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GRA - Q3 2018 W. R. Grace & Co Earnings Call

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OVERVIEW:

Co. reported 3Q18 sales of $495m and adjusted EPS of $1.11. Expects full-year 2018 adjusted EPS to be $4.00-4.05.

CORPORATE PARTICIPANTS

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Third Quarter 2018 W. R. Grace Earnings Conference Call. (Operator Instructions) As a reminder, this conference call is being recorded.

I would now like to introduce your host for today's conference, Mr. Jeremy Rohen, Vice President of Investor Relations. Sir, you may begin.

Jeremy F. Rohen - *W. R. Grace & Co. - VP, Corporate Development & IR*

Thanks, Joel. Hello, everyone, and thank you for joining us today for Grace's third quarter earnings call. With me this morning are Fred Festa, Grace's Chairman and Chief Executive Officer; Hudson La Force, President and Chief Operating Officer; and Bill Dockman, Vice President and Interim Chief Financial Officer.

Our earnings release and presentation are posted on our website under the Investors section at grace.com. Please note that some of our comments today will contain forward-looking statements based on our current view of our business, and actual future results may differ materially. Please see our recent SEC filings, which identify the principal risks and uncertainties that could affect future performance. We will discuss certain non-GAAP financial measures, which are described in more detail in this morning's earnings materials. Reconciliations of non-GAAP financial measures and other associated disclosures are contained in our earnings materials and posted on our website. This morning, Fred will address third quarter highlights and recent developments. Hudson will then provide an update on our key strategic initiatives and business performance, and I will cover our financial results.

So with that, please turn to Slide 4 in our earnings presentation, and I'll turn the call over to Fred.

Alfred E. Festa - *W. R. Grace & Co. - Chairman & CEO*

Great. Thanks, Jeremy, and good morning to everyone. Today we reported our third quarter 2018 financial results, and I'm very pleased with what our teams have accomplished. We continue to execute on the strategic plan that we presented at our Investor Day in March and are well positioned to deliver our commitments outlined in the 5-year financial framework.

Now let me give you some of the highlights from Q3 and our view for the full year. We had another solid quarter with double-digit sales growth and continued strength and momentum across all of our businesses. Sales were up over 15% year-over-year, including 8% organic growth and 7% from the polyolefin catalysts acquisition. Our strong top line growth, the earnings contribution from the acquisition and continued execution by our commercial and operations teams contributed to a 13% increase in adjusted EBIT year-over-year. We delivered another quarter of solid earnings growth, despite the headwinds from last year's insurance recoveries that did not repeat this quarter.

Over the past 2 quarters, there's been a lot of attention around possible impacts of inflation and tariffs across the chemicals industry. In our case, we have experienced some inflation across our supply chain, which we've been able to mitigate through pricing and supply chain actions, and we've had virtually no effect from the tariffs between the U.S. and China. Our continued execution gives us full confidence in delivering our 2018 outlook. We are raising our adjusted EPS in the range of $4 to $4.05 per share.

Looking out to 2019 and beyond, we expect to continue to drive top line growth, earnings and generate cash flow needed to fund our investments. Hudson will give you more details on 2019 in a moment.

When I joined Grace 15 years ago, one of my top priorities was resolving the company's asbestos liabilities. As you all know, coming out of bankruptcy in 2014, the last major milestone was the resolution of the environmental remediation at our former vermiculite mine in Libby, Montana. I'm pleased to report that after nearly a decade of work, we have reached the point where we can estimate the future remediation cost. Today, we announced that we have recorded a $70 million noncash pretax charge. This is our best estimate of the cost to remediate the mine site.

From a cash flow perspective, we expect the remediation to be quite manageable, as spending is expected to occur over a decade or so with most beginning in or after 2022. Importantly, based on the anticipated spending for the mine and dam, and the runoff of existing environmental spend, our environmental cash flow spend should remain about $10 million to $20 million annually over the next 10 years. It is clear this will not have an impact on Grace's growth plan or overall capital allocation strategy.

Before I turn the call over to Hudson, I'd like to share a few thoughts on my final earnings call. Our strategy is sound. We are executing well, and I believe this will ultimately create significant value for our customers, our shareholders and our employees. As I previously announced, I will retire as CEO of Grace on November 8. I'm excited for Hudson to become the CEO. We have spent the better part of the last year working to ensure the transition is seamless. Hudson has the full support of the board, and we are all confident in Grace's future under his leadership. I'm looking forward to my next phase with Grace as nonexecutive Chairman and as a shareholder of this great company.

And with that, I'll turn the call over to Hudson.

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Thank you, Fred. Before I get started, I want to recognize Fred for his leadership of the company these last 15 years. For me personally, and on behalf of our board and our 3,900 employees, thank you, Fred.

Grace is a dramatically different company and a dramatically better company because of your leadership. You made a very significant difference.

Please turn to Slide 6. We had another quarter of solid demand and earnings growth and remain upbeat about our future. Our businesses are well positioned in high-value markets with good industry structure and sustainable growth drivers. Growing demand for plastics, petrochemical feedstocks and cleaner fuels plus growing household income, stricter environmental standards and increased focus on health and wellness, all support profitable 4% to 6% organic growth for our company. We are focused on capturing this growth and monetizing it. Leveraging the Grace

Value Model, we are investing in innovation, commercial capabilities, manufacturing capacity and our people to ensure we are delivering value for our customers and our shareholders. As an example, our focus on customer-driven innovation led us to develop a new manufacturing technology for a key consumer pharma customer. Over 2 years, we expect this one product to add more than 2 points of growth to our Materials Technologies business at an attractive return.

In addition, implementation of the Grace Manufacturing System continues to improve our effectiveness and cost position. Two of the 5 plants currently implementing GMS have already delivered 1-year payback on their initial investment and the other 3 are on track to pay back their investment next year. One example of commercial and operating excellence working together is the rebalancing of our earnings profile in 2018. In recent years, our earnings have been more weighted to the second half of the year. This year, we have made an effort to better balance the year as one element of improved operating excellence. This will help us plan and manage our manufacturing operations in a more effective manner going forward.

Please turn to Slide 7, and I'll address our updated outlook for 2018 and touch on 2019. For 2018, we are raising our adjusted EPS outlook to $4.00 to $4.05 per share from $3.90 to $4.00 per share. We are narrowing our full year adjusted EBIT outlook to $453 million to $457 million, and our adjusted free cash flow outlook to $230 million to $240 million. For 2019, we expect to deliver another solid year, with financial performance in line with our 2016-2021 financial framework. We think earnings growth should be better than the framework based on good demand momentum and the commercial excellence and operating excellence work we've done this year. As usual, we will provide our full 2019 outlook when we report Q4 earnings in February.

Our 2019 views include our current assessment of macroeconomic conditions. Most importantly, we expect solid organic growth, driven by good customer demand for our technologies and improved pricing. We feel confident in the strength of our businesses. We do expect raw material and energy cost inflation to continue into 2019. As always, we use our supply chain flexibility and capabilities to minimize our input costs. As a reminder, our top 5 input costs are aluminum, caustic soda, natural gas, rare earth and sodium silicate. I should also point out that we have minimal exposure to oil-based materials such as solvents, which are only about 3% of our spend. Importantly, we have limited exposure to tariffs, emerging market currencies and interest rates. We export less than 4% of our sales from the U.S. to China. At this point, we have not experienced any significant effect from U.S. or Chinese tariffs on our sales or input costs. While we sell to customers all over the globe, about 95% of our sales are denominated in U.S. dollars, euros or currencies tightly linked to those 2 currencies. We certainly have exposure to the euro, but our exposure to emerging market currencies is less than 2% of sales.

Finally, regarding interest rates. In Q2, we increased the fixed-rate component of our long-term debt to 85% to reduce our exposure to rising interest rates. With all of these factors considered, we are well positioned to manage the impacts of macro risks to our business and continue delivering strong results.

Now let's turn to Slide 9 and review our business results for the quarter. Catalysts Technologies had another good quarter, with sales up over 19% on strong demand and improved pricing plus a solid contribution from the polyolefin catalysts acquisition. In Specialty Catalysts, we continue to see strong demand for our catalyst and licensing technologies. With our broad, highly differentiated technology portfolio, we are well positioned to be our customers' most capable innovation partner.

Organic sales grew nearly 10% this quarter. We announced another UNIPOL polypropylene process license, and the pipeline for future licenses remains strong.

In Refining Technologies, sales were up over 4% this quarter, and we continue to see good results from our value selling activities. FCC catalyst prices are now on track to improve over 200 basis points this year, consistent with our multiyear framework of 1% to 2% per year. We expect to continue our value selling and customer and product mix improvement efforts next year, including resuming supply to one of our largest customers as they restart their FCC unit operations after 2 years shut down.

Hydroprocessing catalyst demand remained solid. Our healthy backlog and the continued growth in clean fuel demand, driven by IMO 2020, support our long-term view for strong growth in our arc joint venture. Our new HPC catalyst capacity continues to progress towards its Q4 2019 startup targets.

As we highlighted at our Investor Day, we are focused on shifting our catalyst business mix towards petrochemicals and clean fuels, and we expect that those end markets will account for over 70% of our catalyst sales in 2018.

Please turn to Materials Technologies on Slide 10. MT continues to perform well and is well positioned to capture the growth opportunities created by growing global middle class, stricter environmental standards and increased focus on health and wellness. Our proven innovation capabilities, balanced specialty portfolio and global footprint support mid-single digit growth in this business. Sales were up for the quarter 4% as reported and almost 6% on constant currency on higher sales volumes and improved pricing. Silica sales remained strong, led by higher consumer/pharma demand. As we previewed last quarter, the MT business was affected by plant turnarounds at 3 manufacturing sites during the quarter. These turnarounds limited silica sales volumes and reduced segment margins in Q3.

In closing, demand for our high-value product technologies remains strong, and we are executing well across the company. I am confident in our 2018 finish, our 2019 opportunities and our ability to generate the long-term profitable growth that will drive shareholder value creation.

I'll now turn the call to Jeremy who will discuss our financial results in more detail.

Jeremy F. Rohen - *W. R. Grace & Co. - VP, Corporate Development & IR*

Thanks, Hudson. I'm on Slide 12. The third quarter sales were up 495 -- sales were $495 million, up 15.2% as reported and up 15.9% on constant currency. Sales were up over 8% organically on higher sales volumes and improved pricing. Adjusted gross margin was up 140 basis points for the quarter, with pricing, supply chain and manufacturing actions more than offsetting inflation. Adjusted EBIT of $123 million was up 13.4% year-over-year. Adjusted EBIT margin of 24.8% was down 40 basis points year-over-year, primarily due to the 280 basis point headwind from insurance recoveries, which was largely offset by higher gross profit and income from our ART joint venture. Adjusted EPS was $1.11 per share, up $0.21 per share, driven by a $0.19 increase on solid business performance. Year-to-date, adjusted free cash flow was $174 million, down 30% versus last year and in line with our prior communications to you about our investments to support our strategic growth and productivity initiatives.

Adjusted EBIT ROIC was 20.6%, down year-over-year as a result of the acquisition in Q2. This measure will naturally increase as a full year of the earnings from the acquisition are realized. Sequentially, it was up 20 basis points.

Now let's turn to Slide 13, and I'll touch on capital allocation. As you know, we have a very disciplined capital allocation strategy with clear priorities for investment. First, we will invest capital in high-return organic growth opportunities and to acquire synergistic bolt-on businesses to build our technology and manufacturing capabilities. And second, we will continue to return cash to shareholders through dividends and share repurchases. As we've discussed throughout the year, 2018 and 2019 include increased levels of capital investment to execute our multiyear investment program, which will accelerate our growth, extend our competitive advantages and drive operating excellence. Year-to-date, we've invested $162 million in capital projects and continue to forecast approximately $200 million for the full year. In Q3, we returned $26 million of cash to shareholders, $16 million through cash dividends and $10 million in share repurchases. Year-to-date, we have returned approximately $110 million of cash to our shareholders.

With that, I'll turn the call back to Fred for closing remarks before we open the lines for questions.

Alfred E. Festa - *W. R. Grace & Co. - Chairman & CEO*

Thanks, Jeremy. I'd just like to take a minute to thank all of the shareholders who have trusted -- who trust us as a management team with their investment, and the analyst who cover our company and help educate the investment community about our story. I truly appreciate the time and energy you spend to learn about Grace. As I said at our Investor Day, the thoughtful insight -- the thoughtful, insightful, and quite often, challenging questions you've asked me have made me a better CEO and leader and our company, a stronger competitor.

With that, those are our prepared remarks, and we'll open the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Robert Koort with Goldman Sachs.

Christopher Mark Evans - *Goldman Sachs Group Inc., Research Division - Associate*

This is Chris Evans on for Bob. Just curious about your guidance. Is there anything about 4Q seasonality or market trends that's leading you to only increase the full year guide by amount similar to the third quarter beat? And then regarding the low double-digit EPS guidance for '19, just curious how much or how long of a year are you expecting hear to clear FCC customer to be on for?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Chris, it's Hudson. For Q4, part of what you are seeing in Q4 is the effect of some inventory accounting as we do the final integration of the polyolefin catalyst acquisition. And as we -- as I talked about in my prepared remarks, the way we've rebalanced the year operationally, there's no loss in momentum. We expect good Q4 sales growth. It's really mostly on our inventory accounting. For next year, I -- we've told investors that they should assume we begin resupply to that customer in the second quarter, and I think that remains our view.

Christopher Mark Evans - *Goldman Sachs Group Inc., Research Division - Associate*

Great. And then just as a customer ramps up, can you walk us through how you're planning to meet the incremental volume requirements? Is there any debottlenecking opportunities? Or are you going to be having to adjust your volumes to make room like you did a few years ago when you were to make some sizable customer adjustments?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Yes, thanks, Chris, a good question. We -- I would expect today that we would take some of that opportunity as incremental volume, but most of it is mix shift. It's a powerful opportunity for us to upgrade our portfolio, and we want to make the most out of that.

Operator

Our next question comes from Chris Parkinson with Crédit Suisse.

Christopher S. Parkinson - *Crédit Suisse AG, Research Division - Director of Equity Research*

You hit on this a little bit, but can you break down the specialty catalyst volume trends based on the growth rate in the quarter and just give us a little insight on how to interpret that into '19? And then also, on the price mix fronts from what you see in the second half of this and once again into '19, what are the key puts and takes which we should be thinking about outside of Takreer, especially anything on the licensing front?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

So Chris, it's Hudson again. We're seeing strong growth in all product categories in our specialty catalyst business, including the acquisition. And I don't mean just the acquisition effect itself, but that business is performing well. Look, at the end of the day, this is driven by 3 or 4 things. One, obviously, at the base level, the demand for plastics on a global basis, but what drives incremental performance for us is the licensing capability that we have that you mentioned, the innovation capabilities that we have with our customers, we're able to do things for our customers that our competitors can't do. And the fact that we're not a competitor with our customers. Being a merchant catalyst supplier, I think, gives us advantage in the marketplace as well. As we look forward to 2019, our guidance to you would be the same as what we've said. We expect high single-digit growth from this business during the term of this financial framework, driven by all of those factors.

Christopher Mark Evans - *Goldman Sachs Group Inc., Research Division - Associate*

And just, I hate to phrase it this way, but in terms of where your stock price is now, it just -- and given your outlook and, let's say, soft outlook for '19 and even into '20, what are you most excited about that you think investors are missing? I mean, is it something on licensing? Is it FCC, HPC catalyst trends? IMO 2020? Just -- and what -- just to give a little more insight on what underscores your optimism would be very helpful.

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Chris, we could spend the rest of the call talking about the things I'm optimistic about. I -- the strong strategic positions of these businesses, we've worked so hard to build the capabilities to innovate, to support our customers, their specific growth drivers, you mentioned a couple of them, demand for plastics, this innovation capability that we have, demand for petrochemical feedstocks coming out of refiners is driving incremental growth for us. IMO will sustain the high growth rate that we're enjoying in ART. The MT business is developing new growth opportunities, new target segments, I mentioned one of those in my prepared remarks. And that's on the top line. We are working hard on an operating excellence focus. We've made a lot of progress. We're not done with those efforts. We've got several years left to go, you all call it self-help sometimes. That's a self-help initiative that we started in real earnest 12 or maybe close to 18 months ago. And I think the other part which we tried to address this morning, as a participant in the chemical industry, we do have exposure to inflation. We clearly operate on the global basis, but our risk profile on those fronts aren't the same as for other companies. And I think -- I hope the data we gave you all this morning helps frame that for you.

Operator

Our next question comes from John McNulty with BMO Capital Markets.

John Patrick McNulty - *BMO Capital Markets Equity Research - Analyst*

Fred, best of luck to you and thanks for all the help over the years.

Alfred E. Festa - *W. R. Grace & Co. - Chairman & CEO*

Well, thanks, John.

John Patrick McNulty - *BMO Capital Markets Equity Research - Analyst*

It just -- I guess, a couple of things. On the materials tech side, you'd indicated that the turnaround impacted the volume. Can you quantify that to some degree as to how we should think about what the normalized volume growth is in that business right now?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Yes, it was mid-single-digit millions type of effect, John. We -- while these plants were down, we're obviously not producing product, and that had a little effect in Q3.

John Patrick McNulty - *BMO Capital Markets Equity Research - Analyst*

Got it. And that won't drag into Q4, is that right?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Correct. Yes. All 3 plants are up and running now, and [whereby] late July or early August maybe.

John Patrick McNulty - *BMO Capital Markets Equity Research - Analyst*

Got it, okay. And then with regard to inflation, do you feel like between the pricing and some of the hedging that you had, did you catch up entirely to kind of the inflationary pressures that you were seeing? And I guess, how should we think about that in 2019 with some of the puts and takes with aluminum prices may be moving higher, costs are coming off, like, I guess, how should we be thinking about that going forward?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

You think by the end of this year, we will have caught up pricing versus inflation. And as we think about 2019, we do think inflation will continue. Obviously, our pricing efforts will continue. How that balances exactly, I'm going to wait until February to be more specific, John, but you can be sure that we're continuing to drive all the things that mitigate inflation, not just on the pricing side but productivity as well.

John Patrick McNulty - *BMO Capital Markets Equity Research - Analyst*

Got it. And then maybe just the last question. With regard to, I guess, your efforts to reduce some of the seasonality that you spoke of, I guess, just thinking about your customer base and how some of them take downtime and that's when you're loading in, I guess, how do you effectively do that?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

The only real seasonality we see is in Q1 when refiners often take turnarounds to reset their production strategy. That's fairly small, frankly. It might be a percentage point or 2 on full year sales at the company level. This is more about level loading our factories, being better at managing our planning horizon in terms of production planning and things that are pretty tactical inside our planning manufacturing operations.

Operator

Our next question comes from Kevin McCarthy with Vertical Research Partners.

Kevin William McCarthy - *Vertical Research Partners, LLC - Partner*

Hudson, as the MARPOL time line is creeping up on us, would you provide some color as to the nature of your conversations with customers? And what the near- to medium-term outlook is for both volumes and contributions from your ART equity earnings as we move through that transition?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

You bet, Kevin. The -- from a customer perspective, our customers either are already making investments in their refining operations to take advantage of this or are actively considering, many of our customers. And we have a fair degree of visibility to those plans that our customers have, either through our direct relationships with them or through the licensing arrangements that we have through the CLG joint venture. There's a lot of activity here. Our customers are investing to take advantage of the tighter fuel regulations. Ultimately, that will show up as demand for hydroprocessing catalysts. Hydroprocessing catalysts are a very economic strategy for taking sulfur, either out of the crude itself before its processed or out of the refined products themselves. We think that translates into continued strong growth in the ART joint venture, not just to 2020 but well through 2020 and into the next decade. This will have some benefit in our FCC catalyst business as well as refiners reoptimize their refining operations. We expect some opportunity to help them do that with better FCC catalyst technologies that will help them, either maximize diesel production in their FCC units or make other adjustments as they reoptimize their refineries.

Kevin William McCarthy - *Vertical Research Partners, LLC - Partner*

That's helpful. And then as a second question, obviously, investors across the chemical sector have been concerned about the ongoing trade war with China. You've characterized your U.S. exports to China as less than 4% of sales. Would you provide a bit more color as to where that exposure resides across the portfolio? And also, what the plan of action might be in terms of alternatives and optionality if the backdrop continues to get more severe?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Sure. We sell into China in all 4 of our business units. FCC catalyst, ART, MT and SC, so the -- it is part of all 4 of our businesses. We have a number of different levers. If any of our products became subject to tariffs, we can move manufacturing operations outside of the U.S. to other plants, our plants in Europe or plants in Asia. That's one lever that we would pull. In some cases, customers would not want to switch. These are high-value products sold in the specialty end uses and sometimes our products are specked into our customers' products. There may be a situation where the tariff just has to be absorbed. The other lever, if we did lose some sales in China, we are actively working on developing demand in other regions of the world to make sure that, that doesn't pass through to the business unit that it would -- you'd see it as geography mix shift or customer mix shift.

Operator

Our next question comes from Mike Sison with KeyBanc.

Michael Joseph Sison - *KeyBanc Capital Markets Inc., Research Division - MD & Equity Research Analyst*

Fred, congrats again, and I'm happy to see you end on a good note. You were one of the very few companies who have -- who actually had expectations and beat expectations and raise your outlook. So Hudson, in terms of 2019, your guidance or your soft guidance is 4% to 6% organic growth, but top line is a little bit better. Does that assume more acquisitions? Or does that include the acquisitions that you've already completed?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

There are no acquisitions in those numbers, Mike. We've got one more quarter of the polyolefin catalyst acquisition, but nothing in the future. That said, that's the assumption that's in those numbers. We are actively working our pipeline as we do, we've got some interesting small bolt-on opportunities that we're working on as we speak. That part of our growth strategy is still very important to us.

Michael Joseph Sison - *KeyBanc Capital Markets Inc., Research Division - MD & Equity Research Analyst*

Great. And then about the same time last year, you announced some price increases for FCC. I haven't seen anything, maybe I missed it, but do you feel pretty good about another round of price increases heading into '19?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

It is high priority for us, Mike, and I do feel good about it.

Operator

Our next question comes from Mike Harrison with Seaport Global Securities.

Michael Joseph Harrison - *Seaport Global Securities LLC, Research Division - MD & Senior Chemicals Analyst*

Hudson, was wondering if you could talk just a little bit more detail about the turnarounds that were going on during the third quarter. I know that some of your manufacturing has overlaps between both the materials business and the catalysts business. So you quantified the impact on materials, but was just wondering, was there any impact at all on your catalysts business from the turnaround?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Yes, Mike. One of the plants also manufactures catalysts products, but frankly, the effect was too small to really call attention to it.

Michael Joseph Harrison - *Seaport Global Securities LLC, Research Division - MD & Senior Chemicals Analyst*

And there was no impact on volume, your volume capability?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Well, the catalyst -- I think on the catalyst business, I'd say no impact on volume, some small impact on margins, but again, I think it's too small to call attention to it.

Michael Joseph Harrison - *Seaport Global Securities LLC, Research Division - MD & Senior Chemicals Analyst*

All right. And then I was wondering on the tariff front, you kind of mentioned that the impact -- the direct impact is relatively low. Just wondering, are you have -- do you have customers that are seeing impacts? And are you maybe seeing some opportunities, either in China or outside of China, where potentially you could displace competition as there are changes that go on with the tariffs?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Well, the -- whenever there is a marketplace dynamic like this, it creates opportunities and it's how we like to think about it. We have very close customer relationships on the technology side. As they think about these strategies for their business, often times, they come to us to help them address those issues. In terms of big effects, we're not seeing anything right now. One of the advantages of our approach is, we run our businesses on a truly global basis. And as demand rises or falls in any one market based on whatever factor, we're very able to nimbly adjust by focusing on opportunities in other markets.

Operator

Our next question comes from John Roberts with UBS.

John Ezekiel E. Roberts - *UBS Investment Bank, Research Division - Executive Director and Equity Research Analyst, Chemicals*

Can you hear me?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

We can hear you, John.

John Ezekiel E. Roberts - *UBS Investment Bank, Research Division - Executive Director and Equity Research Analyst, Chemicals*

I believe you hedge your alumina clocks. Are you hedging a year forward still? Or are you going to let that go to the spot market? And then, even though we haven't had tariffs on rare earths, are the majority of your rare earth purchases still coming from China? They're a large supplier there.

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Yes. We do maintain that hedging program. It has historically been a rolling 12-month program. We extended it early this year, maybe mid this year to be 18 to 24 months. And on rare earth, yes, we do continue to source most of our rare earths from China. That has not been a significant source of inflation for us at this point. And the other thing I should add if something were to happen on rare earths around tariffs, we do still have the technology we developed a few years ago to manufacture no rare earth catalysts. That technology is on the shelf and ready to go if we ever needed it. This is a number of years ago now, but you all may remember when we introduced that technology, it was very rapidly adopted by our customers at the time and the technology performed very, very well compared to the prior rare -- the prior catalyst with rare earth content.

Operator

Our next question comes from Laurence Alexander with Jefferies.

Laurence Alexander - *Jefferies LLC, Research Division - VP & Equity Research Analyst*

Two quick ones. Could you just clarify with respect to the sort of bump in orders that you're seeing related to the IMO 2020 regulations, do you see this as a step up in your run rate? Or do you see it as a -- sort of a more -- sort of a bit of a hill where as the industry adjusts, we'll have to give some of the volume back? And secondly, can you give a little bit of more granularity about what you're seeing sequentially in Materials Technologies for Q4 through the next couple of quarters relative to the full year outlook? I mean, are we seeing a bit of a dip for that business? Or is it going to be a pretty sustainable run rate from here?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Lawrence, on your IMO 2020 question, I think I don't see this is as a bump, I think -- I see it as an extension of the high growth rates that we've had. This is -- IMO 2020 is a specific regulatory change, but it's just -- it's one more chapter in a long story about cleaner fuels regulations. And I don't think that book has finished, sorry if that's a bad analogy. On Materials Technologies, sequentially, we expect growth from Q3 to Q4, and we expect that business to grow mid-single digits next year. I'm not going to give any more specific color at this time. We'll talk about 2019 in February.

Operator

Our next question comes from Chris Kaps with Loop Capital Markets.

Christopher John Kapsch - *Loop Capital Markets LLC, Research Division - MD*

Fred, thanks for your comments and just congrats again on your retirement. Best of luck on the future endeavors.

Alfred E. Festa - *W. R. Grace & Co. - Chairman & CEO*

Thanks, Chris.

Christopher John Kapsch - *Loop Capital Markets LLC, Research Division - MD*

And -- so I had a couple of follow-ups with -- on the catalyst side. The one question specifically was on the pricing initiative. It looks like you're just sort of declaring victory on the success called 200 basis points this year in FCC pricing. I'm just wondering if you look to '19, if there wasn't the benefit of the Abu Dhabi customer ramping, would you expect a similar sort of step up in pricing, all else equal apples-to-apples, with your portfolio customers? In other words, is the Abu Dhabi customer going to be an increment to the pricing variances that you are -- and trajectory that you're seeing in FCC catalyst?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

We will benefit -- there will be a mix benefit as that customer comes fully online next year, Chris. That's right.

Christopher John Kapsch - *Loop Capital Markets LLC, Research Division - MD*

But it was expected the 1% or 2 percentage points of pricing benefit per year didn't necessarily contemplate that one customer contributing positively to the mix. (inaudible)

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Yes, the 1% to 3% a year is meant to be a multiyear view, and there'll be years where it's higher than that, there may be years where it's lower than that. That's how we want you all to think about it. Just like this year, we expect to outperform that metric. There may be years in the future where we outperform that metric, and I'm not going to -- I don't want to get into 2019 any more than that. But we remain -- I mean, the number that you all have asked about at this morning, we remain very bullish about the business next year. We are very focused on continuing to execute on the pricing side.

Christopher John Kapsch - *Loop Capital Markets LLC, Research Division - MD*

Okay. And if I could just follow-up a couple of things on IMO 2020. The -- you have a new HPC facility being built in Louisiana. I think you've characterized that as already sold out. So I'm just wondering, could you just update us on the timing? And what sort of incremental benefit to ART would you expect to see from that? And when does that flow through? And then you mentioned sort of a potential peripheral benefit from -- to the FCC catalyst business from IMO 2020. So what I'm curious about is as these refiners are shifting their configurations to produce more low-sulfur, middle distillates, more low-sulfur distillate, did -- in terms of the benefit to FCC, is it a different type of catalyst that they will have to use to optimize? Or is it just potentially running that FCC unit harder, and therefore, consuming more FCC catalyst?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

You've made some great points. I'll start where you finished. On the FCC side, your intuition is right. Customers will run those units harder and there'll also be some reoptimization. Different customers are going to have different strategies, depending on their geographic location and their overall refinery complexity. But in general, when customers look to reoptimize their refinery, an important part of that is the catalyst. And when we bring them a new technology, 95 times out of 100, that's a higher value product, and we capture that in products and margins. And I'm sorry, Chris, I'm forgetting the first part of your question. I think I...

Christopher John Kapsch - *Loop Capital Markets LLC, Research Division - MD*

Just the timing of Lake Charles.

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Oh, thank you, on Lake Charles. The material financial benefits will show up in 2020. We think that plant will come on late '19, so you should think of it as 2020.

Operator

(Operator Instructions) Our next question comes from Roger Spitz with Bank of America Merrill Lynch.

Roger Neil Spitz - *BofA Merrill Lynch, Research Division - Director and High Yield Research Analyst*

Can you comment on -- Kevin already given it on FCC catalyst volume growth in the third quarter. How should we think about that?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

We had good growth in the third quarter. It was low single digits. And -- but we're seeing a lot of good activity from our customers right now.

Roger Neil Spitz - *BofA Merrill Lynch, Research Division - Director and High Yield Research Analyst*

And with the restart of the Middle East customer, will you revisit whether you build that midsize FCC catalyst facility in the Middle East?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

That is definitely part of our thought process. We want to make sure that, that investment is timed with clear market demand or requirements. I will tell you that, that's bigger than just any one customer. We've actively been managing the timing of that investment to ensure that it coincides with the clear market demand signal. And -- but it is something that we're -- we revisit on a continuous basis.

Roger Neil Spitz - *BofA Merrill Lynch, Research Division - Director and High Yield Research Analyst*

And lastly, a small, but is pharma fine chemicals, is that EBITDA positive or nicely positive business?

Hudson La Force - *W. R. Grace & Co. - President, COO & Director*

Yes, it is.

Operator

I'm not showing any further questions at this time. I would now like to turn the call back over to Jeremy Rohen for any closing remarks.

Jeremy F. Rohen - *W. R. Grace & Co. - VP, Corporate Development & IR*

Thank you, Joel. Thank you, everyone, for your time today and your interest in Grace. We look forward to seeing some of you at the Baird conference in November and continuing to engage with you throughout the year and into 2019. Thank you, and have a great day.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This does conclude today's program, and you may all disconnect. Everyone, have a great day.