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GRA - Q3 2013 W. R. Grace & Co. Earnings Conference Call

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OVERVIEW:

GRA reported 3Q13 sales of $771m and adjusted diluted EPS of $1.07. Co. expects 4Q13 sales to improve sequentially with improvement in catalyst sales.

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the third-quarter 2013 W.R. Grace & Co. earnings conference call. My name is Shaquanna, and I will be your coordinator for today. (Operator Instructions)

I would now like to turn the presentation over to your host for today's call. Mr. Mark Sutherland, Vice President of Investor Relations. Please proceed, sir.

Mark Sutherland - *W. R. Grace & Co. - VP, IR*

Thank you, Shaquanna. Hello, everyone, and thank you for joining us today, October 23, 2013, for a discussion of Grace's third-quarter 2013 results, released this morning. Joining me on today's call are Fred Festa, Grace's Chairman and Chief Executive Officer; and Hudson La Force, our Senior Vice President and Chief Financial Officer.

Our earnings release and the corresponding presentation are available on our website. To download copies, go to grace.com and click on Investor Information. Links are available on the upper right corner of the page.

As you know, some of our comments today will be forward-looking and are made under the Private Securities Litigation Reform Act of 1995. Actual results may differ materially from those projected or implied, due to a variety of factors. Please see our recent SEC filings for more details on the risks that could impact Grace's future operating results and financial condition.

We will also discuss certain non-GAAP financial measures, which are described in more detail in this morning's release and on our website. Reconciliations for the most directly comparable GAAP financial measures and other associated closures are contained in our earnings release and on our website. Our comments on forward-looking statements and non-GAAP financial measures apply both to the prepared remarks and to the Q&A.

We want to remind everyone that this webcast contains time-sensitive information that is accurate only as of today. Any redistribution, retransmission, or reproduction of this call without Company consent is prohibited.

And with that, I'd like to turn the call over to Fred.

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Thanks, Mark. And good morning to everyone, and thank you for joining us.

I am pleased with our third-quarter results. Materials Technologies and Construction Products delivered good sales growth and terrific earnings growth. Sales in Materials Technologies increased 3%, and earnings increased 18%. Our strength in product technology applications development are driving improvement in both price and mix, while our disciplined operating approach drives manufacturing productivity and good expense control.

Sales in Construction Products increased 5% and over 8% organically. Earnings increased 24%, and operating margins increased 250 basis points year on year. This strong earnings growth comes from higher sales in North America, very good operating leverage, and all of the restructuring actions we've taken over the last few years.

In Catalysts Technologies, we achieved our sales and earnings targets in a tough quarter and made great progress with our new FCC catalysts. As you recall, these new technologies improve shale oil processing, heavy resid processing, and propylene production.

Last quarter we highlighted a number of new products that we are just beginning to introduce. Since then, feedback from our customers has been positive, and we're started receiving orders for the fourth-quarter deliveries. One example -- we recently launched a new catalyst family under the Achieve brand name.

This suite of products is targeted at maximizing C4 olefins and octane, a common deficiency when conventional catalysts are used with shale oil feedstocks. Customer trials been successful, and we expect to begin shipments in the fourth quarter.

Two weeks ago we announced an agreement to acquire the UNIPOL polypropylene licensing and catalyst franchise. UNIPOL is a strong business and a great strategic fit with our existing polypropylene portfolio. The people are very well regarded in the industry, and we are excited to welcome them to the Grace team.

The technology significantly strengthens our core capabilities in polypropylene. We have received positive feedback from our customers, who see this as an opportunity to work even more closely with us. We agree, and we expect the acquisition to lead to new business opportunities in the future.

We remain subject to a confidentiality agreement until closing and cannot comment on the UNIPOL financials or valuation metrics until then. I know you want them. You want more information on the business, and we will disclose additional details after closing. We expect to complete our regulatory findings this week and expect to close before year end.

$500 million is a significant investment for Grace. It was important to me that this investment met three key criteria. First, it had to be core to our business. Second, it had to produce returns in line with our overall investment profile. And third, it had to produce hard dollar cost and capital synergies.

We are confident we can successfully integrate this business and have strong plans for growing this franchise in the years to come. This investment will increase our leverage ratio but does not change our intention to return cash to shareholders after emergence.

Let me turn to 2014 for a moment. In our second-quarter call, we lowered our 2014 macro growth assessment to match the 2013 growth rates. Since then we have seen signs of improved growth in North America and Europe. We've also seen some slowdown in the emerging regions.

Over the next two months, we will continue to assess the macroeconomic environment as we complete our 2014 plans. Despite the shifting macro environment, I really like what we are doing to improve the growth in the year ahead.

Our growth programs continue to progress. North American and European commercial construction markets are showing signs of better growth; and, of course, the FCC catalyst business will show growth after a very tough 2013. As always, we will continue to focus on those things that we can control -- driving our product technologies to the next level, serving our customers well, and achieving our productivity goals.

We will provide you with full 2014 outlook will we release fourth-quarter earnings in February.

Before concluding my comments, I would like to bring you up-to-date on our bankruptcy. We have completed the Third Circuit process for four of the five appeals. We are still waiting for the Third Circuit to rule on the default interest appeal.

For the four appeals that are complete at the Third Circuit, the deadlines for any appeals to the Supreme Court are December 3 and 4. At this point we do not know whether anyone will appeal. Because of this, and given where we are in the year, we can no longer reasonably expect to emerge this year.

If there are no appeals to the Supreme Court and we have a ruling on the default interest issue, we would expect to emerge by the end of January. If there are appeals filed, our emergence would be delayed, probably two to three months. We think it is very unlikely the Supreme Court will hear any of these appeals, but we think it would take two or three months for any of these appeals process to conclude. We should know more by December 5, and we will update you at this point.

I will now turn the call over to Hudson.

Hudson La Force - *W. R. Grace & Co. - CFO & SVP*

Thank you, Fred. Our third-quarter and year-to-date results are summarized on Pages 5 through 7. I will comment on a few highlights at the Grace level and then discuss the three businesses.

Sales in the quarter were $771 million, down less than 1% from last year. Base pricing and sales volumes both increased about 1% but were more than offset by lower rare earth surcharges and unfavorable currency translation. Sales growth generally improved in the developed markets but slowed in the emerging regions after many quarters of double-digit growth.

Adjusted EBIT was $131 million, an increase of just over 1% from last year. Gross margin improved 20 basis points. Adjusted EBIT margin improved 30 basis points, and adjusted EBITDA margin improved 40 basis points, driven by strong performance in Materials Technologies and Construction Products and despite weaker sales in Catalysts Technologies.

Adjusted free cash flow was $239 million for the nine months compared with $286 million last year. 2012 benefited from a significant reduction in working capital resulting from the decline in rare earth costs last year. Rare earth costs continued to decline this year, but more slowly.

Adjusted EBIT return on invested capital was 33.8% on a trailing four-quarter basis compared with 34.6% in the prior-year quarter. Adjusted EPS was $1.07 per diluted share, which includes a $0.04 benefit from a lower effective tax rate.

Let's turn to Catalysts Technologies on Page 8. Third-quarter sales for Catalysts Technologies were $274 million, down 8% from last year. FCC catalyst sales declined 15%. Sales volumes declined 7%, and the decline in rare earth costs reduced sales by about 8%. The sales decline was in line with our expectations at the beginning of the quarter.

Specialty catalyst sales increased, driven by 12% higher sales volumes, better pricing, and favorable currency translation. Strong sales of polyethylene catalysts and chemical catalysts more than offset lower polypropylene catalyst sales, resulting from the conclusion of a large supply contract earlier this year.

Segment gross margin was 39.2% for the quarter, and segment operating margin was 28.3%, also in line with our expectations at the beginning of the quarter.

Our share of ART's net income was $3 million, down $2 million from last year, reflecting the lumpy order patterns typical of this business. For the first nine months ART's net income was up 24%. We expect ART to have a good fourth quarter, with earnings up solid double digits for the full year. We continue to be pleased with the progress of our new hydrocracking catalyst activities, which are contributing to the ART's double-digit earnings growth.

For Q4, we expect total Catalysts segment sales to return to Q2 levels or a little better. We expect segment gross margins for the quarter and the year to be just under the year-to-date average.

Let's move to Materials Technologies on Page 9. Third-quarter sales for Materials Technologies were $220 million, an increase of 3% compared with the prior-year quarter, driven by higher sales volumes.

Sales of silica-based engineered materials increased 5%, led by emerging region growth of 8%. Growth in the developed markets was 4%, led by growth in North America and Western Europe. Sales of silica gel used in coating and other applications grew in Europe for the second consecutive quarter.

Sales of packaging products grew about 2% organically, but this was more than offset by unfavorable currency translation. Sales in emerging regions, which represent just over half of this product line's sales, increased less than 1%, as growth in China and Eastern Europe was offset by lower sales in Latin America.

Sales in developed markets declined 2%, with weak food and beverage container demand in North America and Europe. Segment gross margin was 34.8%, a 200 basis point improvement from last year and a 110 basis point improvement compared with the second quarter. The increase reflects improved pricing, lower raw material costs, and manufacturing productivity.

Segment operating income grew 18% to $47 million. Segment operating margin improved to 21.3%, an increase of 270 basis points year over year.

The Materials Technologies team is making great progress with this business. Sales are growing, margins are up, and they continue to build the foundation for stronger growth in the future.

Please turn to Page 10 for Construction Products. Third-quarter sales for Construction Products were $278 million, an increase of 5% over last year. Organic growth was more than 8%, as sales volumes grew over 6%, and pricing improved over 2%.

Total sales in North America increased 7%. Sales of Specialty Building Materials increased 16% from a weak prior-year quarter. Sales of Specialty Construction Chemicals increased 3% year over year and 8% sequentially.

Sales in Western Europe increased 8%, led by a 26% increase in Specialty Building Materials and a 1% increase in Specialty Construction Chemicals. Although we are encouraged by the positive growth rate and the very strong SBM growth, we remain cautious about construction spending in Western Europe. We may be near the demand bottom, but there are few strong, sustainable drivers of construction in the region.

Gross margins for our Europe region increased more than 500 basis points from last year, driven by the pricing, productivity, and restructuring actions that we have taken over the last several years. Emerging regions sales growth was 2%, as reported, but 9% before the unfavorable effect of currency translation. Sales grew in Latin America, Asia, and Eastern Europe, but declined in the Middle East.

Construction segment gross margin improved 90 basis points to 36.3%, in part due to favorable mix from increased SBM sales. Segment operating income grew 24% to $46 million, and segment operating margin improved by 250 basis points to 16.4%. For the first nine months of 2013, operating margin was 14.4%, surpassing the 2007 peak of 14.1%.

Construction Products is delivering very good incremental margins, driven by good operating leverage in North America and the emerging regions, improved profitability in Europe, and good expense control.

Q4 is the hardest quarter to forecast because of the uncertainty of weather impacts on construction activity in the Northern Hemisphere. Construction will generally continue unaffected during cold weather, but rain and snow will slow or stop it. So far sales are in line with our expectations, but obviously, weather conditions in November and December are unknown at this point.

We are affirming our prior outlook for adjusted EBIT of $560 million to $570 million. We expect adjusted EBITDA to be $685 million to $695 million. These ranges include lower pension expense of approximately $45 million from the Q4 adoption of mark-to-market pension accounting and exclude closing costs and any 2013 earnings impact from the UNIPOL acquisition.

We expect Q4 sales to improve sequentially with the improvement in catalyst sales, and we expect gross margin to improve slightly from Q3. We reduced our book effective tax rate from 34% to 33% this quarter, reflecting the tax implications of the delay in our emergence. Our cash tax rate expectation remains 14% for the full year.

With the increase in our stock price, diluted shares have increased slightly. We now expect diluted shares to be a bit over 78 million shares at year end.

One final note before we open the call for your questions. We realize there are some items open as we approach the end of the year. The financial effects of the UNIPOL acquisition, the effects of adopting mark-to-market pension accounting, and the status of our bankruptcy. We expect to be able to disclose additional information about all three of these items by mid-December and will probably host a conference call at that time.

We want to make sure you have the most current information available before the year ends. We will update you on the date as soon as we confirm it.

With that, we will open the call for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Mike Sison, KeyBanc.

Mike Sison - *KeyBanc Capital Markets - Analyst*

In terms of the UNIPOL acquisition, maybe staying away from numbers, but can you give sort of a feel -- what type of products you are picking up, how it fits well with you guys longer term? And maybe -- you know, this was a business that was out there a couple years ago. What changed that gave you more interest this time around?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Let me, hopefully, not stray too far from what we're not supposed to say. But as you know, it is made up of licensing polypropylene manufacturing assets as well as catalysts to supply those assets once it's completed. For the last couple of years, well, maybe the last five years, we've been investing heavily into polypropylene catalysts -- both through acquisition, with some acquisitions we did four or five years ago with Borealis, as well as new technology advancements with some major customers. So we have been supplying polypropylene catalysts.

As well as over the past two years, we have worked closely with this unit, as we announced in prior, through a licensing arrangement we have on some technology that we've been working with for the past year. So all that, to put it in perspective, gives us good comfort that this was the right fit for us at the right time.

Mike Sison - *KeyBanc Capital Markets - Analyst*

Okay, great. And then in terms of FCC catalysts, you talked that the new technologies are getting some traction. In terms of timing and how those could maybe start to proliferate into volume growth, any thoughts there? Is it something more of a next year timeframe before you see some meaningful volume gains there?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

I think double-digits growth in the third quarter was pretty meaningful for us, and we will have double-digit growth going into the fourth quarter as well from our specialty catalysts. So it is taking hold on that side of it.

And we would continue to expect it to grow -- we do continue to expect it to grow in 2014 as well. Stepping back at the total catalysts level, the hydroprocessing that is going through ART -- both sequentially as well as year over year, we've seen double-digit growth. We expect that to continue.

And we are pleased on the FCC side with the technology, the trials, the look we've been getting --- the looks we've been getting, and so on. And so we feel good about where we are right now.

Hudson La Force - *W. R. Grace & Co. - CFO & SVP*

Your point is right, that we will gain momentum on these new products as we head into 2014. But we do expect them to run through the Q4 P&L -- make a difference in the quarter.

Mike Sison - *KeyBanc Capital Markets - Analyst*

Okay, great. And last question on FCC. You have been pretty confident, Fred, that 2014 is the year when industry utilization rates will tighten up. One of your competitors suggests they can expand capacity a little bit more than I think most thought heading into next year. Any thoughts there in your plans for capacity expansions heading into 2015?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Well, as we have said before, we think the industry -- our customers, our refiners -- need some new products, need some new technology. I mean, you see, some of our customers are under pressure as you look at their margins in certain regions of North America as well as Europe.

We believe that the introduction of these new products will help alleviate that, and ultimately we'll be able to share in that value. As you know, we have announced the Abu Dhabi joint venture expansion -- or the joint venture -- we continue to do all the engineering work on that. And timing on that will depend on the new startups as they unfold. But we are confident that the industry dynamics will be healthy next year.

Mike Sison - *KeyBanc Capital Markets - Analyst*

Great, thank you.

Operator

Brian Maguire, Goldman Sachs.

Brian Maguire - *Goldman Sachs - Analyst*

Sort of a related question -- the FCC catalysts volumes were down around 8%. I think that's kind of in line with your guidance. Just wondering if you think that this will be the low point for that year-over-year number looking out over the next 12 months, and whether you think we are going to stay close to that level until the anniversary this quarter? Or as you commercialize some of these new products, do you think there's room to get that materially closer to a breakeven number?

Hudson La Force - *W. R. Grace & Co. - CFO & SVP*

In terms of negative year-over-year volume growth, Brian?

Brian Maguire - *Goldman Sachs - Analyst*

Yes, just to the FCC catalysts part of it.

Hudson La Force - *W. R. Grace & Co. - CFO & SVP*

As you think about comparisons, next year versus this year, Q1 of 2013 was weak because of the operating issues that we had. You may remember, there were a number of customer-driven operating issues in Q1 that made Q1 a weak quarter for us.

Q2 was a strong quarter for us on FCC catalysts from a volume perspective. Q3, obviously, we have been talking about.

We expect Q4 to be a better FCC catalyst quarter. It will grow sequentially from Q3. In terms of the patterns next year, I think the year-over-year compares -- the Q1 of 2014 to Q1 of 2013 compare -- that'll be a relatively easier compare. Because, again, because of these customer operating issues that affected our volumes in Q1.

Q3 will be an easier compare next year, obviously; Q2 and Q4 will be tougher compares. We are not ready to give you exactly what the growth patterns are going to be next year. We can do more of that in February.

Brian Maguire - *Goldman Sachs - Analyst*

Okay, great. And then just on the specialty catalysts or polyolefin catalysts part of the business -- the volumes were up really nicely in the quarter on a year-over-year basis. It seemed like that was one that suffered from a little bit of destocking in the last couple of quarters, so I was just trying to get a sense how much of this you think is just some restocking that might be a little bit temporary, versus how much of this you think is sustainable?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Yes, I think the destocking is behind us now. It will depend on the global macroeconomics. If they continue to stabilize and improve, we will continue to see that growth across our polyolefin catalysts, both polyethylene as well as polypropylene.

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Brian Maguire - *Goldman Sachs - Analyst*

Okay, great. Thanks.

Operator

Mike Ritzenthaler, Piper Jaffray.

Mike Ritzenthaler - *Piper Jaffray & Co. - Analyst*

Just a follow-up on UNIPOL, and I guess the polyolefin catalyst industry, more broadly. What are the characteristics of that industry in particular that led you to that UNIPOL decision? This is a bit of a follow-up to Mike's question earlier. But we've seen others in this space entering into joint ventures and other economic sharing arrangements because they are concerned about being able to secure volumes.

That type of thing doesn't necessarily paint a great picture of the long-term competitive dynamics. But I'm guessing Grace's technology offerings, and market approach, and things like that will be fundamentally different, as we've come to expect.

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Yes. What we like about that polypropylene catalyst is -- and we've seen it. We have seen it with -- that our catalyst has got the attraction of the new investments, and the new investments that are specifically selling a higher-grade or better-performing polypropylene-engineered material. And those catalysts have been used -- our catalysts have been used in the new Borealis developments, and the investments they have made in the Mideast; as well as SABIC in Saudi Arabia.

So we continue to believe that there is no reason that the UNIPOL catalyst, as we merge it into ours and the technology it brings, that we won't continue to play at that higher-end polypropylene catalyst. And ultimately, it's the polypropylene solutions for our customers as they continue to upgrade those polymers.

Hudson La Force - *W. R. Grace & Co. - CFO & SVP*

I will add a point to Fred's, Mike. Some of the divestment decisions that you talk about at the polypropylene level, yes; but at the catalyst level, we see this as very attractive. We hear from our customers that catalyst technology will become increasingly important to them in the future.

Mike Ritzenthaler - *Piper Jaffray & Co. - Analyst*

Okay, interesting. In the release on catalysts, it discusses the lower pricing; obviously, various surcharges; but it also mentions lower refinery catalyst base pricing. I was wondering if you could elaborate on that base pricing component?

How much of that year-over-year delta is base pricing? Is there a mix issue that materialized in these numbers that will abate, or is there some other artifact that we are seeing?

Hudson La Force - *W. R. Grace & Co. - CFO & SVP*

It's about 1% or 2% in the year over year. And more than anything, it is customer and product mix.

Mike Ritzenthaler - *Piper Jaffray & Co. - Analyst*

All right, that makes sense. Thanks, guys.

Operator

John McNulty, Credit Suisse.

John McNulty - *Credit Suisse - Analyst*

With regard with regard to the acquisition, I believe at the time you put out the release, you indicated that it really wouldn't have any impact in terms of your returning cash to shareholders. So I guess I am wondering how that is the case -- whether you are comfortable taking on more leverage in the near term, and once you get through the bankruptcy process; or if it's just maybe pushing out the share buybacks? How should we be thinking about that?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Let me give you a top view, and then Hudson can dive into it. We have always said we're comfortable in this leverage ratio of 2 to 3 times. What it will ultimately do is, we will take on more leverage initially after emergence to make sure -- to fund this side. But we're not looking at any kind of delay in a shareholder returns.

Hudson La Force - *W. R. Grace & Co. - CFO & SVP*

I think Fred captured it, John. This is still within the overall leverage profile we have talked about. And I would include in that both the acquisition and the amount of share repurchase we have talked about. We can do both and still stay within the leverage profile we have talked about.

John McNulty - *Credit Suisse - Analyst*

Okay, great. And then with regard to the construction business, you'd indicated, I think, 2% pricing. What is driving the pricing there, and do you think that is something we can see going forward?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

We hope we can see it going forward. There is definitely better market conditions out there. We watch very closely the price of cement. Cement has been trending up. We have been able to be successful with some new products, as well as there is a recognition some of the raw materials fundamentally underneath the chemicals, the concrete additive chemicals, are increasing.

So we need to make sure that our margins are protected on that side. So it is really a combination of better market dynamics and also a recognition of the industry on some of the raw materials.

Hudson La Force - *W. R. Grace & Co. - CFO & SVP*

There is a technology piece to this, too. We talk about it more in catalysts than the other segments, but all three of these segments have a pricing dynamic that is driven by improving technology at the product level.

John McNulty - *Credit Suisse - Analyst*

Thanks for the color.

Operator

Laurence Alexander, Jefferies.

Laurence Alexander - *Jefferies & Company - Analyst*

Just a couple of quick questions. On the specialty catalysts, how are volumes up year to date if you just aggregate it across the three quarters?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

You are talking just the polyolefin -- the specialty?

Laurence Alexander - *Jefferies & Company - Analyst*

Just the polyolefin specialty catalysts.

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Yes, I think they are up single digits --

Hudson La Force - *W. R. Grace & Co. - CFO & SVP*

Mid-single digits, yes.

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Mid-single digits. We've seen the acceleration, obviously, in the third quarter, where it went to double digits.

Laurence Alexander - *Jefferies & Company - Analyst*

Okay. As you think about -- excluding the Dow acquisition, probably a similar trend next year?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Yes. We are having good momentum in the third quarter, as you know. We think our visibility in the fourth quarter is good. We think it will sequentially grow double digits again. And, again, we will have a better judge as we look at the overall macroeconomic trends for 2014, but we are coming off a good base right now.

Hudson La Force - *W. R. Grace & Co. - CFO & SVP*

If you look back over the last couple years, this business has kind of alternated between high single-digits, low double-digit growth. I think we've said sort of a multiyear -- if we look multi-years into the future, we expect it to grow mid- to high single digits, and where we are in any one quarter, there's a little lumpiness to this. Nothing like ART, Laurence, but it does have a little lumpiness. But this is a good, strong, growing business for us.

Laurence Alexander - *Jefferies & Company - Analyst*

And then just in North American construction, how do you see volume trends right now, if you back out the impact of the wet weather? Do you have any sense for underlying trends?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

We have seen some acceleration, some pick-up, through the third quarter, specifically into September; some pick-up in the early October timeframe. So again, generally, we're seeing some uptick. But we are cautious as well.

As Hudson said in the prepared remarks, weather does impact it. I will tell you, we did see in September/October, an infrastructure spending which I think is related to the government shutdown across both state and federal projects. That did slow. But the general economic underlying fundamentals seem to be accelerating.

Laurence Alexander - *Jefferies & Company - Analyst*

Wonderful. Thank you.

Operator

(Operator Instructions) Tyler Frank, Robert W. Baird.

Tyler Frank - *Robert W. Baird & Company, Inc. - Analyst*

I was wondering if you can just touch on the three business units and give me a sense of what you think the biggest risks are for 2014?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Overall, the macroeconomic environment -- if there is a considerable slowdown, that will generally ripple through all of our product lines from that standpoint. Volatility in the emerging regions -- as you know, we are almost 30% tied to the emerging regions. If there is extreme volatility, like we saw in the first quarter with Venezuela on the whole currency issue.

So that volatility in the emerging region is a caution for us as we think about it. And I would say, lastly, it would be around the refining side, that our customers continue to remain healthy; and on the whole crack spreads and the margin side of it.

Tyler Frank - *Robert W. Baird & Company, Inc. - Analyst*

Okay. Great. And then for the Materials segment, do you guys have any color for how you are expecting Q4 to pan out?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Yes. We continue to expect Q4 to be similar to Q3. We have done a lot in the operational restructuring of that business, as we've talked about, getting that gross profit margin up. And we have seen very good results on that side of it.

We're also pleased with, in the silica side, both the uptick in Europe as well as North America. The packaging -- you know, we are reading our customer press releases as well. We're looking at our customers. It's been -- in the whole packaging, the canned side and the bottle side, has been somewhat slow. We will see as we go into to the fourth quarter.

Hudson La Force - *W. R. Grace & Co. - CFO & SVP*

There is a normal, seasonal weakness as we go from Q3 to Q4 in this business, and I think you'll see that. But the year-over-year should be in line, just as Fred said.

Tyler Frank - *Robert W. Baird & Company, Inc. - Analyst*

Okay, great. Thanks for taking my questions.

Operator

Dmitri Silversteyn, Longbow Research.

Dmitri Silversteyn - *Longbow Research - Analyst*

Just wanted to ask a quick question on the UNIPOL acquisition -- the manufacturing facility that you picked up for making polypropylene. I'm assuming there is going to be some kind of a supply contract from the selling company to go with it. Did you have longer-term plans of getting basic in petrochemicals as a result of this entrance? Or will this always be sort of a side business, and the catalyst development will be the main driver of UNIPOL going forward?

Hudson La Force - *W. R. Grace & Co. - CFO & SVP*

Just to clarify, Dmitri, it is a polypropylene catalyst manufacturing asset. We are not producing polypropylene.

Dmitri Silversteyn - *Longbow Research - Analyst*

That is a relief. That's what I thought I read, but the way you said it, it sounded like you were actually going to be making polypropylene.

(multiple speakers)

And when you -- obviously, it's too soon to talk about it in detail, since you haven't closed on the deal. But as you look at asset that you are buying versus the assets that you have developed internally, is there going to be a possibility or an opportunity to rationalize your manufacturing footprint somehow, either regionally or with respect to new products versus sort of the workhorse products?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Yes, it is too early to talk about that because of the confidentiality we have. We do -- as I said earlier -- we think we have good synergies, both technologically, supply chain, as well as operationally.

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Dmitri Silversteyn - *Longbow Research - Analyst*

Okay. The licenses that you will pick up with this business with third parties -- your expectation is to retain those licenses, being the fact that you are going to be a merchant supplier now versus a competitor? And do you look for that opportunity to expand and gain customers that are not licensees but actually purchasers of your product?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Yes. The license offers opportunities. And as you know, we have been a merchant supplier as well. So we think it is positive. We think it is positive. We will be able to give you, as we get into the year, more strategic direction on how we're thinking, and so on.

Dmitri Silversteyn - *Longbow Research - Analyst*

All right. I will wait for your December call, then. Thank you.

Operator

Chris Shaw.

Chris Shaw - *Monness, Crespi, Hardt & Co. - Analyst*

Now with the UNIPOL deal, sounds like it fits kind of nicely into what you were guiding for M&A growth for 2014. Does that mean your M&A activity would slow down? Does it preclude you from doing other deals in the future? Or do you still think there is a pipeline out there for you?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

We think the pipeline is good. Deals of that size -- it would have to be the right type of deal. We've been very successful with a lot of bolt-on deals in the $50 million to $100 million, and the pipeline looks good for that, to improve our product mix as well as geographic mix. And we will continue to do those.

Chris Shaw - *Monness, Crespi, Hardt & Co. - Analyst*

Okay. And then on Materials Technologies, following up with some other questions -- great job on the margins there. Is that pretty much sustainable at these levels? It looked almost like four-year highs, and then if they're sustainable, can they actually go higher in the future?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

You know, we have said we weren't happy with the margins below 35%. We had a target to get it to 35%. That business unit did a terrific job.

As you know, you are either going up, or you are going down. So we will -- as we flesh out our plans, we will have more discussion on what pressure does that? What more can be done? And we are looking at that very closely.

But as we have said, really, the improvements are coming through application development, the change of the mix, higher-end silica, operationally improving our operations from an asset utilization as well as productivity standpoint. And finally, if there's bolt-ons that we can add to that.

Chris Shaw - *Monness, Crespi, Hardt & Co. - Analyst*

Great, thanks.

Operator

Chris Kapsch, Topeka Capital Markets.

Chris Kapsch - *Topeka Capital Markets - Analyst*

Had some follow-up questions on the refinery catalyst business. You had mentioned some mix shifts in that business. I'm just curious now, with rare earth prices and lanthanum, specifically -- having sort of come off and back to more normalized levels, and maybe reaching steady-state there -- I am wondering if the customers are now shifting back a little bit towards the higher rare earth containing products at all, and if that's affecting your mix demand equation? Or are they sticking with the low rare earth containing products?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Yes, they are sticking with the products that really have been introduced, from a rare earth perspective, over the last 12 months. We don't see any big shift or pushback to loading up those catalysts with rare earth.

Chris Kapsch - *Topeka Capital Markets - Analyst*

Got you. And then -- so just looking at the WTI versus Brent spread, which almost reached parity earlier this year, and now it's sort of widening again, just wondering if that is something that has any influence on your customer or product mix, in terms of them looking to optimize their operations? Generally, it's looked at as a positive for refiners' economics, but I don't know if it affects their catalyst purchasing decisions whatsoever.

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

Well, these changes -- the narrowing of that spread in a specific refinery, if it has a margin compression on their margin, they are looking to the catalyst supplier. Can we help them out, can we run -- can we get a better yield? They are more open to looking at new products at that point in time, when the slates either change, or there is a dynamic in the economics of those slates. So in an overall perspective, we need to keep -- our customers need to be healthy, but overall, that changes are generally healthy for the catalyst supplier.

Chris Kapsch - *Topeka Capital Markets - Analyst*

Okay. And then just a more general question about the intent to return cash to shareholder post-emergence. Have you conveyed -- I know you sort of order of magnitude conveyed what sort of buyback you might be considering, but in terms of the mechanism, is it likely to be a Dutch tender? And then given the changes that you mentioned about the timeline of emergence, does that affect the timing on that particular event?

Hudson La Force - *W. R. Grace & Co. - CFO & SVP*

Chris, we haven't talked yet about the mechanism. We will do that at the point where we start doing something. Our intention has always been to start right after emergence. And whether that's January 1, or February 1, April 1, you should expect us to start fairly quickly.

Chris Kapsch - *Topeka Capital Markets - Analyst*

Okay. Thank you.

Operator

Mike Ritzenthaler, Piper Jaffray.

Mike Ritzenthaler - *Piper Jaffray & Co. - Analyst*

On the cost efficiency or productivity side, Fred, you had mentioned just a little earlier that it had helped materials. Also, corporate expense was a little lower than we had expected.

My question is, is there more to come on the cost efficiency side in 2013 as different programs are implemented? And could things accelerate in 2014, or will we be more annualizing what has been accomplished in 2013 next year?

Fred Festa - *W. R. Grace & Co. - Chairman & CEO*

I would say it'll be more annualizing, which we accomplished in 2013. Now, if the macroeconomic trends go the other way, we have been -- as you know, we are pretty quick to get ahead of the cost curve. But everything we see today, it'll be more of a lap than an annualizing.

Mike Ritzenthaler - *Piper Jaffray & Co. - Analyst*

Okay, that's perfect. Thanks.

Operator

At this time, there are no further audio questions. I would now like to turn the call back over to Mr. Sutherland for closing remarks.

Mark Sutherland - *W. R. Grace & Co. - VP, IR*

Thank you, everyone, for joining us this morning. Enjoyed our conversation with you. If there are any direct follow-up questions, please feel free to call me on my direct line at 410-531-4590. And we will be signing off now. Thank you.

Operator

Thank you for your participation in today's conference. This concludes the presentation. You may now disconnect and have a great day.
