Event: Solvay Q2 2017 Results Conference Call

Date: 01.08.2017

Speakers: Jean-Pierre Clamadieu and Karim Hajjar

Call Duration: 57:12

Operator: Ladies and gentlemen, welcome to the Solvay second quarter 2017 results conference call for the investment community. I am pleased to present Mr Jean-Pierre Clamadieu, CEO, and Mr Karim Hajjar, CFO. For the first part of this call all participants will be in listen-only mode and afterwards there will be a question and answer session. Please dial 01 on your telephone keypad to enter the queue for the question and answer session at any time. I now hand you over to Mr Jean-Pierre Clamadieu. Sir, please go ahead.

Jean-Pierre Clamadieu: Thank you very much for your introduction. Hello, everyone. I'm here in Brussels with Karim Hajjar and Kimberly and we are very pleased to have this opportunity to share with you the highlights of our second quarter results. We'll use the usual structure: I will make an introduction, Karim will come with a bit more detail. We'll try to keep it collectively short so that we can have as much time as necessary for the Q&A session.

Clearly, strong momentum continuing into Q2. Volume growth is indeed the key driver for our EBITDA growth and we are very pleased to see that all four segments contributing to sales and profit growth in the quarter. Sales increased, as you've seen, by 11% and again the key driver is volume growth, which is what we were expecting, but we are pleased to see that this is indeed materialising and that's something which demonstrates that indeed our strategy is paying off. Eighteen percent EBITDA growth with a one-time event, which is linked to Cytec integration synergies. We have aligned the benefit of the Cytec teams to the policy of Solvay. This generated a 38 million one-off positive impact on our EBITDA and we'll see the consequences materialising in cash over the next few years. Once again, the key driver was higher volume and this took place in businesses which have been going for quite some number of quarters, but we've seen also the situation of a couple of businesses which suffered last year turning. This is the case for oil and gas in North America and this was also the case for our smart device position. Our cost grew with our capacity expansion, but operational excellence measures that we have put in place help offset the inflation. Overall, new record operating margin at 23%, which puts us probably in the leading seat within the European-headquartered diversified chemical companies.

And as you've seen in our presentation, we want to present not only financial but also extra-financial metrics and greenhouse gases reduction is probably the one which is the most important for us, and you see that we continue also to improve on this metric and we are very much in line with the strategic commitments that we have shared with you when we had our capital markets day in London almost a year ago.

Maybe just a word on Cytec. Karim will comment the various clusters, but on Cytec, cost synergies are now at a run rate which is approximately €115 million, which is really at the top end of the expectations that we've shared with you. The focus now is on generating revenue synergies and we have several projects underway and we are already seeing some actual impact on some markets, the fact that we are becoming, I would say, more global in this business; Cytec tends to be a little bit US-focused and now we are really – our ambition is really to be a global player in this market. This is already bringing some new revenues and we have some technology developments, the most promising one being around thermoplastic composite.

Talking of composite, we are starting to see a turnaround in composite for aerospace. We've seen some growth this quarter. June was the strongest sales month since we have owned the business and this is very much linked to, one, the improvement in production of single-aisle aircraft both at Boeing and Airbus. These very large players have experienced over the past year a number of difficulties in their manufacturing operations. They are improving, as you might have seen, and we are benefiting from that in a context where we don't see much inventory movement in the supply chain. There was some inventory reduction last year that has impacted us, but now we think the supply chain is quite lean in terms of inventory and we are benefiting directly from what's happening in the beginning of the chain. And on top of that, a couple of very successful programmes, the F45 and the LEAP engine, which are at the very aggressive slope in terms of increasing in production rate and we are benefiting from that.

I guess I'm very pleased, and I have to admit it, with our performance in the first half. I think the strategy that we've put in place over the past few years is indeed delivering and the fact that we see strong volume growth as being the driver of our EBITDA growth is something which gives us assurance that we have built indeed strong and solid growth engines within Solvay's portfolio.

With that, I would like to turn to Karim to go into a bit more detailed insight on our financial performance.

Karim Hajjar: Thank you, Jean-Pierre. As usual, the numbers I'm going to discuss are on an underlying basis and I will refer to a few slides that are available on our website.

I'll start with our top-line growth, our sales growth of 11% and on slide 10 you will see the facts and the figures there. I'll maybe just highlight the fact that this is the third consecutive quarter where we've now seen sales growth and that dynamic is very, very encouraging so far as we are concerned. Volume, as Jean-Pierre alluded to, contributes the vast majority of that, with 8% of that growth, but it's also good to note the contribution that pricing has contributed as well in terms of the 2.8%, mainly in the polyamide business. But it's EBITDA where I'd like to focus most of our time today and perhaps invite you to turn to slide number 11.

And beyond the fact of EBITDA being up 11%, what I'd like to highlight is the volume we referred to contributed €96 million to the growth in EBITDA, and that was partially offset by fixed cost increases. Now, clearly, as we drive volume growth we have also been investing in new capacity. So, for example, if I look at the three most notable capacity increases in Sadara, in the PEEK plants in Georgia and the States, which actually serve the smart devices market, the carbon fibre expansion within South Carolina, all of that comes at a cost and that's why you see cost increase there as well.

Pricing did contribute a positive impact of 5%. Again, that is helped not least by our excellence programmes as well as successful price increase initiatives.

I do want to draw your attention to one item on the profit bridge, which is the 27 million positive other and that includes the 38 million of one-time synergies in the US, whereas in Q2 last year you may recall that we had a one-time gain of €11 million resulting from the sale of surplus assets in soda ash.

That's the overall picture. If I turn to the individual segments, Advanced Materials: EBITDA up 22%, a record EBITDA margin, 31%. So, where does that come from? Specialty Polymers has sustained its broad-based growth in a number of markets, again led by strong demand in the automotive sector, but we also saw some acceleration of growth in smart devices; remembering, however, that the first half of last year was somewhat subdued, not least because of the destocking impact that you will, no doubt, recall.

Jean-Pierre has already mentioned the positive momentum in the Composite business and he's explained to you how the production increases we're seeing in single-aisle LEAP and the Joint Strike Fighter are really being to show themselves now to our bottom line.

But there's more. Advanced Formulations grew 5.2% and the EBITDA margin was sequentially flat, at 17%. As we explained last quarter, the activity levels in the oil and gas market are improving and this is positively impacting our Novecare business, driving sales up 24% in the quarter. We also benefited from increased demand in the agricultural market.

Turning to Technology Solutions, customer-specific issues in mining were offset with new business developments in that business.

Performance Chemicals had a decent quarter, with 1% EBITDA growth while sustaining a very strong margin of 29%. Where is it coming from? Peroxides was a significant contributor in the quarter with the start-up of the Sadara operation for HPPO in Saudi. Soda ash remained steady and, in fact, we saw slight volume increases mainly in the seaborne market, whereas bicarbonate continues to grow supported by the investment that we made in the new Thailand plant. Also, you remember that soda ash benefited this time last year from that one-time gain with the sale of surplus assets of 11 million.

Functional Polymers had a superb result in this quarter driven by – well, they had a 57% EBITDA increase driven by two factors: strong demand in auto and price increases that passed through the cost increases that we experienced earlier in the year.

But there's more to our delivery this quarter than just EBITDA. If you turn to slide 12, you'll notice that our net income is up 38%. Not only does that reflect the EBITDA increase but also two other things: one, a drop in financial charges and, two, a reduction in our underlying tax rate from 30% last year to 26% this year, and this is driven largely by the evolution in the geographic mix of our pre-tax earnings.

Cash. On page 12, you will see the picture on debt and cash and there's a few things I'd like to highlight here. One is the fact that our free cash flow in the first half of this year from our continuing businesses doubled, from €123 to 245 million. It's coming from a number of factors: higher profits, clearly, but also very strong discipline on working capital. Our working capital intensity is remaining flat compared to last year despite an 11% increase in revenues. Now, that takes some doing and so we're really pleased with that continuing discipline. Clearly, we also have the reduction in capital expenditure, but that shouldn't be a surprise; that's exactly where we thought we would be at this stage. So, all in all, we're very pleased with the operational cash flow performance of the quarter.

Debt is down materially at this time of year. You may recall that the seasonal nature, the profile of our cash generation is very much back-ended and we see a much stronger profile in this first half, but M&A contributed just under a billion euros of net proceeds. That obviously helps to reduce our debt by €800 million when compared to 31st December 2016.

Now, finally and before I forget, I just want to highlight the fact that you may have picked up already that in May S&P upgraded our credit rating to BBB flat from BBB minus. I really welcome this as an independent indication and validation of the portfolio progress and fundamentally of the real improvement and the strength of our cash generation and resilience of our balance sheet.

And with that, I hand the floor back to Jean-Pierre.

Jean-Pierre Clamadieu: Thank you very much, Karim. So, just a couple of comments before opening the Q&A. The first one, on strategic priorities and I think that, indeed, besides what we've presented in terms of numbers for our Q2 results, we are continuing to make progress, which are worth noting. We are at the midpoint of our 2016/2018 strategic roadmap, the one we have commented in our last capital market day, and at this point we are on track to deliver on our mid-term objectives and I feel confident that the company will indeed be able to achieve or exceed the objectives that we shared with you almost a year ago.

I would really like to take this opportunity to thank all our employees and I appreciate the fact that our customers indeed are trusting us. We are more and more focused on large programs which are absolutely key to the success of our customers, being smart devices, being airplanes, being automotive, and our ability to deliver new solutions to our customers is key and we can do that only if they trust us and this is the case.

Regarding portfolio upgrade, we have taken some significant actions and you've seen that we've been very focused on closing the transactions that we have announced at the end of last year or early this year. We remain focused on remaining opportunities. I've made several comments that the portfolio movement expected in '17 would be more in the direction of divestiture, so we are looking at opportunities. We are not yet at the point of time where we can share with you any actual news, but be confident that we are indeed continuing to work on these opportunities.

2017 outlook, how do we see the rest of the year? Well, we expect to continue to see sequential improvement, which will be linked to volume growth, especially from our core growth engines in Advanced Materials and Advanced Formulations. We have to be aware of what was the profile of 2016. 2016 is the year in which we had a rather slow first half and a more dynamic second half, so the comparison will be a little bit different in the first and second half. Taking our performance and expectations into account, we have decided to raise our full-year EBITDA estimate to grow by high single-digit, taking into account the current situation in various macro parameters, including exchange rate.

And with that, we are ready, Karim and myself, to take your questions. Thank you very much.

Operator: Ladies and gentlemen, we will now begin our question and answer session. If you wish to ask a question, please dial 01 on your telephone keypad and you will enter a queue. After you are announced, please ask your question.

We have a question from Peter Mackey from Exane BNP Paribas. Sir, please go ahead.

Jean-Pierre Clamadieu: Hello, Peter.

Peter Mackey: Thanks very much. Good after, Jean-Pierre and team. A few questions, as ever, if I can, please. First, in the Advanced Formulations business, if we strip out the Cytec pension gain, you did see some margin pressure there. We've seen that at a number of your peers in the surfactants formulations area. Can you talk about what you're doing and the confidence you have in regaining lost margin from input costs, please? And perhaps give us some pointers on the mining side, when you think Tech Solutions is going to start to recover. You know, that's still lagging, I think, some of your longer-term growth expectations.

Secondly, in Performance Chemicals, obviously everybody's very focused on what's going on in soda ash. Excepting the annual contract situation, you know, you're still enjoying pretty strong volumes on the seaborne market and spot markets; are you seeing that the initial Turkish volume, the expansion at Eti Soda, you know, are you seeing any evidence of those volumes in the spot markets and are you feeling any or seeing any signs of pre-marketing from the Ciner capacity, please?

And then perhaps just a final question, on the guidance. You indicated at the first quarter stage that you expected to meet or exceed your mid single-digit guidance, so you're already pointing towards high single-digit. You've just got this 38 million one-off, which adds close to two percentage points. I mean, is it a simple case of, in your mind, adding that 38 million or are you more confident in the underlying performance as well?

Thanks very much.

Jean-Pierre Clamadieu: Okay, let's start with the last question, because the answer is very easy. In fact, we knew that the 38 million would take place this year. We didn't know at which quarter, because there were some accounting complexities there. So, for us, it's not something new. It's new for you, but it's not for us. So, indeed, the sequential increase in guidance from mid-single to over mid-single and now to high single really demonstrates the fact that we've gained confidence in the volume growth and, yes, today we feel very confident to share this high single-digit guidance with you.

On the Advanced Formulations business, we've seen a bit of margin pressure. There's two elements, one which is linked to Novecare and this is very much the raw material price situation. So, we've suffered, as we said in the Q1 call, we suffered from oleochemical not only increase but volatility in oleochemical prices, which put pressure on margin, delayed, in some cases, our customer orders. What we've done – and it's something that we started, in fact, a year ago – we have renegotiated two very large contracts for oil chemical access, which will give us extra competitiveness, so we feel reasonably confident that, indeed, over the course of the second half we'll see margin increasing.

On Technology Solutions, we have seen also a bit of pressure on margin, which was mostly linked, in fact, to some operational difficulties that our customers were facing: strikes or various technical difficulties, which impacted our ability to deliver and had some impact on margin. Things are normalising there, so overall, yes, I would expect the Advanced Formulation cluster to improve its margin over the course of the next couple of quarters.

Regarding soda ash, to try to be as specific as possible: you might know that our Turkish competitors are working on two different projects. There was a first extension of half a million tonnes a year, which is done and in the market, so it was in the market already for Q1, and then there is a second project which will come online in the remaining part of 2017 and mostly in 2018. This project has been expected for quite some time, and for the last three or four years we've been discussing about this. We have prepared ourselves as much as we could, and indeed I think the rather good delivery of soda ash – I can probably take the 'rather' – the good delivery of soda ash for this first half of the year shows that we are, indeed, well prepared and able to do the most out of the current market conditions, taking into account a bit more competitive pressure. So, very much what we've said: there will be impact when all this Turkish capacity will be on the market, but we think that we'll be able to weather this impact, with some pressure on our margins but not for such a long period of time. And again, our confidence in our ability to manage this situation is probably a bit better today than it was six month ago.

Operator: Thank you. The next question is from Nathalie Debruyne from Petercam. Madame, please go ahead.

Jean-Pierre Clamadieu: Hello.

Nathalie Debruyne: Hello, good afternoon. Well, first of all, congrats on the solid set of results. I have two questions. The first one would be on working capital. Karim, I know that you flagged that actually, working capital was more or less flattish in the first half of the year, but it tended to spike from what I see in Q2, so can you elaborate a bit what it was driven by? Because I do not have the impression, when I look at your balance sheet, that it was driven by an inventory build-up, so did the payments terms change with your suppliers, something like that? I would like to understand this a bit.

And then the second one – well, actually, perhaps I have three, I'm sorry – the second one would be on automotive. We see a lot of players who are somewhere in the supply chain actually being a bit more cautious on the second part of the year, so what is your stance on that one, and what does that mean for your businesses in both specialty polymers and polyamide?

And then the third one, perhaps you'll start to feel that I'm obsessed with that, but it's on oil and gas. We have seen the rig counts – well, actually increasing since May last year, but it seems to be slowing down as from June, somewhere like that, and I was wondering how you feel for the second half, for oil and gas? Should we expect that the – well, less support, as I would say, not to say negative price mix, to persist in the second part of the year?

Jean-Pierre Clamadieu: Karim, working capital; where is the spike coming from?

Karim Hajjar: I'm looking for it but I can't see it, so let me straight away say that, Nathalie. If we look at inventories, €1.7 billion this quarter and the same point last year; receivables, €1.7 against €1.7; payables, €1.323 this year compared to €1.25 last year. So, these are the facts. If we look at working capital intensity, so taking total working capital to sales, we're about 3% – in fact 2.9% – better than last year. Last year I did flag the fact that we had an exceptional receivable in respect of Inovyn and our accelerated exit. So, on a like-for-like basis, it's very, very similar.

If I look at the internal metrics – and we look at this every month; I look at day sales outstanding, I look at overdues – this time last year, I did say to you that we set a new record. And you know what? I wish I hadn't said it, because I'm going to say that this year is a new record. So, all the key operational KPIs and indicators are flashing green in that respect.

And finally, to give you an order of magnitude: if you look at our working capital and add up all the gross sums, you're talking €4.7 billion of gross working capital; to try and predict and manage to even 1% of accuracy, it's €50 million-ish. So, I look at this performance, I look at it not just in a monthly basis, on a quarterly basis, but I see real strength. So, the spike that you mentioned, help me see it; I don't.

Jean-Pierre Clamadieu: Okay, so automotive and oil and gas. Automotive, we have to realise that a little bit like Solvay results, the overall performance of the automotive sector last year was a little bit backhanded. I mean, the second half was stronger than the first half, and then the comparison will become a little bit more challenging. This being said, we continue to see strength in this business, and we are not expecting any meaningful change in this trend for the second half. There was probably a bit of stocking in the very beginning of the year in China. We think that this is now – well these cars now went to the market. So overall, a good level of confidence, knowing again that the comparable will be a bit more difficult. So, if you look at the same quarter of consecutive years' difference, it will be probably a bit less pronounced in the second half.

So, oil and gas, it's clearly a volatile market, so I have to be cautious on the comment I've made, but the situation on the ground looks good. Yes, there is a little – the speed of increase in rig count has diminished, and it has been, I think, a bit flattish on the last few weeks. This being said, there was a number of wells which we have drilled during the first half for which there was no fracturing done, so we think that this stimulation job will come. We've seen the oil and gas supply chain in the US working very, very hard to improve its overall competitiveness, and our view today is that in the current oil price conditions, activity will continue at quite a sustained rate. I was commenting in the past two quarterly calls that we've seen some negative mix effect; I mean, people moving out of the expensive guar-derivatised formulation to friction reducers. We continue to be very successful in friction reducers, but we start to see enquiries, interest, into these guar-derivatised solutions, so we think that the opportunities will continue to be significant on the ground for our oil and gas position in North America at the current oil price.

We are continuing to work on diversification. China, Argentina, Russia offers interesting opportunities, we have some businesses there. The challenge is to make sure that we can grow with the operations that are developing in these different parts of the world. But overall, we're feeling that oil and gas will continue to be a growth driver for the second half of the year.

Operator: Thank you. The next question is from Thomas Wrigglesworth from Citi. Sir, please go ahead.

Thomas Wrigglesworth: Thank you very much. Good afternoon everyone, and thank you for your presentation. I'll limit myself to two questions, if I may? The first is with regards to the outlook for 2017 and the performance of Functional Polymers. I mean, if I look at the run rate that you're delivering in the first half, you'd easily hit your guidance for the full year. So, can you just explain: am I wrong in thinking that you're expecting some kind of normalisation in Functional Polymers? And how do you see that evolution; is this now at a new level of performance in Functional Polymers?

And my second question, on Advanced Materials and the ramp – I know that we've been talking about this for a number of quarters now – of the LEAP engine and the F-35. Can you help dimensionalise the impact that we should expect through the second half and into 2018, obviously noting that you've got that mid- to high-single-digit EBITDA target for 2018 as well? What kind of contribution to that should we expect from that Composites business? Thank you.

Jean-Pierre Clamadieu: Thank you for your questions. On functional, yes indeed, we have a strong performance; we are back to EBITDA margins around 18%, if my memory is correct. There was a bit of a sweet spot in the first half linked to butadiene prices. We will see the results impact in the second half, but the operating conditions continue to be very favourable for this business, both in terms of pricing and in terms of volume. So, yes, indeed, we are wishing that this very good level of performance will continue for Functional Polymers.

On Composite, I don't want to quantify the impact that we expect from Aerospace, but we will continue to see strong ramp-up in F-35, strong ramp-up in LEAP Engine. If I listen to our customers, Airbus and Boeing will continue to see the single-aisle production developing very well, in a context where there's most new inventory movement in the supply chain, and will continue to have a negative impact on the large-body aircraft, mostly the A380 and the 777, waiting for the new version, the 777X, which will be a plus for us. So, overall, we expect to continue to see growth in composites for Aerospace during the second half of the year, and obviously, into 2018.

When you look at single-aisle airplane from both Boeing and Airbus, plus F-35, plus LEAP Engine being associated with a fourth item, we have indeed quite a nice amount of growth in front of us in these various businesses.

Operator: Thank you. The next question is from Wim Hoste from KBC Securities. Sir, please go ahead.

Jean-Pierre Clamadieu: Hello, Wim.

Wim Hoste: Hello, good afternoon. A couple of questions. First, can you offer some insight into the industrial performance of the Sadara HPPO plant? Second question, on Speciality Polymers: I think in the past couple of quarters, you cycled some easy comparatives into the smart device market. Can you maybe shed a light on how the order books are looking for that segment in the second half and into 2018? And then a third question: with the volume growth having been very strong in both first quarter/second quarter, and your CapEx guidance for the full year maintained, I can assume that maybe some parts of your organisation will run into full capacity utilisation somewhere later in the year or maybe next year. Can we expect a step up in CapEx again beyond 2017? Can you say something about that? Thanks.

Jean-Pierre Clamadieu: Sure. All very good questions. So, Sadara, I mean, if I'm a little bit provocative, I would say we are not so much interested in the operational performance, because we have a take-or-pay contract, which secures our profitability. This being said, since the end of April, we've seen the chain operating reasonably well for such a large and new complex. There were a few hiccups here and there, but overall a good performance. And again, we are in a situation where we are protected by a take-or-pay contract which started in fact in December 2016.

Specialty Polymers, I don't want to comment too much on the smart device market. We tend to be exposed to one customer – and I don't want to share information about these specific customers. I would just say that the product life cycle plays very much in our favour for the next quarters, because we expect to see new models being launched, and this is always a period which creates opportunities for us in terms of ramp-up of new production. But yes, since the end of 2016, we've seen this market turning, and this is a contributor to the growth of the group, and it will continue to be a contributor. And by the way, we are all focused – or some of us, at least – on new products, but we are going in a situation where there will be probably be a broader range of products, with existing products being continuing and new products coming. And we have also a strong position on existing products, which will continue to be produced in the next quarters.

CapEx, no, you should not expect to see a rebound in CapEx. We still have a number of plans which are not filled up, in fact, that are beginning to produce. Just to name a few which are important for us, our peak facility in the US, we are still in ramp-up mode, which means that we have capacity available in front of us. So yes, we will be pleased to fill it up quickly, but not to a point where we would be willing to add new capacity soon. Same comment on the PDDF facility that we are starting up in China as we speak. It will come online at the right amount of time, because the battery market in China is boiling because of the fast development of electric vehicles, so this facility will ramp up pretty quickly but not to a point where we will be looking at new expansion. I can continue the comments on aerospace our new facility in the UK is starting to produce the qualification batches, which will be needed to have the facility approved. So, it will take probably another year before it's operational in the sense of generating commercial sales, but as you see, I think we have quite a nice course in front of us which will allow us to continue to grow with existing assets. I mean, I could continue the example, but growth in terms of carbon fibre, we have now capacity available in North America, our Oestringen facility. We will there support the growth of F-35, LEAP engine and the new 777X. So overall, no need for new CapEx for I would say an increase in our CapEx, but just for the next two/three years. On the contrary, we probably expect to be able to continue to slightly diminish our CapEx. We've said several times that our objective was to align CapEx and our depreciation. We are still a little bit higher, but clearly, we've a lot of capacity available to supply the increasing volumes that we see coming from our customers.

Operator: Thank you. The next question is from Geoffrey Haire from UBS. Sir, please go ahead.

Geoffrey Haire: Good afternoon, everybody. I've just got three quick questions. I'm just going to come back to Thomas's question on Functional Polymer margins into the second half. Can I just confirm that you've said that you expect the 17% EBITDA margin you achieved in the first half to continue into the second half despite the fact that prices will reverse, because butadiene prices are going down?

And secondly, can I just ask, what other one-offs do you know about in the second half of the year that would be helpful for us to know? And then also, the fixed cost increase in the EBITDA that you reported because of capacity coming on; how much of that was structural, i.e., will stay within the cost base, and how much of it was one-off, i.e., the ramp-up of new capacity, etc.?

Jean-Pierre Clamadieu: Do you want to comment on the last one, on fixed costs, Karim?

Karim Hajjar: Sure. I mean, it's an important question, but there's no straightforward answer. I'd say there's nothing that particularly distorts our performance on fixed costs that you want to normalise out. Clearly, there are some efficiencies, some kind of learning curve impacts, as you ramp up, but nothing of note that I would say this would be helpful to you. And as I said, fundamentally, we continue to eat inflation through our existing programmes, and this is predominantly capacity-driven. Really, nothing comes to mind to shed more light on.

Jean-Pierre Clamadieu: And on your second question, we don't see any one-off. I mean, the only one we expected to have this year was this alignment of Cytec benefits onto Solvay policy, and Functional Polymers to try – to be clear, what I was referring earlier regarding sweet spots is more the inventory revaluation that we benefited from in the first half, which is likely to be reversed. We expect to continue with good pricing and good volumes, so I don't want to commit on the specific level of margin, but again, very good performance expected until the end of year from Functional Polymers.

Operator: Thank you. We have time for a few more questions. The next question is from Markus Mayer from Baader-Helvea. Sir, please go ahead.

Jean-Pierre Clamadieu: Hello, Markus.

Markus Mayer: Yeah, good afternoon, gentlemen. Several smaller questions remaining. First one again on Composites business. How do you see yesterday's statement of Boeing to do more work internally, in-house, therefore to reduce the dependency on suppliers?

Jean-Pierre Clamadieu: Boeing what, sorry?

Markus Mayer: Yesterday, Boeing said in their statement that they wanted to move work internally, and therefore reduce suppliers, or dependency on suppliers. Do you see any impact from this for your Composites business, or kind of business which has aerospace exposure?

Then the second question is on your comment on M&A and that you're looking for opportunities. Just a clarification question: am I right that you are focusing on really innovative specialty chemical opportunities, and not on things which are not really specialty, so like Akzo's business?

And then the last question, another clarification question. You said this lower tax rate is sustainable; I assume this is not true for the financial charge, am I right?

Jean-Pierre Clamadieu: Okay, so first question, frankly speaking, I don't see Boeing becoming a chemical company, so my understanding of why--I have not seen the specific announcement you're referring to is that we had a few difficulties in the 787 production, linked to the fact that we had a very complex supply chain with a lot of partners, so they might be referring to the fact that they want to re-source some elements from this supply chain. For Composites, they will need to continue to work with their existing suppliers, because there is no other practical option. So, I would probably welcome directionally the fact that they have a more simple chain.

Regarding M&A, just to be clear, I mean, I've said that significant M&A could only take the form of divestments in 2017. If you look at acquisitions, we are always interested in looking at add-on acquisitions which could allow us to increase our position in Advanced Materials or Advanced Formulations, either by bringing a new technology or bringing a specific market access. But this would lead to a small transaction, a couple of hundreds of millions, but even after having said that, I don't have currently on my desk any file of this size. So, don't expect us to be very active on the acquisitions side of the equation in the next 12 to 18 months. I think the focus is very much, when finalising the transformation, full divestment, if the opportunity arises. And second, very much focusing on internal improvement. I think there's a lot we can do to generate top-line synergies in Advanced Materials. There's a lot we can do to simplify the overall organisation of the company, and this is what we are currently focusing our efforts on.

Karim Hajjar: I think in your other two comments, Markus, one is on financial charge. It's clearly, as we generate the kind of cash levels we have, that yes, you can expect over time a reduction of financial charges. On tax rates, our strategic guidance is around 30%. We're not going to change it just opportunistically, but it's fair to say that when I see last year, 28%, when I see us in the first half at 26%, it's fair to say that for this year at least, coming in under 30% is a plausible outcome. But let's be clear: it doesn't take much to create 1% of variability. 1% is less than €50 million, so a relatively small change in our geographic pool of taxable profits can swing it. But I do feel that coming in under 30% is a realistic expectation at this stage, for this year.

Operator: Thank you. The next question is from Laurent Favre from Evercore. Sir, please go ahead.

Jean-Pierre Clamadieu: Hello, Laurent.

Laurent Favre: Hello, Jean-Pierre. Thank you, good afternoon, everybody. My two questions will be, number one, can you remind us on the FX transaction exposure what we should have in mind in terms of areas where you are exposed, areas where your competitive position might be at risk, including Functional Polymers, for instance?

And the second question on M&A: again, you hinted at further disposals, I think it's the second time on a quarterly call that you do that. Can you remind us of what's driving your decision? And in terms of timing as well, is it a matter of having your teams finding some time to do the disposals? Is it a matter of further work that you need to do internally to improve performance? Is it about the right valuation that you have in mind for those assets? Thank you.

Jean-Pierre Clamadieu: FX, Karim?

Karim Hajjar: I'm not sure I understood your first question in terms of business impact and FX. Can you maybe just repeat or clarify, please, Laurent?

Laurent Favre: Well, I'm thinking about the transactional exposure. And for instance, I'm thinking about polyamides where your key competitors are based in the US and would have a US dollar cost base.

Karim Hajjar: Sure. Now, I think fundamentally for our transaction exposure, we typically are hedged about 70–75% of our forward nine months. So, to the extent there is an impact, we have a significant degree of protection in place already, by virtue of the fact that we are hedged. So, whilst we don't welcome what is at the moment 1.18 dollar/euro, clearly we have an element of protection that would defer an impact for the short term, just to give you an example. Does that help at all, or do you have more in mind?

Laurent Favre: 2018, when we all do our forecasts tonight, do we all land or take out, ten cents times €12 million for EBITDA? And I'm just wondering if we should just play the sensitivity or if we should also think about volumes impact, as you may have to lose volumes because your competitors will just be able to gain share?

Karim Hajjar: Yeah, I think it's difficult to, let's say, try and really give an indication of how foreign exchange movements can impact demand dynamics. What I can tell you is the sensitivities: we indicated ten cents for the whole of Solvay is about €120 million a year on an annualised basis; roughly 60% conversion, 40% transaction if you ignore the hedging. So, to give you an order of magnitude, ten cents does give you roughly €10 million a month. Hopefully that helps you make your own assumptions. But I don't think that anybody can give you a reliable indication between FX and volumes.

Laurent Favre: Thank you.

Jean-Pierre Clamadieu: And maybe just to complement what Karim was saying on Functional Polymers: clearly, the units are running very close to full capacity, so I don't see much transfer of product from one region to the other. And we all have in mind the overall competitiveness of our chain, so I don't expect much disruption coming from the volatility of foreign exchange.

On M&A, I think if I understood well your question – in fact, there was a bit of static on the line when you talked – but our view is that we have currently a portfolio which fits very well with our expectation. I think we've built very strong growth engine in Advanced Materials, we have a very good position in Surface Chemistry/Advanced Formulation. The real challenge for us is to make sure that we work, one, on generating growth; we have a number of innovation projects or top-line synergy projects that we want to bring to fruition, and we need the resources to do that, one. Second, I think that there is a need for Solvay at this point of time to look at all the business support part of the organisation, and look at how we can align them very well with the current portfolio, the current business model and the current set of customers. This also is taking a bit of time and resources, starting with ComEx, and is the reason why I'm telling you: don't expect big movement in terms of acquisitions. I think the priority is really to increase or improve our position in the two growth engines that we have today.

I could see very specific opportunities to bring in new technologies: I don't know, a new polymer, for example, or buying a company which gives us specific access to some difficult to access markets. But this would be rather small opportunities. And yes, I think we need to get ready for maybe a next stage. But the next stage is, as I've said, a little bit distant in terms of timing.

Laurent Favre: Thank you.

Operator: The next question is from Patrick Lambert from Raymond James. Sir, please go ahead.

Patrick Lambert: Good afternoon, everybody. A few questions left, I think, and mostly still overlapping with the others. Regarding, again, Cytec: I think, if I remember correctly, at end of last year you were talking about stabilisation in H2, and return to growth more in 2018. We had plus two: would you venture though, in terms of growth rates going into H2 in next year, give us an update on where you see the platform? And I know it's complex, there's a lot of industrial versus commercial aircraft, but if you could help us in terms of the ramp-up of the overall platform, that would be one.

And second, on Functional Polymers: again, is there a risk of an inventory devaluation in Q3, or what we saw in Q2 already reflects that risk? Or it's mostly a Q3 story? And if you could quantify the impact, if any.

Jean-Pierre Clamadieu: I won't quantify the impact, but there will be some slight impact due to inventory devaluation. In this case, I mentioned that we had some inventory revaluation during Q2. But again, broadly speaking, the business will continue to perform well because the fundamentals are strong.

On composite, I would refrain from giving you a number in terms of expected growth rate. I think the inventory movements that we've seen last year are behind us. Now, what we see are the real impacts of what's happening in the programmes. I think with the equation, conceptually it's rather simple: strong growth in F-35, strong growth in LEAP, significant growth A320neo and Boeing 737 MAX, and some moderation in A380 and Boeing 777 until the 777X is launched. And then still some work to do in our part on the industrial material composite business, the non-aerospace where we had a bit of a, I would say, mediocre performance for the first half of the year. And it's an area where we need to fix things, either by improving the commercial performance or by adjusting our cost base, so we are working on that. So, I will ask you probably to be a bit patient before we give you a bit more visibility on what it means in terms of growth rate.

But clearly, we are going out of a difficult zone in which we were a year ago – when I say difficult, I don't want to overemphasise that, but I would say a challenging situation – where inventory reduction was playing against us. We think that this is behind us now, and we are back to growth rates which are close to what we were expecting when we made this acquisition.

So, maybe time to go for the last question.

Operator: Thank you. And our last question is from Chetan Udeshi from JP Morgan. Sir, please go ahead.

Chetan Udeshi: Yeah, hi. Thanks. Maybe one question on free cash flow, as you define it. So, how should we consider in terms of second-half dynamics? Would you say it will be broadly similar to last year, that we see working capital improvement being the key driver of improving cash flow? Because based on your full year guidance, CapEx will be up versus first half. So, number one question on the free cash flow generation dynamics for the second half.

And second question, just a clarification on butadiene re-entry revaluation effect: did you say you had some positive impact also in Q2? Because butadiene prices actually started coming down in second quarter, so why was there an incremental positive impact in Q2 over Q1? Thank you.

Karim Hajjar: On free cash flow, Chetan, the best I can describe it is this: all levers that have contributed to our cash will continue to be deployed. So, high profits, less CapEx, very clear focus and discipline on working capital. That's what I expect as being, call it, the recipe. It's nothing dramatic, nothing new, just more of what we've done in the past. There is almost an automatic outcome; the seasonal nature of our business, our patterns, results in that. And what we've done is confirm the guidance on a continuing business basis, so you eliminate the distortions of selling businesses like Acetow, Vinythai etc. So, we're looking on a clean, like-for-like comparable basis. I said this is going to be more than €800 million. And that is almost double-digit higher than the figure last year, that from memory was €735 million. So, we reconfirmed that, and that's exactly what we intend to deliver.

Jean-Pierre Clamadieu: Okay. Now, just on the butadiene: in fact, there was a bit of an exaggerated evaluation, but this was an H1 but mostly Q1 event. But again, not something major. It just supported a bit the performance of the business, and we expect again to see the other movement in the second half. But again, probably more importantly, good fundamentals in this business, both in terms of ability to price but also in terms of demand and volume.

So, maybe just a couple of words to close this call. I think these results demonstrate or confirm the momentum that we've seen in Q1. So, strong volume growth, ability to control margins and cost. And this is, again, a performance we are quite pleased with. The challenge is to continue, but the upgrades that we have done of our full-year guidance show that we are confident that we'll continue to deliver in the same direction. So, thanks a lot for having shared this time with us, and we'll back for the Q3 results in three months. So, thank you very much and have a very good day.

Operator: Thank you, Mr Jean-Pierre Clamadieu and thank you Mr Karim Hajjar. Ladies and gentlemen, this concludes the conference call. Thank you all for your participation, you may now disconnect.