Q4 2016 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.

In order to give a clearer insight into the performance of our ongoing business, the discussion of both fourth quarter and 2016 EBITDA and Distributable cash will exclude three specific items.

First, as we did when discussing third quarter results, we will exclude the $20.3 million foreign exchange loss resulting from the repayment of US dollar bank debt.

Secondly, we will exclude the $8.5 million of costs related to the Canexus Acquisition incurred in the fourth quarter.

And finally, we will exclude our Aglobis, or International segment. As announced yesterday, we have entered into an agreement to sell Aglobis to Mitsui International. Therefore, our International segment has been treated as discontinued operations in our December 31st financial statements. Our comments today will be on continuing operations, which will increase significantly once the Canexus transaction is closed.

As you can appreciate from those introductory remarks it was a very busy fourth quarter. There was significant corporate activity directed towards improving and growing our portfolio by reaching an agreement to acquire Canexus and by implementing our decision to sell the International segment. I will have more to say on both of those matters shortly.

First, I will provide some comments on our operating results from continuing operations. Excluding the items I mentioned at the beginning, for the full 2016 year Chemtrade's continuing operations generated distributable cash after maintenance capex of

$128.5 million, or $1.86 per unit. This was comfortably ahead of our annual distributions of $1.20 per unit.

Chemtrade's fourth quarter business performance was essentially in line with the guidance we provided in November during our third quarter call. We indicated in that call that the cumulative effect of the issues outlined would be that Adjusted EBITDA for our North American business segments in the fourth quarter would be roughly 20% of annual Adjusted EBITDA for 2016. We came in very close to that estimate. We will review the various items and their impact on the fourth quarter in the appropriate segments.

As expected, the Sulphur Products and Performance Chemicals, or SPPC, segment's fourth quarter EBITDA in 2016 was lower than 2015 for the reasons we had outlined, including a number of plant maintenance turnarounds and the loss of production at the Augusta sulphuric acid plant. Our Water Solutions and Specialty Chemicals, or WSSC segment also reported lower EBITDA in the fourth quarter than the same period last year. The primary reason was lower production resulting from operating issues at one of our larger water plants and at our potassium chloride plant in Midlothian, Texas. The operational issues at the water plant were largely fixed during the first quarter of 2017.

We continue to be pleased with the results of our strategy of expanding the product range in our water solutions business. Our second polyaluminum chlorate (or PACl) plant and our new aluminum chlorohydrate (or ACH) plant are scheduled to come on stream towards the end of the first quarter. The reduced production at Midlothian was largely planned as it related to the implementation of the first phase of the expansion plan we noted last year.

So, to summarize, the fourth quarter results were below our going forward expected earnings, but were in line with the expectations we outlined in the third quarter, with the exception of the operational issue at our water chemicals plant.

Last, let me provide a little colour on the sale of our International segment. As we noted on our last call, the International business was going through a step-change with the significant reduction in the deep sea element of this business. During 2016, this business incurred significant, for that segment, restructuring costs. Excluding those costs, it would have generated EBITDA of about $5.5 million. Given the change in the business and its reduced size, we concluded that the business was no longer a strategic fit for Chemtrade. Accordingly, although we are sorry to no longer be working alongside our talented and professional colleagues in the International business and are sad to part with a business that was part of Chemtrade's IPO, we are pleased that it has found a good home with Mitsui. It's a good strategic fit for their business and we pass it along in good shape. As we noted in our financial statements, we will receive sales proceeds of about Euro 34 million, subject to adjustments, and the sale is expected to close in the second quarter this year.

We are now well positioned for 2017 and are focused, as always, on extracting value from our portfolio of assets.

Rohit will now provide you with some additional details on the fourth quarter and annual financial results.

Rohit Bhardwaj

Thank you, Mark and good morning everyone.

In general, for the fourth quarter, our SPPC and WSSC segments met the guidance we provided during the third quarter conference call.

Revenue from continuing operations for the fourth quarter of 2016 was $251.7 million, a decrease of $25.7 million from 2015. This decrease was primarily due to lower selling prices for sulphuric acid and sulphur in SPPC and lower volumes of some products in WSSC.

For the three months ended December 31, 2016, ignoring the acquisition related costs Mark mentioned, Distributable cash after maintenance capital expenditures from continuing operations was $19.7 million, or 28-cents per unit compared with $6.0 million or 9-cents per unit in 2015. As a reminder, we typically incur higher than run rate capex during the fourth quarter and this was the case in 2016 as well. Aggregate EBITDA from continuing operations for the fourth quarter of 2016, ignoring acquisition related costs was $40.1 million compared with $47.1 million in the fourth quarter of 2015. The decrease is mainly attributable to the cessation of production at the Augusta plant and the temporary reduction in production at our KCl plant. As usual, the fourth quarter had a high level of capex, although this was more than offset by large income tax recoveries during the quarter. These related to provisions established for previous acquisitions that were no longer required and therefore were released.

For the full year 2016, Distributable cash from continuing operations after maintenance capital expenditures and before the items Mark mentioned, i.e., the foreign exchange loss and the acquisition related costs, was $128.5 million, or $1.86 per unit, compared with $122.7 million, or $1.78 per unit in 2015. Consolidated revenue from continuing operations for 2016 was $1.1 billion, which was $60.2 million lower than 2015. The decrease was due primarily to lower selling prices for sulphuric acid and sulphur in SPPC and lower volumes of certain products in WSSC. Aggregate EBITDA from continuing operations for 2016 before the foreign exchange loss and the acquisition related costs was $209.2 million compared with $220.9 million in the previous year. Relative to 2015, the stronger U.S. dollar had a positive impact of approximately $5.8 million on EBITDA in 2016.

Turning to segmented results for the quarter, SPPC generated revenue of $141.9 million compared to $158.7 million in 2015. The main reason for the decreased revenue, year-over-year, was lower selling prices for sulphuric acid and sulphur. EBITDA for the quarter was $30.9 million, which was $2.3 million lower than 2015. As we discussed previously, we ceased production at our acid plant in Augusta, Georgia when our customer wound down its caprolactam operations in early November and this was the primary reason for the lower EBITDA. We incurred some costs in the fourth quarter to safely shut down and moth ball the plant in hope of repurposing this asset in the future. As mentioned previously, we have an agreement with this customer through 2021 which should provide us with some mitigation for the loss of this earnings stream.

Our WSSC segment reported fourth quarter revenue of $109.8 million compared with $118.8 million in 2015. EBITDA was $20.3 million compared with $27.4 million generated in 2015. Our alum business continues to gain strength although some of this performance was masked by operating issues at one of our large water treatment chemicals sites. We ensured that our customers remained supplied, but our cost to do so eroded some profitability. We also had lower production at our Midlothian, KCl site as we continued to implement the expansion plan.

Maintenance capital expenditures in the fourth quarter were $19.7 million, bringing our spending on maintenance capex for 2016 to $44.7 million. The heavier weighting of maintenance capex in the fourth quarter primarily reflected the five plant turnarounds mentioned in Q3. We expect maintenance capex in 2017 to be approximately $45 million. Non-maintenance, or growth, capex in the fourth quarter was $4.4 million, bringing our growth capex for 2016 to $11.6 million, which was the same as 2015.

Corporate costs during the fourth quarter of 2016 were $19.6 million, compared with $13.5 million in the fourth quarter of 2015. The primary reason for the difference was $8.5 million of acquisition costs related to the Canexus acquisition.

Finally, a couple of comments on our balance sheet. We strengthened our balance sheet during the third quarter by issuing $143.8 million of seven year 5% coupon unsecured convertible debentures and used the net proceeds to pay down long-term debt. At December, 2016 we had drawn down about US$334.1 million on our senior credit facility. From a senior debt-to-EBITDA ratio perspective that puts us at about 2.3 times. Our term loan is fully drawn but we maintain about US$581.5 million of undrawn capacity, which provides us with ample liquidity. The credit facility matures in October 2020. Of course all of this changes when we complete the Canexus acquisition and the new capital structure was outlined in our presentation dated October 4, 2016.

I'll now hand the call back to Mark.

Mark Davis

Thank you, Rohit.

For Chemtrade 2016 was an interesting year in our continuing evolution. We continued to pursue our strategy of adding size, scale and diversity of earnings where it benefits our stakeholders. This led to a review of our portfolio and the decision to sell our International segment as this particular business no longer adds a strategic benefit. On the other hand, our ability to invest in organic expansions in our water and KCl businesses is a clear strategic benefit to us and we will continue down this path.

Obviously this path leads to the significant increase in strategic size, scale and diversity that will result from our acquisition of Canexus. We were pleased to be able to reach a consensual agreement with the Canexus Board in December. The transaction will be completed through a Plan of Arrangement. As many of you know, Canexus shareholders and the court approved the Plan in February.   We have already raised approximately $400 million of equity that will be used to partially pay for the acquisition. At this point we are only waiting for the Canadian Competition Bureau to complete its review. The transaction has been previously cleared by the US FTC. We expect that the Canadian Competition

Bureau will also approve the transaction and are still on track to close the transaction this quarter as we had indicated in our December 15 release.

We are looking forward to concluding the Canexus transaction. The additional size, scale and diversity of earnings will position Chemtrade well for future continued success.

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

Operator (Joanna): Thank you. Ladies and gentlemen, we will now begin the question and answer session. Should you have a question, please press * followed by 1 on your touchtone phone. You will hear a 3 tone prompt acknowledging your request and your questions will be polled in the order received. If you are using a speakerphone, please lift the handset before pressing any keys. Your first question comes from Nelson Ng, RBC Capital Markets. Nelson, please go ahead

Nelson: Great, thanks. Good morning everyone.

Rohit: Good morning

Nelson: Mark, I just wanted to clarify. You mentioned that the international business would have generated $5.5 million of EBITDA in 2016 excluding restricting costs. I was just wondering what the run rate EBITDA would have been after losing the large customer in Q3?

Mark: It's hard to quantify for any given year. As we said, I think last call, it was going to be less than 10, so, the answer is somewhere between 5and 10 depending on the year.

Nelson: Ok, got it. And then in terms of the operating issues in the water facility and also at a lower operating rate at the KCl facility. Could you just break down the rough EBITDA impact from each item?

Rohit: If you look at our WSSC segment, it's down by about $7 million from last year. I'd say about roughly 2/3 of that was from the issue that the water facility and about 1/3 from the KCL facility. So, both of those things are now back on track in Q1 so we shouldn't see that linger on.

Nelson: So, it would probably partially impact Q1 to some degree

Rohit: There's a little bit of impact in Q1 yes, but not as pronounced as Q4.

Nelson: Ok, so for that KCL expansion – you said that was the phase 1 of 2 phases? Is that right?

Mark: Yeah and we were able to do some good in the fourth quarter and early this quarter. The plant should actually operate pretty well for the rest of this year and then we'll take another bigger kick at the expansion probably in the fourth quarter; might trip into 2018.

Nelson: Ok, so another reduced operation rate in Q4 this year or similar.

Mark: You know what, I think it's probably 2018. We could probably give you some more colour on that in our next call.

Rohit: That reduction may be more pronounced and we will definitely give some colour on that as we get closer.

Mark: I suspect it slips into 2018

Nelson: Ok, and just to clarify. You said that one large water facility was down but I thought you had 40+ water facilities

Mark: Let me give you a little more colour on that. All water facilities are not created equal. This one in particular has an effect that's actually material enough to notice because it's also where we made PACl and ACH; you know those are two products that we're expanding to higher margin products for us than Alum. The issues we had was with probably our largest PACl and ACH operating facility to date. So as Rohit had said in our comments, the Alum market has been pretty good for us this year. This particular water plant hurt us because we lost PACl and ACH volume that we had to cover from other sources.

Nelson: I see, and then I guess my next question – in terms of the Canexus acquisition on the regulatory approval side, I'm not sure what you're able to say but do you have to do any asset divestments to satisfy the regulator?

Nelson: I think all we're going to say on that is that the Bureau is doing its work. It has all the information that it needs from us and Canexus and we expect to be able to close this transaction before the end of the quarter and we expect the transaction to be approved by the Bureau. They'll do their work and make their decision.

Nelson: Alright, and then just my final question regarding Copper Cliff, has it moved to a single furnace yet or is that later this year? I just wanted to kind of get a sense of what the acid volume reduction is. I think sometime last year you mentioned that it could be around 20% or so.

Mark: So, they start making the move the second quarter of this year. So, they take one furnace; actually they had a big shut down second quarter of this year and they start re-plumbing life. This year I think the decreased volume; I can't remember the number, do you have the number?

Rohit: I think we're looking at about 100,000 to 150,000 tons and then by next year, they'll be running at their one-furnace rate so we should steady off in 2018.

Nelson: So, the run rate is 100 to 150 tons less?

Rohit: Yes

Nelson: Ok. Does that mean you're going to see a reduction from the sulphuric acid business in Q2 as they kind of transition from 2 to 1 furnace?

Rohit: So, we'll see a reduction in volume but actually 2016 is a good example where we got extra volume and that actually hurt our profitability. So, although we'll see some lower volume it is not clear as to what the impact if any, will be on the bottom line because you know the way this by product acid works is you don't make a lot of money on the last bit of volume. We said in the past that you don't expect this kind of volume reduction to have any significant impact on the bottom line.

Mark: Not to sell it short, our logistics and supply chain guys are going to be jumping through hoops to try and cover Vale's down and then back up again. But from a financial perspective we don't think it should be a material effect on our results.

Nelson: Ok. Alright, thanks for the clarification

Rohit: Thanks

Operator (**Joanna**): Thank you. Your next question comes from Steve Hansen from Raymond James. Steve, please go ahead

Steve: Good morning guys, a couple of follow ups for me. Maybe just on the Alum business and some of the better strength that you've been seeing in that business, can you just maybe give a little background and colour there as to what that means and whether it's sustainable. We've gone through a period of margin compression a year and some change ago so I'm trying to understand what's happening there.

Mark: Well, we went through margin compression in 2015. It started to stabilize at the end of '15 early '16 and in the latter half of '16, margins actually started expanding for us again. Two reasons – one is lower raw material cost but more importantly, pricing has stabilized and started turning the other way. So, the last 2 or 3 calls I don't think we've talked at all about margin compression, we've talked about the business stabilizing and I think last call we actually talked about business improving as pricing slowly starts to recover.

Steve: Ok, so it's a trend that we should…this ability is intact now and slight climb higher still possible from this point forward?

Mark: Yes

Steve: Ok, and then just on the organic PACl and ACH facilities – I recall the CAPEX being relatively modest but can you give us a sense of the contribution as well as those start to come online?

Mark: The CAPEX we've said is basically $10-15 million a year all in on our projects and we expect to make at least 20% return on that capital.

Steve: Ok, fair enough. And then just on the Augusta, Georgia facility, the wine down now place, any thoughts on the potential repurposing of that merchant product at all in the future or do we just sort of stalemate at this point?

Mark: No, we are cautiously optimistic we might be able to do something. It's premature to talk about it but although we've had to write off the plant for book purposes because at the time we didn't have a use, it's just conceivable we might find one. On the other hand, as we've said, we do have that contract that goes through to 2021 which provides us with some comfort, too. But there is a possibility to repurpose that plant, it's just premature to tell you what it is.

Rohit: Unlikely that it will go back to its full earnings stream but there's some hope of recovering part of it.

Steve: No, that's understood. And then just the last one on the Canexus deal – I know you can't say much about the actual process itself but at what point or what are you able to do at this juncture before the official approval is in place in terms of thinking about extracting the synergies. Do you put a team in place or you evaluate it more fully, are you able to talk to the other side to any degree just to sort of coordinate efforts as the transaction is approved or is just wait and see until the official transaction goes ahead?

Mark: We're able to do some high level planning administrative type functions. We're being very cautious and careful to abide by everyone's lawyers advice not to get involved in running the business or to actually understand any details on the ongoing business that the Bureau is investigating. Quite frankly, we see no reason to go anywhere close to that line. The Bureau will finish its work and then we'll go to work.

Steve: Ok, great. So any update on potential synergies is something that we'll hopefully be able to get later on the year as your process evolves.

Mark: You'll be the first person we tell, Steve.

Steve: Much appreciated. Oh, just one last one if I may, sorry. You've got down this organic path both in PACl and ACH and I guess KCL, have you thought about that process evolving any further in terms of more facilities or is it just the current facilities that we have under plan?

Mark: There's another two potential. Having said that, we need to vet the markets more before we actually make a decision. We're currently starting up one like, now, and there's another one under construction. Whether or not there's another one or two we have to re-evaluate the market once we're done with these.

Steve: Ok, great. That's it for me guys, thanks

Mark: Thanks Steve

Operator (Joanna): Thank you. Ladies and gentlemen as a reminder, should you have a question, please press * followed by 1. And your next question comes from Anoop Prihar from GMP Securities. Anoop, please go ahead

Anoop: Good morning, I just wanted clarification – the $45 million in CAPEX for fiscal '17, that's excluding any sort of contribution or any sort of allotment to Canexus, correct?

Rohit: That's just a standalone legacy business

Anoop: And I suppose at this point in time there's not much you can say in terms of what you may be spending on that side of the business?

Rohit: No, I think you can look at what Canexus has publicly said and I think they've talked about $25 million of maintenance CAPEX but we really don't have more insight than that at this stage.

Anoop: Ok, and then similarly on G&A on a pro-forma basis – just similar approach at this point?

Rohit: I think what we've said in the past was that in any public company we expect to get $10 million of cost synergies but again, we can't fine tune that anymore until the deal closes.

Anoop: Alright. Fair enough, thank you

Mark: Thanks

Operator (Joanna): Thank you. Your next question is from Trevor Johnson from National Bank. Trevor, please go ahead

Trevor: Hey, good morning gentlemen.

Mark: Hi Trevor

Trevor: Could you just remind us kind of the mechanics for the 2021 contract that's still in place for the mothballed Augusta facility? And also, did you see any impact or inflow from that relationship in the quarter?

Rohit: In terms of… there's no inflow and I think in terms of the mechanics from that contract, I think it's probably not one to get into that detail because we are in talks with them so, I don't think you want to get too far down that path on a conference call.

Trevor: Ok, that's alright. And then just a last one for me looking at the legacy business – curious if there's any other kind of non-core or other assets that you might be looking to ring-fence and then maybe streamline operations, kind of like what we do on the international side. Just wondering if there's anything above and beyond maybe the international segment that you could look to monetize to going forward?

Mark: We could but we're not looking at it nor inclined to. I mean, although we do have some plants in North America that make one product for us, operating businesses within North America are a lot easier for us just geographically and within reach and with the people we have than actually across the ocean. We like our portfolio, we like the diversity it provides for us and we're considering standing pat and growing as opposed to divesting.

Trevor: Got ya. And then something that you might revisit with Canexus entering the fold, that there might be an opportunity there to streamline, I'm guessing.

Mark: Sure, but we kind of like the portfolio of assets. I think they'll fit together pretty nicely for us.

Trevor: Good stuff, thanks guys

Mark & Rohit: Thank you

Operator (Joanna): Thank you. There are no further questions at this time, you may proceed

Mark: As usual, thank you all for your continued attention and we look forward to talking to you next quarter. Thank you

Operator (Joanna): Ladies and gentlemen this concludes today's conference call. We thank you for participating and we ask that you please disconnect your lines.