First Quarter 2016 Financial Results Transcript – May 4, 2015

Operator: Good morning ladies and gentlemen, and welcome to the Trinseo First Quarter 2016 Financial Results Conference Call. Turning to Slide 2, we welcome the Trinseo Management team, Chris Pappas, President & CEO, and David Stasse, Vice President of Treasury and Corporate Finance, who will be conducting the call. I will now hand the call over to David Stasse.

Dave Stasse: Thank you Tamara and Good Morning everyone. At this time, all participants are in a listen-only mode. Later, we will conduct a question and answer session, and instructions will follow at that time. If anyone should require operator assistance during the call, please press *, then zero, on your telephone.

The slide presentation for today's call has been posted on the Company's Investor Relations website, in the webcast viewer and with the financial results press release by means of a Form 8-K filing with the Securities and Exchange Commission. A replay of the conference call and transcript will be archived on the Company's Investor Relations website shortly following the conference call. The replay will be available until May 4, 2017.

Our disclosure rules and cautionary note on forward-looking statements are noted on slide 2. During this presentation, we may make certain forward-looking statements, including issuing guidance and describing our future expectations. We must caution you that actual results could differ materially from what is described or implied in these statements. Factors that could cause actual results to differ include, but are not limited to, factors set forth in our annual report on Form 10-K under the Item 1A, "Risk Factors".

I will now hand the call over to Chris Pappas.

Chris Pappas: Thank you, Dave. Good morning and thank you for joining us, I'll start on slide 3. Where I'd like to highlight the four key points you should take away from this call.

First, we had $153 million of Adjusted EBITDA excluding inventory revaluation in the first quarter which is a record quarterly result. This is well above the guidance of $125 to $135 million that we provided during the fourth quarter of 2015 call and these results are driven by higher than expected margins in our Basic Plastics & Feedstocks segment. We also achieved this without any fly-up styrene margin. We continue to see a higher and more sustainable, level of EBITDA and earnings due to structural improvements in the styrenics and polycarbonate markets.

Second, we had free cash flow of $63 million during the quarter. Traditionally we've had negative free cash flow in the first quarter due to a working capital build after the seasonally slower fourth quarter. However, due to strong EBITDA performance, first quarter free cash flow was positive in each of the last two years. In addition, we had our highest ever quarter-end cash and liquidity at the end of the first quarter, including the $57 million we spent to repurchase 1.6 million shares in the quarter.
Thirdly, our second quarter outlook is $140 to $150 million of Adjusted EBITDA excluding inventory revaluation. This result would be another very strong quarter and includes no fly-up styrene margin. We expect a slightly favorable inventory revaluation in the second quarter.

This guidance, combined with the first quarter's outcome, would result in Adjusted EBITDA excluding inventory revaluation, of about $300 million, in the first half of 2016.

Fourth and final point, we are increasing our full-year 2016 Adjusted EBITDA guidance to a range of $570 to $590 million. This assumes essentially no impact from inventory revaluation or from fly-up styrene margin. Please keep in mind that we have had fly-up styrene margin contribution in each of the last three years, so this continues to be upside to our forecast.

Now, please turn to slide 4 where I'd like to call out some highlights from the first quarter. I mentioned our strong financial performance for the quarter, which is further evidence of a sustainable, higher level of EBITDA for the company. Our Performance Materials division continues to be steady, delivering $77 million of Adjusted EBITDA excluding inventory revaluation in the quarter, which was within our guided range and puts us on track to deliver at least 5% EBITDA growth for full year 2016 versus 2015. The Basic Plastics & Feedstocks division exceeded our expectations due mainly to higher styrene margins, as restocking in Asia and the beginning of the Spring turnaround season in March contributed to a strong market.

In March Bain Capital, our parent, sold 10.6 million of our ordinary shares in a block trade at a price of $35.63, of which we purchased 1.6 million shares with cash on hand at the same price. In accordance with Luxembourg law, we made a tender offer to our public shareholders to purchase up to 1.1 million of their shares, also at the same price. That offer expired on April 25, and about 39 thousand shares were tendered for a total purchase price of approximately $1.4 million.

These transactions resulted in an additional 9 million shares in the public float, which now totals 20.5 million. Our public float now represents approximately 43% of our total shares outstanding. We are pleased that there is more liquidity for our shares in the market, and also that we were able to repurchase shares at what we believe to be a compelling value.

As we disclosed in our most recent proxy filed with the SEC, we will be seeking approval for two items at our annual general meeting on June 21st that I believe are meaningful to investors. First, under Luxembourg law, equity distributions are subject to a shareholder vote. We are seeking shareholder approval to authorize our board to declare equity distributions in the future. If this proposal is approved, our board plans to declare an annual equity distribution of $1.20, payable in quarterly installments.

Second, our existing shareholder authorization for share repurchases has approximately 2.1 million shares available. We are seeking a new share repurchase authorization, which would sunset the existing authorization, for 4.5 million shares to be utilized over the next two years under guidelines to be established by the Board. In the intervening period between now and the annual general meeting in June, our Board has authorized us to use up to $36 million for share repurchases.

These two items should be viewed as a sign of our confidence in the structural sustainability of the EBITDA and cash generation of Trinseo. At the midpoint of our 2016 EBITDA guidance and excluding changes in working capital, we expect to generate about $290 million of free cash flow in 2016. With $63 million of free cash flow in the first quarter, which is seasonally our lowest cash generating quarter, we are off to a good start.

Now, let's look at the details of the first quarter performance on slide 5.

First quarter Adjusted EBITDA of $143 million included an unfavorable inventory revaluation of $10 million. Excluding this, Adjusted EBITDA was $153 million. We also reported $1.62 of adjusted earnings per diluted share, which was inclusive of a 16 cent negative impact from inventory revaluation.

Now, turning to slide 6,
Latex volume for the quarter was 299 million pounds, in line with historical volume. We have implemented price increases in North America and cost reduction initiatives continue. To date, these cost reductions have achieved $5 million in annual savings, including the closure of the Gales Ferry, CT plant. We continue to pursue additional cost savings opportunities and evaluate our global footprint.

Let's turn to Slide 7,
Adjusted EBITDA in our Synthetic Rubber segment of $23 million was in line with our guidance, and included an unfavorable inventory revaluation impact.

We had record SSBR sales volume in the first quarter as the high-performance tire market remains very strong. Overall, our Rubber sales volume was lower as we were utilizing the Nickel-PBR and Neodymium-PBR swing train capacity for plant trials. In addition, we are conducting trials for our next generation SSBR products at key tire customers.

Now, turning to slide 8,
Performance Plastics Adjusted EBITDA for the quarter came in at $30 million, at the high end of our guidance. This performance was driven by higher margins as raw material costs decreased during the quarter. We estimate this benefit was about $5 million, which we don't expect to repeat in the second quarter.

On Slide 9,
Turning to Basic Plastics & Feedstocks had another strong quarter, including $33 million of equity income from Americas Styrenics. Margins improved versus prior year in each of styrene, styrenic polymers, and polycarbonate products. This is consistent with our thesis that supply/ demand dynamics in these markets are structurally improving, driving sustainable results. As operating rates continue to rise we would expect margins to improve as well. In addition, we were able to achieve this level of EBITDA in the absence of any fly-up styrene margins.

Now, let's turn to slide 10 for a discussion on cash and liquidity. Free cash flow for the quarter was $63 million, inclusive of $36 million in dividends from joint ventures, $26 million of capital expenditures, and $6 million of cash interest payments. At the end of the quarter we had record liquidity of $883 million, which included $438 million of cash, and reflects the $57 million used for the share repurchases mentioned earlier.

As expected, our net leverage continued to decrease due to higher EBITDA and cash generation, and was 1.5 times at the end of the quarter compared to 3.5 times at the end of the first quarter of 2015.

Now I'd like to discuss performance expectations for the second quarter. Please turn to slide 11 for a discussion on styrene monomer.

These are the same charts we've shown in the past, with Western Europe styrene margin data in the top chart, and Asia data in the bottom chart. You can see that March styrene margins increased from earlier in the quarter, as expected, due to the anticipated spring turnaround season.

Looking into the second quarter, we expect Europe styrene margin to increase from the first quarter as more supply will be offline, including, amongst others, a six week planned outage at our plant in Boehlen, Germany, styrene site. Asia margin is expected to decline as more local supply is expected to come back online in the second quarter. Overall, we expect a small sequential increase in profitability as the increase in Europe margin will be mostly offset by the decrease in Asia and lower production volume from our planned outage.

Inventory revaluation for the second quarter is expected to be slightly favorable as we expect increases in key feedstocks.

So with that backdrop for styrene margins and inventory revaluation, let's move to slide 12 to discuss our view of the second quarter of 2016.

We expect a sequential decrease of about $5 million for the Performance Materials Division in the second quarter driven by the first quarter price lag benefit in Performance Plastics, which we don't expect to repeat.

Latex Adjusted EBITDA is expected to be approximately $20 to $25 million as we continue to see the effects of the cost reductions as well as the price increases.

Synthetic Rubber is expected to be roughly flat to Q1 at about $25 million.

We believe Performance Plastics will be about $25 million - as we don't expect a repeat of the first quarter price lag benefit.

Now, moving to Basic Plastics & Feedstocks, we believe the second quarter will be between $90 and $100 million of Adjusted EBITDA excluding inventory revaluation. This is just slightly below the first quarter due to some planned outages in the segment which will increase maintenance costs and result in a net inventory draw. This guidance includes no contribution from fly-up styrene monomer margin.

Corporate expense should be about $22 million for the quarter.

Therefore, in total, we expect to have another strong quarter, delivering between $140 and $150 million of Adjusted EBITDA excluding inventory revaluation. This translates into an EPS range of $1.55 to $1.70 per share.

Let's look at Slide 13 for our guidance on the full year.

Based on our current view, we are raising our guidance for the full year to $570 to $590 million of Adjusted EBITDA. This assumes a minimal inventory revaluation impact in 2016. The driver of the increase is our strong performance in the first quarter as well as continued structural improvements to supply / demand dynamics which is resulting in higher sustained Basic Plastics & Feedstocks margins.

For Performance Materials, we are reaffirming 2016 growth in Adjusted EBITDA of at least 5%.

We also expect to continue to generate significant free cash flow. For modeling purposes, we continue to anticipate $75 million of cash interest, $65 million of cash taxes, and $150 million of capital spending in 2016.

Using the midpoint of our 2016 guidance of $580 million, this would yield about $290 million of free cash flow before working capital impacts.

To summarize, Slide 14 shows the build to the midpoint of our 2016 guidance, from 2015 Adjusted EBITDA excluding inventory revaluation. Overall we are guiding to about a $30 million year-over-year increase from 2015. Importantly, the 2016 guidance excludes benefit from fly-up styrene margin, which was $60 million in 2015. Therefore, on an equivalent excluding inventory revaluation and no fly-up styrene margin basis, we are guiding to a $90 million year-over-year increase in EBITDA. This is made up of about a $15 million increase in Performance Materials EBITDA, with the balance driven by higher structural margins in Basic Plastics & Feedstocks, mainly from styrene. At $570 to $590 million of Adjusted EBITDA, we expect Adjusted EPS of $6.40 to $6.70 per share.

We've had a strong start to the year and look forward to continuing to build on this momentum into the second quarter and beyond.

And now, Tamara, you may open the phone line for questions.

Operator: Thank you. Ladies and Gentlemen, if you'd like to ask a question at this time, please press Star and then One on your touch-tone telephone. If your question has been answered or you wish to remove yourself from the queue, please press the pound key.

Our first question comes from the line of Frank Mitsch of Wells Fargo Securities. Your line is now open.

Frank Mitsch: Good morning gentlemen, and a hell of a start to your year, Chris.

Chris Pappas: Thank you Frank. How are you doing?

Frank Mitsch: I'm doing fine; I'm doing fine, thank you. Hey, I wanted to drill a little bit more into the styrene business. Typically you do see a seasonal pick-up in Q2. You mentioned that you're going to have the turn-around in Boehlen. About how much negative impact do you anticipate from that turn around?

Chris Pappas: About six million, Frank, from our turn around, and that's baked into our guidance for the quarter.

Frank Mitsch: Alright, terrific; and then Chris what's your read of styrene monomer operating rates as you tour the world. Where do we sit now exiting Q1 and what would your expectations be there?

Chris Pappas: Well globally Frank, as you know, they're continuing to rise, and we think they'll continue to rise with limited capacity and some growth. At the moment we would peg them globally at about 86

percent with North America being higher than that, Europe being at about that level, and Asia being lower than that level, so well in the range of where we believe we have good operating rates and good margins, but still a ways to go, and with continued growth in demand, which we expect as we said at about 2 to 2.2 percent and very limited capacity coming, we expect the complex to do quite well over the next several years.

Frank Mitsch: Terrific and then lastly you raised an interesting point about increasing the stock liquidity with Bain peeling out. Any thoughts in terms of the pace that they may be looking to monetize what has been a very successful investment?

Chris Pappas: Well, obviously that's clearly Bain's decision Frank, and you know how the company feels about the shares. We've put the proxy in place that allows us to do certain things around equity distributions and share repurchases, and of course we've already participated in a share repurchase, so we believe the shares are undervalued at this point. Bain will have to make their own decision about valuation, timing, and so on, and that will be their call when the time is right.

Frank Mitsch: Alright, thank you so much.

Operator: Thank you. Our next question comes from the line of Hassan Ahmed with Alembic Global. Your line is open.

Hasan Ahmed: Good morning Chris.

Chris Pappas: Hi Hassan, how are you doing?

Hassan Ahmed: Good, thank you. One of the questions that I keep getting, obviously Styrene margins have improved dramatically over the last several quarters, and I guess for folks who have covered the industry for a while everyone's kind of rubbing their eyes sort of thinking about the sustainability of these margins. And one of the questions I keep getting is alright if these margins are indeed sustainable, why hasn't there been a supply response thus far, or is a supply response imminent? So how would you think about that question?

Chris Pappas: Great question. A couple of things; first of all, I think we all know the history of the styrenics business in terms of its long difficult period in the last twelve or so years. We've done some pretty good analysis of the economics of investing in styrene, as you might imagine. It turns out that from our point of view, over the last thirty months, even though we've had these relatively decent and I should say increasing margins in styrene, only one or two months of those last 30 in Europe have had margins that would be high enough to support an investment in a new facility. And if you look at the US where they've had even stronger styrene margins, over that same period of 30 months, we believe that only 7 or 8 months in that period have been high enough to justify new investment.

I think when you put together the historical backdrop, the actual facts about investment economics, not just improved margins but investment economics. And if you finally add to that the structural dynamic of who actually is integrated for example to ethylene and benzene anymore in terms of styrene players I think you'll conclude as we do that the likelihood of building remains very low. Furthermore we of

course know the announced building over the next three or four years and that of course is baked into our expectation. So I just don't see it for all of those reasons I mentioned Hassan, I just don't see it.

Now we have been very explicit as a company. We are not building styrene monomer, we are not building polystyrene we are not building polycarbonate, and the joint venture America Styrenics, of which we own fifty percent, will not build polystyrene, will not build styrene. So we have been explicit in our plans, but those are some of the economics and other factors involved.

Hassan Ahmed: Very fair question, very fair. And as a follow-up, obviously you guys just announced that you guys are taking this to the Board, the implementation of a dividend as well as a shared buy-back program. Just strategically as you think longer term and the like, how are you thinking about the cash outlay? Or asked differently, are you thinking of a recurring sort of buy-back program where every couple of years you would buy back X percent of the shares outstanding?

Chris Pappas: Well, we've made our first statement about use of cash with regard to return to shareholders, Hassan. It's in the form of the proxy that, of course, those items have to be approved at the annual general meeting, and those include the $1.20 distribution per year, quarterly installments, and the 4.5 million authorization over two years. We haven't obviously thought beyond that period. We'll take it as it comes.

We have stated many times that our investment of free cash flow will be in growing our performance materials business. It will not be to grow our basic plastics business. Our opportunities there would only be in consolidation. So we're going to take it the way we have the entire time we've been running this company. We're going to manage ourselves in a very thoughtful, methodical, timely way. We're going to shepherd our cash, watch our balance sheet, do the right thing for our shareholders, which we think the proxy agenda addresses. And that's the way we're going to continue to run the company, Hassan, because we think it's been successful and we think our shareholders have been rewarded and will continue to be under that kind of guidance.

Hassan Ahmed: Super. Thanks so much, Chris.

Operator: Thank you. And our next question comes from the line of Lawrence Alexander with Jefferies. Your line is now open.

Jeff Schnell: Hi, this is Jeff Schnell on for Lawrence. As we just talked about the new dividend and buy-back announcement appears to account for a large part of your free cash flow over the next few years, but is that because you don't like the multiples for M&A or is there a scarcity of available assets that you're looking at?

Chris Pappas: Well, first of all Jeff, the math on the $1.20 and the potential share buy-backs would not account for most of our expected free cash flow over that period. It would account for some reasonable portion of it, but our expectations based on EBITDA guidance we've given for certainly this year, and any expectations we have for next year, would still give us substantial free cash flow beyond those activities, number one.

Number two, we have stated our M&A appetite is relatively limited. It's limited to both on acquisitions in the performance materials arena, because that's where we think we can add the most value to the company in terms of shareholder value. And we continue to look at that but, you're correct, the multiples are high, and transactions therefore are not easy, and we have no immediate plans to be engaged in the M&A arena.

Jeff Schnell: Thank you. And if you look at the market structure respective of latex can you talk about how you think margins might evolve over the next couple years?

Chris Pappas: Well, I think the thing to look at is of course operating rate, and with the recent announced various closures in the latex business, particularly in North America, the operating rates now have moved comfortably into the high 80's. That has allowed, at least for the time being, these price increases to go through. We continue to look at cutting costs in our global footprint, and we believe that the structural dynamics at the current time in latex are constructive, and we'll have to see how they develop over time. But we continue to look at our footprint and other activities in the latex arena that would continue to improve the operating rate and therefore the potential margin.

Jeff Schnell: Great, thank you.

Operator: Thank you. And our next question comes from the line of Jermaine Brown with Deutsche Bank. Your line is now open.

Jermaine Brown: Hi. Good morning gentlemen.

Chris Pappas and David Stasse: Hi. How are you?

Jermaine Brown: Chris, looking at your guidance bridge for 2016 you've raised your expectation for EBITDA improvement within basic plastics and feedstock from ten million to seventy-five million. Can you provide some color on what the drivers are within that segment, and what changed between last quarter and this quarter?

Chris Pappas: Yes, if you go to the last page of our deck, page 14 is the page we're looking at. Largely the $75 million is some polycarbonate, some polystyrene and ABS, but generally speaking it's a view we have that the styrene margins are going to continue to be strong and that's driving substantially all of that change. Now, over the last quarter we've had more data, we've had more information that suggests that the styrene market is in fact showing signs of sustainability, structural improvement, and that's the basis for that uptick in guidance. We've held steady on performance materials at least 5 percent EBITDA growth, that's the 15, and the balance as you point out is BP&F, largely styrene driven.

Jermaine Brown: Understood. And remaining within BP&F your volumes came down four percent. Can you provide some color on what caused that and how should we think about volume trends going forward?

Chris Pappas: Yes, there's really nothing in those volume trends that should be looked at as other than,

for example, Q1 restocking in the previous year which drove some higher volumes relative to the first quarter this year. There's no dynamic in the market that suggests to us that there's any volume decline of substance. In fact, I think a topical question that we get is Asia, and China specifically.

Last couple weeks we had our folks in China for the Chinaplas Show which is one of the largest trade shows in the world and we had multiple people there talking to many, many customers. Frankly, as I said on the call last time, and we were ahead of everybody by the way I'll remind you on China, with our view that China was not collapsing. We continue to have that view having just spent time there last week with many, many customers. Is China slowing down? Yes, I've been saying that for eighteen months. But if you look at our last six quarters of results including the guidance for Q2, in a slowing China environment, this company has averaged over $140 million of EBITDA over the last six quarters. Now I'm including Q2 guidance in that at the midpoint. But we do not see volume changes in our business of substance going forward.

Jermaine Brown: Understood. And finally, SSBR; what will it take for the industry to invest in capacity expansions?

Chris Pappas: Well, there have been some investments in SSBR, and we continue to look at ways to grow our capability in SSBR, because we were sold out. And we continue to look at ways to grow our high performance rubber business. That's what our neodymium investment is about. So, there have been some investments in SSBR, but not all of those investments are able to make the kind of product that the tire companies really need for the higher and higher performance of these high performance tires, and that's why we have continued to put dollars in the technology investment in SSBR, so that we can continue to be at the forefront of products that are required by our key customers to make these high performance tires. And we have steadily grown our SSBR percentage of our total rubber business, and the enhanced SSBR portion of our total rubber business. So, there are some capacities coming, but we remain sold out, we remain very proud of our performance and margin. And we're looking for ways to grow that business in SSBR and other high performance tire rubbers like neodymium.

Operator: Thank you. And our next question comes from line of Bob Koort with Goldman Sachs. Your line is now open.

Ryan Berney: Good morning. This is Ryan Berney on for Bob.

Chris Pappas: Hi Ryan.

Ryan Berney: Hey, Chris. I was hoping you could – you could help me out a little bit here. It seems like, it's very clear from your full-year guide for Basic Plastics, you're passing through the first quarter number and you've given very clear guidance on second quarter, but it seems like you're implying that will stay very strong here in the back half as well as you kind of commented earlier in the call. So, I'm wondering is there any other planned industry outages that are going to keep that market tight in Europe or how do I think about the impact of Shell Moerdijk also coming back up over the last couple weeks?

Chris Pappas: Well, first of all, Shell has been up for a long time; quite a while. And in the mind of the market in terms of putting product in the market, it's that activity started really in the fourth quarter. So

that's been in the market for a while, Shell Moerdijk, number one. Number two, we are looking at really just the normal level of planned outages through the balance of the year that continues to support the kind of styrene margins we've had through the first and second quarter, and that's essentially what we have in our guidance. We don't have anything other than that in the guidance. The styrene monomer complex has proven resilient, as we've been saying it would be. We've been saying this for two years. It's moving up slightly in operating rate. There is limited capacity coming and on that basis we make our guidance.

Ryan Berney: Great, that's helpful. And then maybe secondarily, you had a question earlier on kind of new capacity and you mentioned basically the margins not being high enough in Europe and North America sustainably to clear maybe a hurdle rate for new investment. What do you think that industry hurdle rate is even if you don't anticipate investing in it yourself?

Chris Pappas: You mean in terms of say an internal rate of return or peak margin or what do you – or margin or what do you mean, margin or either ones...

Ryan Berney: Either one, yes.

Chris Pappas: Well, first of all, we've been very clear about what we're going to do and what AmSty's going to do or not going to do. Look, I don't want to speak for other companies on what hurdle rate they might have, but you'd sure hope that people would have to have high teen percent internal rate of returns to make investments of this magnitude. These are very large investments with forward looks. In other words, you have to be convinced that when the asset starts up, and as of now that would be 2019 at best, that you have to have a very strong view of the margins in that period as sustainable in order to make that investment and you have to go get the money in an environment where you don't have those margins today and the history is not very good. And so, it just doesn't look very probable to us is the short answer, Ryan.

Ryan Berney: Great, thanks again, Chris.

Operator: Thank you. And our next question comes from the line of P.J. Juvekar with Citi. Your line is now open.

Eric Petrie: Hi, good morning. This is Eric Petrie on for P.J.

Chris Pappas: Hi Eric.

Eric Petrie: Chris, what is your styrene margin embedded in your 2016 forecast for BP&F? It looks like first half, the second half EBITDA, excluding inventory revaluation, will decline by 30 or 35 million dollars. Is that margin hit or is that seasonality? I'm just looking for a little more color.

Chris Pappas: Yes, we put the guidance together, Eric, with some view to seasonality in the back half of this year driving that construct, not per se any step down in margin, but really more of a seasonality effect as we move into the fourth quarter.

Eric Petrie: Okay. Your synthetic rubber prices declined 9% year-over-year. Was that mostly driven by your commodity grades, or are you offsetting pricing pressure in your specialty and enhanced SSBR grade?

Chris Pappas: Yes. Well, first of all, we run the rubber business, as you know, on a contracted margin basis, so that's the first thing. And the prices can move with raw materials, obviously, the price of the material. But I think to the question about say, price and margin in general, yes the commodity grades of ESBR have been relatively weak over the past period. We think that could change. It looks like the arbitrage for butadiene and butadiene related rubber out of Europe to Asia is now open, in fact it is open. We're seeing some constructive signs of rubber prices in Asia including natural rubber.
So, we're starting to see the signs of maybe some improvement in the ESBR business either through arbitrage or general lift, and that would probably help us going forward if it materializes, Eric. But I would be cautious about looking at the revenue and price line. I'd be more conscious about looking at the margin line for the business. And margins in the commodities have been compressed over time in the commodity side of our business. That's why we keep saying for five years now, we don't want to be in the broad rubber business. We want to be in high performance rubber for high performance tires and that's why we put all our money there. capital, research, et cetera.

Eric Petrie: Okay, last Pirelli announced they're building a second tire plant in Mexico with capacity of 2.5 million tire capacity. Will you see any incremental demand from that? Just talk about opportunities for rubber volumes.

Chris Pappas: Sure, yes, we will. Now look, it's a construct again for us in synthetic rubber, high performance tires, that's our focus. That business is still growing at about three times the regular tire market. And almost all tire producers, Pirelli being one, Continental being another, Good Year, Hankook, others, generally are expanding capacity, and it's almost always in relationship to that dynamic. In other words they're trying to build capacity to satisfy this high growth market called performance tires, driven by all the dynamics we've talked about many times. So, yes, as those assets go in, whether it's Mexico or wherever it is, and as those assets are designed, which they generally are, to participate in this high growth market, then of course for us and other producers, there will be more demand for SSBR. That's how we get the high growth rate.

Now, I mentioned earlier, we're essentially sold out. So, we're looking at our neodymium trends, our conversion as a source of growth in our rubber business. And we're looking at other ways to get assets into the ground. We talked about this in Asia for example, in SSBR in order to continue to grow our business. But your point is they're growing the tire market in that arena and it's going to grow the demand for SSBR.

Operator: Thank you. And our next question comes from the line of Vincent Andrews with Morgan Stanley. Your line is now open.

Matt Andrejkovics: Hi, good morning. This is actually Matt Andrejkovics calling in for Vincent.

Chris Pappas: Hi Matt.

Matt Andrejkovics: Hey, how are you?

Chris Pappas: Good.

Matt Andrejkovics: In the performance tire business, with your production primarily in Europe, are the sales that you export to Asia sold to customers in Europe and then exported to Asia, or are those actually sold to Asian customers?

Chris Pappas: In some of both, so we do both, and we do both into the Americas as well.

Matt Andrejkovics: Got it. And just on the development of that market, is it primarily, performance tires, is it primarily through OEMs at this point or has it started expanding further into the replacement market, or is it, are you seeing just due to regulations that the OEMs are putting it on cars that are new and then maybe through the leasing cycle and the replacement cycle you'll get the – there's still a lot more to do to come in terms of the growth for the replacement demand.

Chris Pappas: It depends on the region of course. Now, this isn't a new dynamic. This has been going on for several years. We recognized this early. That's why we built the new rubber train we built in SSBR right at the beginning of the company. In late 2010 we announced the plans to build that plant. We brought it up in 2012. We sold it out immediately. But it depends on the region. So if you look at Europe, for example, the OEM penetration is very, very high, as you would expect. That's where the regulatory push, if you will started for high performance tires, driven around better gas mileage, better rolling resistance, good wet grip, and overall better environmental drivers for the car companies and the tire companies. So Europe, quite high penetration on OEM, replacement market's a driver in Europe. You could contrast that generally to the Asian markets, where OEM penetration is still pretty low. And so in that case you have OEM growth on top of eventual replacement tire growth. So it depends on the region, but we're partway through the transition, in some regions we're heavily into replacement and others we're into both. Remember. OEM tire demand is about 25%, replacement is 75%, Matt. So that's the general global dynamic, okay.

Matt Andrejkovics: Great, thanks. And then...

Chris Pappas: Lots of growth left is the short answer, three times the rate of regular tire, so in the range of 10% growth year-over-year in high performing tires.

Matt Andrejkovics: And then just what do you assess would be your capital needs to meet the growth in this business given your position today. I know that you continue to assess it, but, how do you see the CapEx levels trending as you look to take it in...

Chris Pappas: Our CapEx profile that we've guided to is $150 million this year. We've guided to $125 million next year. We have not talked about 2018 and beyond. We have talked about a significant investment this year, $55 million, and next year about $35 million in IT related investments, new SAP system, new operating hardware and software in our plants. Those capital investments will be falling off as we move into 2018. And it's in that timeframe that we may or may not be ready to take an investment forward say in the rubber business, which is what you're asking for a bit or asking about. So we have not declared an investment in rubber. The last one we made was in 2010 into 2011. It was $130 million, Matt, was the capital investment over about an 18 to 20 month build period. So that's the scale

of an asset investment in rubber in our case, in our company at least on the last one we built, okay? And that is not happening in 2016 or 2017 obviously, or we would have announced it.

Operator: Thank you. And ladies and gentlemen, that does concludes today's question-and-answer session. Thank you all for attending today's conference. You all have a great day.