FMC Corporation

Fourth Quarter 2017 Earnings Call Script

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4Q17 Conference Call

Introduction – Michael Wherley

Thank you and good morning everyone. Welcome to FMC Corporation's fourth quarter earnings call. Joining me today are Pierre Brondeau, President, Chief Executive Officer and Chairman and Paul Graves, Executive Vice President and Chief Financial Officer. Pierre will review FMC's fourth quarter performance and provide the outlook for 2018 and the first quarter. Paul will provide an overview of select financial results.

The slide presentation that accompanies our results, along with our earnings release and 2018 Outlook Statement are available on our website and the prepared remarks from today's discussion will be made available after the call.

Mark Douglas, President, FMC Agricultural Solutions, and Tom Schneberger, Vice President and Global Business Director, FMC Lithium, will then join to address questions.

Before we begin, let me remind you that today's discussion will include forward-looking statements that are subject to various risks and uncertainties concerning specific factors, including but not limited to those factors identified in our release and in our filings with the Securities and Exchange Commission. Information presented represents our best judgment based on today's information. Actual results may vary based upon these risks and uncertainties.

Today's discussion will focus on adjusted earnings for all income statement and EPS references. A reconciliation and definition of these terms, as well as other non-GAAP financial terms to which we may refer during today's conference call, are provided on our website.

With that, I will now turn the call over to Pierre.

Business Review – Pierre Brondeau

Thank you, Michael, and good morning everyone.

Before outlining our fourth quarter results, I wanted to first state that 2017 was a pivotal year for FMC, and we are excited about the opportunities ahead of us in 2018. The integration of the acquired DuPont ag business is progressing very well, as is the process of separating the Lithium business into a public company. As we prepare for a listing in the second half of this year, we will continue to expand both our lithium hydroxide and our lithium carbonate capacity to capitalize on the significant demand expected in the coming decade.

4Q 2017 Reported Results

Turning to slide 3. FMC reported fourth quarter revenue of $980 million, which was up 42 percent year-over-year.

Adjusted EPS was $1.10 in the quarter, an increase of 67 percent versus the same period a year ago. Adjusted EPS was 2 cents above the top end of our guidance, driven by strong operating results in each of our two segments.

We are very pleased with our fourth quarter results. In Ag Solutions, our business performed very well, and earnings came in above the high end of our guidance range. The integration of the acquisition into FMC is meeting all our expectations. In Lithium, we delivered our first full quarter of commercial production at our new lithium hydroxide facilities in China and finalized an important agreement with the Argentinian government, paving the way for expansion in that country and for the separation of our Lithium business into a standalone company.

Moving on to slide 4 and Ag Solutions. Revenue grew 40 percent year-over-year. Performance of FMC's legacy Agricultural Solutions business was very strong, growing 9 percent year-over-year, driven by double-digit revenue growth in North America, Asia and Europe. Acquisition revenue of $193 million accounted for the remainder of the growth. We do not have comparable results for the acquired business for the last two months of 2016. However, it performed well and as expected.

Fourth quarter segment earnings of $189 million increased 48 percent year-over-year.

Segment revenue for 2017 was approximately $2.5 billion, an 11 percent increase compared to the prior year. Full-year segment earnings were $486 million, a 21 percent increase year-over-year, and segment earnings margin improved 160 basis points to 19.2 percent. Our legacy Ag business posted 3 percent revenue growth and strong earnings growth in the year.

On slide 5, we outline the regional performance in the quarter.

In North America, we posted a 38 percent revenue increase. Our legacy FMC business grew 14 percent.

The performance was driven by early demand for pre-emergent herbicides, as farmers plan for expanded soybean acreage this year, and strong demand for our SU herbicides for cereals.

In Latin America, revenue increased 21 percent in the quarter. Our legacy FMC business grew 3 percent in Q4 and 9 percent for the entire year. In Brazil, FMC's legacy business grew 15 percent on a full-year basis – a very strong performance in a market that contracted approximately 10 percent.

In Asia, revenue increased 84 percent in Q4. Our legacy FMC business grew 14 percent, driven by successful product launches and strong growth in our plant health product portfolio. We also saw strong sales of Rynaxypyr® insect control, especially into rice markets in India and Indonesia.

And finally, in Europe, revenue increased 59 percent in Q4. Our legacy FMC business grew 13 percent with strong sales in Eastern Europe and in France, where you may recall we have moved to direct market access.

Lithium

Moving now to Lithium on slide 6. Lithium delivered another exceptional quarter. Revenue of $113 million increased 60 percent year-over-year, and segment earnings more than doubled to $44 million. Significantly higher prices – and a shift in mix to higher value products – drove the increase in segment earnings margin to 39 percent, versus 30 percent in the prior-year period.

We took an important step in December, when we finalized new operating agreements in Argentina. The provincial government of Catamarca formalized these agreements by passing legislation that sets our royalty rates and our commitments to corporate social responsibility programs, while also paving the way for us to expand capacity and move toward the intended separation of our lithium business later this year. We want to highlight the revised royalties and CSR programs are at the levels generally consistent with our prior commitments. Combined, they amount to a mid-single digit percentage of sales out of our Argentina operations.

2018 Outlook

Turning to Slide 7, which summarizes our outlook for the first quarter and the full year. We expect adjusted earnings per share for full-year 2018 to be between $5.20 and $5.60 per share, which represents, at the mid-point of the range, a near doubling of EPS year-over-year. First quarter 2018 adjusted EPS is expected to be between $1.45 and $1.59.

We expect 2018 Ag Solutions revenue will be in the range of $3.95 and $4.15 billion and segment EBITDA will be in a range of $1.05 and $1.15 billion. We anticipate legacy Ag Solutions revenue will grow 2 to 4 percent, while the acquired business is expected to grow by 6 to 10 percent. First quarter segment revenue is expected to be in the range of $1.0 to $1.07 billion, and EBITDA is forecasted to be in the range of $290 to $320 million.

The Lithium business is well positioned to deliver another year of significant earnings growth in 2018. We expect full-year revenue for Lithium to be in a range of $420 to $460 million, a year-over-year increase of 27 percent at the mid-point. Full year EBITDA is expected to be in a range of $180 to $200 million, which represents an increase of 34 percent at the mid-point. We expect price/mix and incremental volumes to each contribute approximately half of the increase in earnings. The volume increase is largely due to the 4,000 tons of incremental capacity coming online from debottlenecking projects. We expect first quarter segment revenue to be in the range of $95 to $110 million, and EBITDA is forecasted to be between $44 and $48 million, which represents a year-over-year increase of 78 percent at the mid-point.

Moving now to slide 8, and the key drivers for the Ag Solutions business in 2018. Starting with the overall ag chem market, where our expectations for 2018 remain unchanged from what we saw in November. We continue to expect the global crop protection chemical market – on a U.S. dollar basis – to be flat to up low-single digits in 2018.

We expect the market in Asia Pacific will grow the fastest, increasing by a low-to mid-single digit percent range, driven by India and Southeast Asia.

We expect the market in Latin America will increase in the low-single digits. Brazil will be a bit ahead of that pace, benefitting from increased acreage for nearly all crops. The market in Argentina should see continued expansion in soybean applications, and in Mexico we expect growth in niche crops.

In North America, we expect the market will be flat to up low-single digits, as farm incomes remain below trend.

Growth will come from post-emergent herbicides and a modest increase in soybean acreage, in general.

We expect the market in EMEA will be flat to up low-single digits. Improved weather and growth in Eastern Europe could provide upside to this forecast.

Turning now to our forecast for how FMC will perform in 2018, considering the market conditions just outlined. We expect revenue for our legacy Ag Solutions business will grow 2 to 4 percent, driven by several factors. In Brazil, we expect to see a continuation of the positive trends in cotton and sugarcane markets, where we are well positioned, as well as increased demand in the soybean market. In Asia, we anticipate higher demand for our products going to rice, fruits & vegetables, as well as cotton. In Europe, the move to direct market access in France, new products for oil seed rape and price increases, will all drive growth for FMC in 2018.

Moving on to our acquired business, which we expect will grow 6 to 10 percent in 2018 on a full-year basis, well ahead of the market. This will be driven primarily by increased insecticide revenue. We believe Cyazypyr® insect control is far from its peak in annual sales. In 2018, volumes are expected to grow for cotton and soybean applications in Brazil. New product registrations in EMEA will also drive growth. Rynaxypyr® insect control will continue to expand into new crops and geographies – such as rice and sugarcane in India – and further penetrate into Southeast Asia. Finally, we also expect to increase sales of our acquired SU herbicides with new formulations in North America for cereal applications.

As I said earlier, the integration process is progressing very well after almost 4 months of ownership. Our 2018 guidance reflects what we believe will be the maximum operating costs, as a percentage of revenue, for our combined Ag Solutions business. Our assumptions for gross margin, R&D expenses and SG&A expenses are not meaningfully different than what we have shared with you on calls last year. But as the DuPont transition service agreements roll off, and as we implement a new SAP system in 2019, we will see further cost savings and improvement in EBITDA margins.

Turning to slide 9, and starting with our views on the Lithium market. In summary, we expect global demand for lithium, on an LCE basis, to grow from about 200,000 metric tons in 2017 to 335,000 metric tons by 2020 and to one million metric tons by 2025. This is an average annual growth rate of over 20 percent. On the supply side, despite recent news out of Chile, we believe that supply from high-cost spodumene producers will continue to be needed to meet end-market demand in every year through at least 2025. We expect this will create a price floor for lithium carbonate of low double-digit dollars per kilogram for at least the next 7 years.

FMC is very well positioned to take advantage of these market conditions. Our business is focused on lithium hydroxide, and we have demonstrated that our approach to expanding our hydroxide capacity is more than capable of meeting the growth in demand, with relatively low capital needs. Our low-cost carbonate production resources in Argentina are capable of expansion to at least three times our current capacity, and we have secured the necessary agreements with the local and national governments to allow us to pursue an expansion of this scale.

In 2018, prices will be higher than in 2017, across all our product categories. The majority of our 2018 forecast revenue falls under multi-year contracts that have defined pricing already in place. We expect this trend of customers looking for longer-term supply commitments to continue – especially in hydroxide – reflecting customers' general view that supply will remain tight into the foreseeable future.

In 2018, FMC will produce more lithium hydroxide, as well as more base LCE's, than in 2017. FMC was the only producer to add significant hydroxide capacity in 2017, when we expanded our production capacity from 10,000 tons to 19,000 tons. We will realize significant growth in 2018 as we run our China plant for the full year. Our next phase of hydroxide expansion should see us commissioning at least one additional 4,000-ton unit by the end of this year.

In Argentina, we expect to produce about 21,000 LCE's in 2018 – up from 18,500 tons last year – as we realize higher volumes due to the debottlenecking projects at our plant. The completion of these projects will lead to an incremental increase in LCEs produced as the year progresses.

The subsequent expansion project in Argentina will add around 10,000 tons of lithium carbonate capacity by the end of 2020 and a further 10,000-ton increase by 2022. These first two increments are expected to require total capital spending of around $250 to $300 million, as we have previously stated. We are currently exploring adding a third carbonate expansion phase, providing a further 20,000 tons of capacity by 2025 at the latest.

Moving onto market demand. We believe that today too much of investor focus is on supply and not enough on demand. In particular, we believe the investment community as a whole has yet to absorb the impact that the growth in demand for electric vehicles in the coming years will have on the lithium industry. Simply adding mining or extraction capacity will not be enough, without a corresponding increase in manufacturing capacity for battery-grade lithium products that are in a form that the customers can use. Equally, producing technical grade carbonate that needs to be further processed to remove impurities will simply add to the cost of that product. And as we move to nickel-rich cathodes in high-performance batteries, hydroxide will become a requirement in the production process, not just a preferred option.

Our view of the demand outlook is summarized on slide 10. Clearly the source of growth for lithium demand is the rapid penetration of pure EVs into the global auto market. We model the growth of EVs at the individual vehicle level, based on public announcements as well as our own direct interactions with auto manufacturers and their suppliers. The chart on the left shows the growth of pure electric vehicles, and a few things stand out. First, we expect pure EV penetration to reach 2.5 percent by 2020 and 12 percent by 2025. The source of this growth is multiple launches by over 30 manufacturers – this is not dependent on any one manufacturer. And it shows the importance of China, as this country maintains its position as the largest single market for electric vehicles.

Of course, this growth in EVs needs to be converted into a demand forecast for lithium. The right hand side of the chart shows how important the EVs will be to the market as a whole, by 2025. And equally important, you can see that the nature of the growth in demand is such that there will be heavy shift towards lithium hydroxide. We reach these conclusions through a vehicle by vehicle assessment of the battery technology and size which we expect to be used in each announced vehicle, as well as through discussions with our customers and end users. In fact, many of our customers and the ultimate end users of lithium are coming to FMC today looking for multi-year contracts that commence in 2019 or 2020, demonstrating their confidence in the demand growth shown here.

Ultimately, it is this detailed analysis of future demand that gives us the confidence to pursue our strategy in Lithium.

Now let me move onto the supply side of the equation. This is another area that we believe the market as a whole is not correctly assessing. We have seen repeated examples of new entrants making large claims about intended capacity additions that are ultimately proven to be far too ambitious. Even a simple review will show that almost without fail, the capital costs increase significantly and the start-up dates are pushed further and further back. Once projects have been brought online, we have seen production rates that fall far short of nameplate capacity, product quality that is inconsistent, and operating costs per unit of production that are far higher than what was originally projected. While it is possible today to construct a cost curve using announced projects that suggests a risk of oversupply in the near future, all available evidence suggests that this is highly unlikely to occur.

The supply curves are well known to you all, and the current status, shown on the left side of slide 11, is reasonably well understood and accepted. It is clear the incremental ton of supply is coming from high-cost spodumene, which is being shipped to convertors in China. We have marked a range for the market price, based on data published by others. The prices publicized by our competitors as their realized price, plus those quoted by independent market observers such as Benchmark Minerals, indicate a price range of between $11 and $14 for carbonate in most markets today.

On the right side of slide 11, is the cost curve we expect in 2020, taking into account all the expansions that have been made public. I would point out a few key items on here. First, you can see that at today's price range for carbonate, the higher royalties payable in Chile mean that there is no meaningful cost difference between carbonate produced in Argentina and in Chile. Second, the marginal producer of carbonate remains a high-cost spodumene source, and would likely remain so even if demand fell by around 10 percent from our forecasts. There is simply not enough brine capacity capable of being added by 2020 to change this. When you overlay the price range from today out to 2020, you end up with a chart that looks remarkably similar to the situation we saw in 2017.

We acknowledge that there are many differing opinions about supply and demand growth over the coming decade, and that this analysis could see positive and negative surprises. However, we remain of the view that the risks to the demand side are that we are underestimating the level of EV demand, and that the risk on the supply side is that we are being over optimistic about the industry's ability to add capacity on time and on budget.

I will now turn the call over to Paul.

<u>Selected Financial Results – Paul Graves</u>

Thank you Pierre.

2017 saw a solid cash flow performance, driven by a significant improvement in cash collection in Brazil. One important metric that we track is of course past due receivables in Brazil, which have declined by almost 30 percent compared to the end of 2016. While we do not expect past dues to completely disappear, we believe that 2018 should see us move back to levels consistent with historical performance.

For the full year, we saw Adjusted Cash from Operations slightly below 2016. However, this was entirely due to a cash outflow in the final two months from the acquired business, as we started to build trade receivables. As you recall, we did not acquire any of the receivables with the business, creating this one-off cash outflow in the quarter.

Net debt finished the year at just under $3 billiion, reflecting the $1.2 billion payment to DuPont made in the fourth quarter.

One important area that is getting a lot of attention today is the tax rate. We finished 2017 exactly where we expected, with an effective tax rate of approximately 15 percent. This rate reflects the fact that the majority of our income is generated in lower-tax jurisdictions, reflecting the nature of our supply chain and our revenue mix. Looking forward to 2018 and beyond, recently enacted tax reform in the US impacts us in three main ways. First of all, we will have a transition tax, payable over the next 8 years, of approximately $200 million, reflecting tax on overseas retained income. This will impact cash flows in the coming years but will not impact our effective tax rate. Second, we see a one-off charge to GAAP earnings reflecting the revaluation of certain assets, most notably deferred tax assets, of around $160 million. Again, this will not impact our future effective tax rate.

Third, we will see a rise in our effective tax rate for 2018 as a result of the imposition of what is effectively a minimum tax on overseas income, combined with a restriction on the use of foreign tax credits to offset this additional tax. What this means to FMC is that wherever we see a tax rate outside the US of less than around 13 percent, we will be hit with an additional US tax bill under the GILTI provisions of the tax reform. For us, the offsetting reduction in the US tax rate will not be sufficient to offset this minimum overseas tax surcharge, since we do not generate significant US income today. While this changes a little as a result of the acquisition of assets from DuPont, the net effect is that our effective tax rate for 2018 is likely to increase by about 300 basis points, at the midpoint of the range, to 18 percent. I would caution you that we continue to work our way through what are very complex calculations, and legislation that in many areas is somewhat ambiguously worded. We will continue to refine our calculations and seek clarity as to the treatment of certain items, and you should expect us to update you on our estimate as to the tax rate in each of the coming quarters.

Looking into 2018 for cash flow, we expect to generate Adjusted Cash from Operations in the range of $550 million to $650 million. Capital spending will increase to around $250 million at the midpoint. Lithium will invest around $105 million, led by the expansion of lithium carbonate capacity in Argentina and the continued addition of lithium hydroxide capacity. The benefits of these investments will start to accrue later in 2018 for the carbonate debottlenecking, in 2019 for the hydroxide expansions and in 2020 for the carbonate expansion. Ag Solutions capital spending is expected to be approximately $95 million. And corporate-level capex will be approximately $50 million, which is mainly the initial spending on the two year implementation of a new SAP system.

Finally, the Lithium separation remains on track. We expect to be in a position to file initial drafts of the required documents with the SEC in the summer of this year, which gives us confidence that we will list Lithium in the late third or early fourth quarter of 2018, with the full separation from FMC taking place late in the first quarter of 2019.

With that, I will hand the call back to Pierre.

<u>Concluding Remarks – Pierre Brondeau</u>

Thank you Paul.

In summary, we feel very good about where FMC is today. Our Ag Solutions business delivered a strong Q4, and we are set to deliver an exceptional 2018, with revenue growth significantly above the market growth rate. The integration of the acquired business is progressing very well. We are in the early stages of understanding the growth synergies, and we will communicate further regarding scale of these synergies on future calls. Lithium had a very strong quarter to finish the year and is on track to deliver another exceptional year in 2018.

With that, I will now turn the call back to the operator for questions. Thank you for your attention.

Closing – Michael Wherley

That is all the time that we have for the call today. As always, I am available following the call to address any additional questions you may have. Thank you and have a good day.