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CONFERENCE CALL PARTICIPANTS

Operator

Ben Kallo *Robert W. Baird & Company, Inc. - Analyst*

Gerry Sweeney *ROTH Capital Partners - Analyst*

PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Calgon Carbon Corporation's Third Quarter 2016 Earnings Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session.

(Operator Instructions)

Thank you. I'll now turn the conference over to Dan Crookshank, Director of Investor Relations and Treasurer. Please go ahead, sir.

Dan Crookshank - *Calgon Carbon Corporation - Director of IR & Treasurer*

Thank you, Chrystal. Good morning everyone and thank you for joining us for today's conference call. This call is also being webcast through our website at www.calgoncarbon.com via a webcast link that can be found on the investor home page.

As a change to our previous practice, management's prepared remarks are being accompanied today by presentation slides. Those of you accessing the call via the webcast will find the presentation displayed in the webcast window. A standalone copy of this presentation is also available for download by the same link to today's webcast.

Our speakers for the prepared remarks portion of today's call are Calgon Carbon's Chairman, President and Chief Executive Officer, Randy Dearth; and Calgon Carbon's Senior Vice President and Chief Financial Officer, Bob Fortwangler. Also on the call and available to take your questions are Executive Vice President and leader of our Core Carbon and Services business, Jim Coccagno; and Executive Vice President and leader of our Advanced Materials, Manufacturing and Equipment business, Steve Schott.

I'll now draw your attention to Slide 2. Statements made today during the call which are not historical facts are considered to be forward-looking statements and are made pursuant to the Safe Harbor provisions of federal securities laws. A list of factors that could affect actual results can also be found in the news release we issued earlier this morning and are discussed more fully in the reports we file with the SEC, particularly those listed in our most recent Annual Report on Form 10-K. These filings, as well as this morning's news release can also be found in the Investor Relations section of our website.

Now, let me turn the call over to Randy.

Randy Dearth - *Calgon Carbon Corporation - Chairman, President & CEO*

Thanks, Dan, and thank you everyone for joining us for our third quarter conference call this morning. As you can see on Slide 3, we're reporting EPS of $0.13 on revenue of $124 million for the quarter. As we mentioned on last quarter's call, sales were expected to come in 3% to 6% lower than the second quarter, reflecting normal seasonal patterns and continued sluggishness in global industrial markets. Relative to that guidance, sales came in near the low end of that range. In addition to softness in industrial-related sales, we encountered some temporary operational issues at our Tipton reactivation site, which have since been resolved.

If I take a step back and look at the quarter relative to last year and the first half of this year, it is apparent that the continued softness in demand among industrial customers is weighing heavily on the sales of our carbon and service offerings in our industrial processes, environmental water and environmental air markets. During this slowdown in global business spending, we are maintaining our market leadership, but we can't escape the fact that our industrial sector customers, that also include many of our top customers, are purchasing lower volumes from us this year than last year. Because these global customers account for about one-third of our consolidated sales, the slowdown naturally nationally cascades down to our results.

About half of the year-over-year variance in sales is related to weak industrial sector customer demand. The other sizable impact on this year's sales versus last year is the exit of a significant legacy food pack contract for mercury removal, which we've talked about on past calls this year.

A bright spot continues to be the very attractive opportunity for our FILTRASORB products and equipment solutions for the removal of PFCs. We continued to have great success in this market during the quarter. Also during the quarter, the IMO ratified the 2004 ballast water convention finally. With the convention coming into force on September 8, 2017, this development brings exciting opportunities into our line of sight, especially starting in 2018.

Another piece of good news during the quarter was the annual redetermination by the Department of Commerce of the tariffs to be assessed on steam-activated carbon imported from China. This tariff increase helps ensure a fair pricing for products sold in the United States. And finally, we closed on the acquisition of CECA's activated carbon and filter aid business yesterday. This marks our entry into exciting new product areas for us, including the manufacture of wood-based activated carbons and adjacent filtration media products. It's day-two, and I'd like to officially welcome our new employees to the Calgon Carbon team.

Please turn to Slide 4 for an operational overview of the third quarter. We've organized this review into six sections, one for each of the key end markets we serve. Starting with the left side of the slide, a thread running through our performance in the industrial processes, environmental water and environmental air end markets is the weak demand we already discussed.

Staying on the left side of the slide, in the environmental water market, ballast water system sales remained slow during the quarter. However, since the IMO ratification, we're seeing a sharp pick up in monthly quote activity, which bodes well for sales gain starting late next year. Regarding US Coast Guard Type Approval, we plan to proceed with required testing using United States Coast Guard prescribed test methods beginning in the first quarter of 2017. If all goes as expected, we should be ready to file a Type Approval application with the Coast Guard in the fourth quarter of 2017 and enter 2018 in even a better position to drive growth in ballast water treatment system sales.

In the environmental air treatment market, mercury removal sales were solid as expected. We continue to win business, reinforcing our expectation that we will capture approximately 30% or more of the market for powdered activated carbon for mercury removal based on value.

Turning to the right side of the slide and starting with potable water, demand in this end market continues to steadily develop. During the quarter, we won six orders totaling $5.6 million for the removal of PFCs in drinking water in the United States, bringing to 15 the number of projects we have won this year. We're continuing to proactively develop opportunities grounded in the proven track record of our FILTRASORB coal-based granular activated carbon, which provides superior performance compared to other carbons and technologies.

While the significant portion of the value of these awards relate to our carbon absorption equipment, development of this market opportunity continues to add value to our installed base of granular activated carbon for potential reactivation work in the future.

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As planned, toward the end of the third quarter, we also shipped 2.5 million pounds of virgin granular activated carbon to a drinking water treatment facility in Hong Kong. As you may recall, we won an award earlier this year to provide 3.8 million pounds of virgin granular activated carbon to this facility. The balance is expected to be delivered in the fourth quarter. Our high-quality products and proven technical service expertise continue to make us the granular activated carbon provider of choice to meet the drinking water purification needs of potential customers around the world.

Our sales into the food and beverage end market remained stable. In specialty carbons, we benefited from the strong demand for activated carbon for metals recovery in the Americas and some increased sales for respirator carbon products in Asia.

That completes my review of the third quarter performance. I'm going to close our prepared remarks today with a high level view of what we see on the horizon for Calgon Carbon during 2017, but first, I'd like to turn the call over to Bob, who will take you through the review of our financial results for the quarter and our guidance for the fourth quarter. Bob?

Bob Fortwangler - *Calgon Carbon Corporation - SVP & CFO*

Thank you, Randy. Good morning, everyone. I'll start my review on Slide 5, which presents the income statement highlights for the quarter. The waterfall chart on the upper left displays the bridge for our margins from the third quarter of 2015 to this year's third quarter.

For the third quarter of 2016, we generated a margin rate of 31.1% compared to 36.2% last year. As you can see, the two largest contributors to the 5.1 percentage point decline relate to the expiration of a high margin legacy mercury removal contract that Randy mentioned earlier, as well as product and customer mix. Our decision to sell opportunistically into low-end more competitive markets to partially make up for sluggish sales into higher end areas of our markets, while a sound economic choice, resulted in an unfavorable mix and represented an estimated 2.2 percentage point decline. In addition, our margins were negatively impacted by higher total contribution of sales from Japan, which is traditionally a lower margin market for us.

The second waterfall chart on this slide displays the bridge of income from operations from the $17 million we reported for the third quarter of 2015 to the $9.3 million for this year's third quarter. What stands out here is the flow-through of both the year-over-year decline in sales and the impact of the unfavorable customer and product mix on our margins. Expenses related to our acquisition totaled $600,000 for the quarter. Offsetting these decreases were lower employee-related costs, including lower pension settlement costs, as well as the absence of expenses related to last year's SAP re-implementation.

Turning to Slide 6, I'll go over balance sheet highlights. We ended the quarter with $57.2 million in cash and $102.3 million in debt. In terms of working capital metrics, which are displayed in the chart on the right, accounts receivable DSO has improved from 66 days last year to 61.6 days this year. Inventory turnover in days increased to 123.4 days. However, this is approximately nine days less than where we were at the end of the second quarter and reflects our ability to slow down our procurement and use of outsourced carbons as a lever to reduce inventory levels. Working capital as a percent of sales rose to 27.6% compared to 24.8% last year due to the lower sales base.

Looking at our operating cash flow on Slide 7, despite the decline in net income for the first nine months of 2016, we have generated roughly the same level of operating cash flow as last year. The difference is mainly the improvement in working capital.

On Slide 8, we display uses of cash for the first nine months of 2016 compared to the same period last year. Of note in comparing these two waterfall charts is the difference in capital expenditures. We have been investing heavily for the past couple of years in various plant refurbishment, expansion and efficiency projects. Having invested $23.4 million in capital expenditures year-to-date, we are still within our expected range of $30 million to $35 million for the full year.

Please note, we expect our 2017 capital expenditures to increase as we expect significant spending on the plant refurbishment and expansion of our Neville Island facility, which until recently was delayed by permitting issues.

And I'm pleased to report that earlier this week, Calgon Carbon's Board of Directors declared a quarterly cash dividend of $0.05 per share, payable on December 15, 2016 to shareholders of record on December 5, 2016.

That concludes my review of our third quarter financial results. Now, I'll go over our outlook for the fourth quarter. Please turn to Slide 9.

Starting with sales on the left side of the slide, we expect fourth quarter sales to be 2 percentage points to 5 percentage points higher than the third quarter of 2016. This excludes any contribution to sales from the acquisition. This increase is primarily due to sequential growth in potable water end market sales from PFC projects. Our outlook includes an expected negative impact from currency translation in the range of $500,000 to $1 million.

The right side of the slide details our guidance for other income statement line items. We anticipate flat to slight sequential improvement in margins with expected results in the range of 31% to 33%, primarily reflective of a more favorable product and customer mix. We expect depreciation and amortization expense to be in line with the third quarter and SG&A expenses, excluding costs related to the acquisition, to be roughly 16% to 17% of sales. And we expect the effective tax rate to be in the range of 33.5% to 34.5%.

On the bottom right side of the slide, we've detailed a few financial impacts related to the acquisition. Given that the transaction closed just yesterday and based principally on our review of the acquired businesses' historical financials, we believe the acquisition will generate sales of approximately $14 million to $16 million in the fourth quarter. We also expect to incur approximately $5 million to $6 million in acquisition closing and related project costs. And finally, we expect to incur approximately $850,000 of incremental interest expense compared to last quarter due to the revolver borrowings we initiated to complete the acquisition.

I'll now turn the call back to Randy for closing remarks.

Randy Dearth - *Calgon Carbon Corporation - Chairman, President & CEO*

Thank you, Bob. So turning to Slide 10, I'd like to share with you our initial views on 2017. First and importantly, we are keenly focused on integrating our newly acquired business and capturing planned synergies. While already a nicely profitable and steadily performing business, we look forward to delivering on our valuation creation plan to improve the business' EBITDA by 40% or more by 2019 through a combination of synergy capture, de-bottlenecking of the wood-based activated carbon manufacturing facility and other operational improvement initiatives.

We're excited to get moving and continue to expect the acquisition to be accretive to EPS in 2017 by $0.08 to $0.11, excluding impacts from yet-to-be-determined purchase accounting adjustments. In terms of sales and consistent with the business' prior performance, we expect the acquisition to add approximately $100 million to our sales in 2017.

While current global economic conditions do not provide us with the confidence to assume a rebound in sales growth from our industrial sector customers, we do expect that several of the positive market developments that I've already mentioned and that are highlighted on the slide will benefit our performance in 2017, specifically in the domestic drinking water market, the environmental water market for ballast water treatment systems, and the environmental air market related to mercury removal products. And we expect that executing on our cost improvement programs will lead to improvement in margins and a reduction in our SG&A operating expenses. Once again, these are our initial directional views and as our usual practice, we will provide more granularity and detail related to our 2017 outlook on our fourth quarter call in February.

In closing, while we can't control or predict the timing of a recovery of industrial-related end markets, expect us to stay focused on the things we can control, including advancing business opportunities that have already been developed and those that may emerge for premium activated carbon, services and equipment offerings. We'll ensure an efficient and effective integration of our acquired business, and we're going to continue to control and reduce our cost. As a result, and when industrial related markets eventually swing back to growth, we will be leaner and well positioned to leverage the higher end market leadership positions that we expect to maintain.

That completes our prepared remarks, and I'll now open it up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Ben Kallo, Baird.

Ben Kallo - *Robert W. Baird & Company, Inc. - Analyst*

I guess, as we look ahead into the integration of -- and congratulations for closing the acquisition. How much more leverage do we think about -- how much more levered are you to some of these industrial markets where you're seeing weakness and what do we worry about that? And also within Europe, what are you guys seeing there?

Then my second question is around -- there's some commentary around the ballast water market developing and just that's been on the come for a long time. But what are you guys seeing as far as inquiries and orders right now? And knowing that's most likely in 2018 is when we see revenue. And then, I guess my last question is, as these markets come together -- you talked about, with the exception of industrial market maybe going to [re-bounce]. How do you guys think about capacity? Where you are right now? I know, you just have a lot to deal with the integration, but how you think about capacity going into next year, potential to expand capacity?

Randy Dearth - *Calgon Carbon Corporation - Chairman, President & CEO*

Let me start with first part of your question, which was about CECA and what type of markets is it exposed to. If you go back, when we introduced the acquisition back in April, one of the things that excited us about the acquisition was the fact that these are more stable markets that we're going into. So 50% of the CECA business is in food and beverage and roughly 25% of their businesses is in pharma and the rest of that is split between other -- for instance, industrial and water, etcetera. So 75% of their business is not related to the traditional industrial that we refer to here which again is a great market for us and the diversity CECA is going to help level that up. So that's the CECA question. I'm going to defer to Steve to talk about the ballast water question.

Steve Schott - *Calgon Carbon Corporation - EVP of Advanced Materials, Manufacturing & Equipment Division*

Relative to the ballast water, I think as we indicated, there has been a tremendous pickup in activity for quotes, three times the several months that preceded ratification. We're quite excited about it. We are intending to -- we think, as you indicated, that the ramp-up really is in 2018 but we certainly expect to see increased sales in 2017, principally in the latter part of the year once the September 8 compliance date takes effect.

And I think you also had a question on Europe, and I would say in general, Europe has been very steady and the challenges they've had have been what we've experienced as a company overall, principally in the industrial sector and some general slowness. But overall, Europe is relatively flat year-over-year and we think at the moment, that's a reasonable result.

Jim Coccagno - *Calgon Carbon Corporation - EVP of Core Carbon & Services Division*

This is Jim. I'll answer the capacity question. So going into 2017, it's a bit early to tell you what our plan is for capacity. But we do have levers as Bob has mentioned about pulling back on outsourced purchases and some other levers that we can pull and we will pull them if need be. So as we roll into our plans for 2017, I think that will become more clear.

Operator

Gerry Sweeney, ROTH Capital.

Gerry Sweeney - *ROTH Capital Partners - Analyst*

Just a question on the industrial market side. Pardon me if you've answered this. I was jumping on back and forth a little bit between calls. Has the industrial market gotten worse or has it sort of plateaued? I'm just curious of how it has developed, let's say, over the -- anywhere from 12 to 18 month towards today, obviously with the headwind for a while, but I'm curious if it has gotten worse or sort of just steady state down per se?

Jim Coccagno - *Calgon Carbon Corporation - EVP of Core Carbon & Services Division*

This is Jim. It surely hasn't gotten better. I would say, beginning in the second quarter of this year, we've seen a further decline from what we've been experiencing, say, for the last 18 months. Not sure when that will change. We're hoping that there will be some stabilization, but we are not predicting at this point in time that there will be a rebound at least through the first half of next year, but I would say from our perspective, we really started seeing it kind of in the middle of the second quarter take a tick down.

Gerry Sweeney - *ROTH Capital Partners - Analyst*

Okay. That's helpful. I knew it wasn't up, that's for sure. And then also on the PFC, perfluorinated compounds, how big of a potential market is that? I see more and more tidbits about something the community is dealing with it. I think some of it comes from the firefighting foam and plastic manufacturing, et cetera, but any indication on that how large of a market that could become and will that become, I guess, a regulated compound by the EPA?

Jim Coccagno - *Calgon Carbon Corporation - EVP of Core Carbon & Services Division*

Yes. So, this is Jim again. It's still too early to tell on how big the opportunity will be. It's kind of evolving daily, given example the EPA advisory limit is 70 parts per trillion. Now you have states getting involved and lowering that. So, New Jersey is lowering at the 14 parts per trillion and there's some -- there is a bill in Pennsylvania to lower it to five parts per trillion. So I think in the end, the market will be determined by not only what the regulatory environment is saying, but also what the consumers are demanding which at this point in time is non-detect level. So still too early to tell. Lot of activity going on. I'm proud to say that we're being looked at as one of the experts in the area and people are coming to us to provide solutions, and our equipment and FILTRASORB coal-based product line is the solution of choice right now.

Operator

(Operator Instructions) Gerry Sweeney, ROTH Capital.

Gerry Sweeney - *ROTH Capital Partners - Analyst*

This is probably more directed towards the ballast water, and we've talked about this a little bit. The US Coast Guard has their own methodology and the IMO has their methodology. Where are you seeing some of this bidding activity? Is it more some of the international players? And what I'm trying to get at is, I'm curious as to how these markets are really going to develop because you have two different standards. It could cause a lot of headaches across the board. You have your existing Hyde platform. I think you modified it to go for the US Coast Guard standards. So, I'm just curious as to where the opportunity is near term, how this market develops through these two-system pipes, sort of delayed timing and uptake of orders, etc.?

Randy Dearth - *Calgon Carbon Corporation - Chairman, President & CEO*

Sure, Gerry. Obviously, it's a really big market opportunity at $18 billion to $28 billion. It's early. Interestingly enough on potential delays, recently -- very recently, the Maritime Environmental Protection Committee of the IMO met. They refused to entertain a discussion around the delay. So there is not a provision for a delay, yet. So, we're planning as if there won't be -- we're planning to test for Coast Guard early 2017 and ultimately file for a Coast Guard approvals later, assuming that there is not a convergence of these rules and then we have separate rules to deal with. But I think we and others will find a way to tend to the market or markets. And then, ultimately, if the timelines stick, then we will be serving [fully] the $18 billion to $28 billion market, and hopefully, our innovative solutions will give us an advantage. And that's how we're thinking about it currently.

Gerry Sweeney - *ROTH Capital Partners - Analyst*

Okay. And correct me if I'm wrong, the rule goes into effect next December and then -- at which point, any ship that goes into drydocking has to implement, say, a ballast water system at that time.

Randy Dearth - *Calgon Carbon Corporation - Chairman, President & CEO*

Yes, September 8 is the date of implementation. And I think, at this point under the IMO, it's not necessarily the drydocking date, but the date surrounding their pollution control certificate. It will still have the same five-year interval affect, as I understand that the pollution control certificate is typically obtained sometime after a drydocking occurs. But it's still very much looked at like a heavy five-year window, five or six year window of business, perhaps in total, a 10-year attractive market. So, it's not necessarily the dry dock at this point under the IMO, but rather it will be in relation to the ship's pollution certificate.

Gerry Sweeney - *ROTH Capital Partners - Analyst*

Okay, which is -- sounds like it's tied a little bit to drydocking.

Randy Dearth - *Calgon Carbon Corporation - Chairman, President & CEO*

It is, yes.

Gerry Sweeney - *ROTH Capital Partners - Analyst*

But in essence, it's the similar window.

Randy Dearth - *Calgon Carbon Corporation - Chairman, President & CEO*

That is correct.

Operator

At this time, there are no further questions in queue.

Dan Crookshank - *Calgon Carbon Corporation - Director of IR & Treasurer*

Thank you, Chrystal. I'll let you close the call, but I'll let you all know on the call that we will be available for questions throughout the day. Thank you very much for joining us this morning.

Operator

This concludes today's conference call. You may now disconnect.