one for me on the Midlothian expansion. It sounds like that's starting to contribute now but is there any more downtime expected with that expansion plan going forward? What is the cadence there that we should expect?

Mark Davis: You shouldn't expect any significant downtime, right? Having said that, when you tie into things there might be a few teething pains but it's not like this plant has to stop for a month to actually do what it's doing, right? So, I think that for your purposes at an aggregate level is you shouldn't see any material down—you shouldn't see any financial impact from any downtime we would have to do.

Steve Hansen: Okay, that's helpful. Just trying to get a sense. I think Joel might have alluded to this in his question, but you guys have had a couple of quarters of I'll call them operational hiccups. I'm just trying to get a sense for whether there's any of those that we should be expecting in the back half of this year or if those are well behind us now.

Mark Davis: We always hope they're well behind us. There are a number of regen plant turnarounds coming up, right? But those aren't unexpected by us and it kind of ties with the increased cap ex load that you always see late in the year.

Rohit Bhardwaj: But nothing peculiar to 2017. If anything, 2016 in Q4 we had a fair amount of downtime.

Steve Hansen: Understood. No, that's helpful. Then just lastly on the other small expansions on the PACl side, just give us an update as to where you're at there and whether there's any plans in the future for additional growth. It sounds like next year will not include any but down the road and broader strategic plans for that group.

Mark Davis: Yes, so we're—what we have is actually, I'm going to say starting or started up, right? The sales pipeline is filling out and we're feeling pretty good about that. We'll probably rest for 2018 as we survey the market and determine whether or not there's demand for us actually to either construct another PACl plant or ACH plant — as we've said, we like those products. They're good sticky products. They perform well for the customer at a lower all-in cost, but alum should still be the workhorse. So, we think we have what we need for now but we'll keep our eye on it.

Steve Hansen: Okay, great. Just the last one actually, if I may. It's just on the M&A front. You guys are clearly still digesting or close to I guess finishing here on Canexus. What do you see in the landscape, Mark? Do you get a sense for how the pipeline looks at this moment? Are you interested in more? Any thoughts on the broader M&A front would be helpful.

Mark Davis: Sometimes I think I should just record this from quarter to quarter but I'll try it right. Joking aside, although Canexus was a large chunk of EBITDA for us, right? It was a relatively small number of plants serving a very, very similar customer base, and actually their culture wasn't all that different than ours, right? So that from an integration perspective—although, look, there's lots of people doing lots of hard work is we're well advanced on that, and since we actually don't always find assets that we like we're always looking and if we find something that fits, we see whether or not we can make that happen.

What I have said, I think, the last few quarters, and I'll say it again, is that it looks to us as though valuations in today's world are relatively high and to make acquisitions work you probably need to be able to realize synergies or have a good strategic reason to actually staple something on. So, we're looking. If the right thing came along and we could execute on it, we're not interested in levering our balance sheet any further so the valuation would have to work. If the right thing came along, yeah, we would do it. There's lots of stuff in the market now, which is I guess not unusual when valuations are pretty high.

Steve Hansen: Okay. Very helpful, thanks.

Operator: Thank you. Your next question is a follow-up from Joel Jackson from BMO Capital Markets. Joel, please go ahead.

Joel Jackson: Thanks. I had a couple of housekeeping questions. Rohit, depreciation for ElectroChem was quite high. I think it was $24 million in the quarter. That's much higher than the Canexus depreciation run rate, so what's going in the background?

Rohit Bhardwaj: What happened is when you do an acquisition for accounting rules, you're supposed to write up the value of the assets to their current market value and that's what dictates the depreciation going forward, because otherwise if you have your own existing business, you do not write up your value for the assets. You look at the original cost and depreciate based on that, but when you do an acquisition there's a purchase price allocation that requires you to write up value of assets, and that's still—you still have another year to firm that up so there was some adjustments in Q2 and there may be some further adjustments to go out in Q3 but that's what really dictates the higher depreciation and amortization.

Joel Jackson: So, Canexus is doing like a $50 million annual run rate for their assets. Is that about right for ElectroChem? Add a bit for your plant, extra plant?

Rohit Bhardwaj: Sorry, could you repeat the $50 million for what?

Joel Jackson: They're running at about a $50 million depreciation rate and then you add in a little bit for your own chlorate plant, would that be right?

Rohit Bhardwaj: Okay, yes but do you understand that what I just said was that we ……

Joel Jackson: What's the run rate then you think for depreciation for EC going forward?

Rohit Bhardwaj: I'll probably give you that response in Q3 because Q2 had some adjustments to it because what happens is when you do an acquisition you take a first kick at what you think the market values are. Then you engage a professional valuator to come back with fair market values, which we haven't received yet, so Q3 we should be able to give you a much better idea as to what a good run rate for depreciation is.

Joel Jackson: Okay. Then you talk about maybe $90 million to $100 million of maintenance cap ex next year, so I wanted to ask does that mean that all the growth cap ex for KCL and PAC is done in '17? Then $90 million to $100 million, does that include some initial idea of how much Brandon's special cap ex will be in?

Mark Davis: I guess we're trying to answer the question before we're ready to answer the question, right? So, again, you'll get more clarity in the third quarter right. Around $100 million all-in is probably a good place-

Rohit Bhardwaj: Including Brazil, yes.

Mark Davis: Including, a good thing to assume, right?

Joel Jackson: Okay. Then my last question is you talked about some asset regen plant turnarounds. Is that weighted to the fourth quarter or is a little bit in Q3 as well?

Rohit Bhardwaj: There will be a little bit in Q3 but, again, comparatively speaking it wouldn't be as much as Q4 last year.

Joel Jackson: Okay. Thank you very much.

Rohit Bhardwaj: Okay.

Operator: Thank you. Your next question is from Benoit Leprade from Scotiabank. Benoit, please go ahead.

Benoit Leprade: Thank you. Just follow-up on the chlor alkali side of the business. Obviously the timing appears very good. The business is improving. The volatility is something you've never partly appreciated. Just curious how—does that change your view of that asset? Or does that change the view of other people's of that asset and do you think that you could be considering divesting of this one earlier than previously planned?

Mark Davis: I don't know how it changes other people's views of the asset, but — what we said when we bought it is that we don't generally actually like volatility, as everyone knows, but we also said that actually a piece of volatility as part of our aggregate whole is something we don't mind living with, and especially if you actually bought it off of what appears to be a trough. So, we like the asset. We plan to keep the asset. Whether or not other people have a different view of the asset now that it's making this much money is they might but we're quite happy with it as part of the overall portfolio.

Benoit Leprade: Thanks. Fair enough.

Operator: Thank you. Ladies and gentlemen, as a reminder, should you have any questions, please press star, one.

There are no further questions. You may proceed.

Mark Davis: Thank you everyone for your time and attention, and we'll look forward to talking to you next quarter.

Operator: Ladies and gentlemen, this concludes today's conference call. Thank you for participating and we ask that you please disconnect your lines.