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# EDITED TRANSCRIPT

GRA - Q1 2016 W. R. Grace & Co Earnings Call

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**OVERVIEW:**

Co. reported 1Q16 sales of $363m and adjusted diluted EPS of $0.57. Expects 2016 adjusted EPS to be $3.02-3.21.





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## CORPORATE PARTICIPANTS

**Tania Almond** *W.R. Grace & Co. - IR Officer*

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

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

**Tom Blaser** *W.R. Grace & Co. - SVP and CFO*

## CONFERENCE CALL PARTICIPANTS

**John Roberts** *UBS - Analyst*

**Mike Sison** *KeyBanc Capital Markets - Analyst*

**Dan Rizzo** *Jefferies LLC - Analyst*

**Chris Kapsch** *BB&T Capital Markets - Analyst*

**Ken Debrune** *Credit Suisse - Analyst*

**Bob Koort** *Goldman Sachs - Analyst*

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

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

**Jim Barrett** *CL King & Associates - Analyst*

## PRESENTATION

**Operator**

Good day, ladies and gentlemen, and welcome to the W.R. Grace & Co. first-quarter 2016 earnings conference call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session, and instructions will be given at that time. (Operator Instructions) As a reminder, this conference call is being recorded.

I would now like to turn the conference over to our host for today, Tania Almond, Investor Relations Officer. You may begin.

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**Tania Almond** - *W.R. Grace & Co. - IR Officer*

Thank you, Sonja. Hello, everyone, and thank you for joining us today on April 27, 2016. With me on the call are Fred Festa, Grace's Chairman and Chief Executive Officer; Hudson La Force, President and Chief Operating Officer; and Tom Blaser, Senior Vice President and Chief Financial Officer. Fred will start with the highlights; Hudson will review more detail on the operations; and Tom will go over the financials. Then we'll open it up for Q&A.

Our earnings release and corresponding presentation are available on our website. To download copies, go to grace.com and click on the Investors tab. Some of our comments today will be forward-looking and are made under Section 27A under the Securities Act and Section 21E of the Exchange Act. Actual results may differ materially from those projected or implied due to a variety of factors. Please see our recent SEC filings for more detail on the risks that could impact Grace's future operating results and financial condition.

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

With that, I'll hand the call over to Fred.

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

Thanks, Tania, and good morning to everyone. Thanks for joining us. We had a very busy and productive first quarter. Since the spinoff of GCP, we've continued to align our company to ensure we have a simplified operating structure and a portfolio of businesses that can outperform the market.

I am sure by now you've read our announcement last week regarding the acquisition of BASF's Polyolefin Catalysts business. This is going to be a great addition to Grace's strong portfolio. Not only are we acquiring a proprietary polypropylene and polyethylene catalyst products and technology, but we also added capacity and manufacturing flexibility that we do not have today. This opportunity is perfectly aligned with our strategic focus on growing faster -- on faster-growing catalysts and materials technologies.

We are under confidentiality restrictions and will not be able to comment on specific terms of the deal. We started the year as planned, delivering $83 million of Adjusted EBIT or $0.57 per share. We exceeded margin expectations in both Catalysts and Materials as a result of strong productivity programs, capturing and retaining raw material deflation, and selective pricing opportunities.

One negative to the quarter was a greater slowdown in Asia across our short cycle silicas business and a slower order pattern of polypropylene catalysts in China. As discussed at Investor Day, we had plans for a slow Asia start, but this was slightly slower than anticipated. Hudson will provide more color during the portion of his call.

In terms of macro trends, China continues to be a headwind and a drag on the rest of Asia. We saw some uplift in late March and into April, but it's too early to predict a turnaround. Both US and European markets are seeing modest growth. For the remainder of the year, we will focus on sales growth, maintaining the margin gains from the first quarter through productivity and operational excellence actions, and delivering strong cash flow to fund growth and return cash to shareholders.

With that, I'm going to turn the call over to Hudson.

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

Thank you, Fred. The acquisition of BASF's Polyolefin Catalysts business creates significant new growth and productivity opportunities for us. It builds out our catalyst technology portfolio, and adds important capability and flexibility to our manufacturing network. The well-known LYNX polyethylene and polypropylene catalysts, will strengthen our product offerings in many major polyethylene and polypropylene manufacturing processes.

The acquisition includes about 170 employees globally, and manufacturing plants in Pasadena, Texas and Tarragona, Spain. Since the spin was completed in February, we have exited several small product lines in Materials Technologies to further focus our portfolio. These product lines total about $35 million in annual sales.

These product lines did not meet our growth or profitability requirements, and added significant complexity and costs to our operations. With the exits, we will reduce about 125 people in seven operating sites in seven countries. We will net about $11 million in cash from the exits with a small negative impact to 2016 adjusted EBIT. We continue to pursue smart bolt-on acquisitions in Catalysts and Materials, and have no further divestiture plans at this time.

Industry conditions for our catalyst customers are good. We see global demand for transportation fuels growing between 1% and 2% this year. Refinery utilization rates are good, and we see refinery margins improving in Q2, as refiners switch to summer gasoline grades. For polyolefin's producers, North America and European markets remain tight. Demand is strong and polymer prices are increasing.

In China, polymer demand has weakened and inventories have increased. China is only 7% of our sales, but it has been a growth market for us and we are watching demand trends there.

Our catalyst business performed well in Q1 with very good margins. As you will recall, we expected Q1 catalyst volumes to be low, due to higher-than-typical turnarounds, lower trial volumes, and the reduction of FCC catalyst capacity at our Curtis Bay plant. Specialty Catalysts revenue was up slightly, with significant volume increases in North America and Europe, partly offset by declines in China.

The FCC catalyst capacity reduction at Curtis Bay is complete as expected. We have eliminated 10,000 tons of the least efficient capacity in our network with minimal impact to 2016 earnings. We are also implementing our FCC catalyst pricing strategy as expected. We have a customer-by-customer, product-by-product approach that will take up to three years to fully implement.

We are starting to see results, including better bid prices, and expect FCC catalyst prices to improve slightly from Q1 to Q2. The improvements will be small at first and then increase over time. Because our strategy includes catalyst reformulation for many customers, the improvement will be seen in gross margins and in price. For Q2, we expect catalyst sales volumes to improve from Q1, as turnarounds return to typical levels and new account volumes increase.

The Takreer FCC unit started up in March and operated at full feed rates for a period of time, but since has experienced mechanical issues and is now operating at reduced feed rates. The unit has not completed its performance tests or been turned over to Takreer for commercial operations. We continue to monitor progress of the FCC unit startup and are ready to supply catalysts from inventory in our logistics hub and Abu Dhabi as agreed in our contract with Takreer.

But given the risk of delay, we are evaluating our commercial and operating options for the year. We think there are enough sales and cost opportunities to offset the effects of a delay.

In the Materials Technologies business, demand was better than expected in the US and Europe, and we are on track with our new product programs in architectural and wood coatings, and consumer and pharmaceutical applications. Demand in China was weaker than we expected, with sales volumes down 40% year-over-year. The Q4/Q1 demand pattern in China looks like an inventory correction. Q1 started very weak but finished much better. While channel inventories now look normal in the region, we remain cautious on Asia.

Looking forward, we see improved sales volumes in all of our businesses. FCC sales will increase as we begin supply to new customers, including Takreer, and with a return to normal turnaround activity. Specialty catalyst sales will increase with the growth of new products to existing customers and order timing, and sales and materials technologies will increase with new products, order timing and biopharma, and normal seasonality. We also have good visibility to second-half demand in ART, and expect a solid second-half for that business.

With that, I'll turn the call over to Tom.

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**Tom Blaser** - *W.R. Grace & Co. - SVP and CFO*

Thank you, Hudson. Before we get into the financial performance, let me do a little bit of housekeeping that will help you understand our financial results on a comparative basis. Earlier this month, we filed an 8-K containing Grace's 2015 adjusted financials to account for GCP Technologies on a discontinued operations basis.

Our financial commentary throughout 2016 will compare to 2015 on that basis. As a guideline, the disc ops presentation has about $9 million of additional operating costs per quarter compared to our run rate for 2016. These costs were either assumed by GCP at the time of separation or have been eliminated through restructuring or other cost reduction actions.

We've included, on page 4 of our presentation, a year-over-year Q1 bridge to help you understand our comparative performance. Now to the numbers.

Grace's first-quarter sales were $363 million, down nearly 9% as reported and down 6% adjusting for currency. Adjusted EBIT was roughly $83 million, up 16% as reported and up 19% on constant currency. Adjusted EBITDA margin was nearly 23%, up 480 basis points over last year. Adjusted EPS for the quarter was $0.57 per diluted share, up 39% from last year and up 44% on constant currency.

Adjusted Free Cash Flow for the quarter was $74 million and compares to $84 million a year ago. Our adjusted EBIT return on invested capital was 25.2%. This compares to 24% at year-end 2015. ROIC will improve as we lap the disc ops effect and digest the BASF catalyst acquisition.

Looking to our business segments, catalyst earnings grew 6% and operating margin was up 380 basis points in the quarter despite volumes being down. Q1 catalyst revenue was down 7% versus last year and down 6% on constant currency. Adjusted gross margin was up 460 basis points compared to last year to more than 43%, reflecting combined productivity improvements and lower operating costs, partly offset by lower volume and product mix.

Materials Technologies revenue was down nearly 12% and 7% on constant currency. Earnings were down 14% from volume leverage and currency translation. Sales excluding currency were down slightly in North America and Europe, and up slightly in Latin America and down to a greater degree in Asia.

Adjusted gross margins expanded to more than 39%, up 110 basis points compared with the prior-year quarter. Operating margin of 20.2% was down slightly from last year. I'll touch on a couple of capital allocation items and then we'll move to our 2016 outlook.

Last month, we paid down an additional $100 million of secured debt, bringing our total debt reduction, post-spin, to $600 million. After completing the BASF transaction, we expect our leverage ratio to edge outside our target range of 2 to 2.5 times. However, we intend to revert back to that range as we successfully integrate the business.

Our capital allocation strategy remains unchanged, and it is focused on reinvesting in the business through capital investments, funding growth initiatives, and bolt-on acquisitions. In addition, we will return cash to shareholders through our dividend as well as a programmatic regular share buyback program.

In the first quarter, we spent $15 million for share repurchase. Today, we announced our first quarterly dividend equal to $0.17 per share, with payment expected June 9.

Let's review our 2016 outlook and then we can open the call for questions. We are reaffirming our full-year guidance for 2016 adjusted EBIT to be in the range of $400 million to $420 million; adjusted EBITDA in the range of $500 million to $520 million; and adjusted EPS to be in the range of $3.02 to $3.21 per share. This assumes a euro exchange rate of [1.10] for the remainder of the year.

We see credible drivers in improving sales and margins throughout the year, including the startup of Takreer, the seasonal shift to the summer gasoline formulations, strengthening demand for Materials Technologies in Q2, new product introductions in that segment, and the continued capture of productivity and deflation. We expect catalyst earnings to increase mid-single digits for the year and for Q2 earnings to be up low-to-mid-single-digits sequentially with improved margins.

These projections take into account a likely range of outcomes for Takreer startup in the second quarter. Once we close the BASF transaction, we will provide you with insight on how to think about the earnings impact from that addition.

Turning to Materials Technologies, after adjusting for the spin and sale of certain discontinued product lines, segment earnings for 2015 were about $97 million. And we expect a nearly double-digit earnings growth year-over-year. In Q2, we expect segment earnings to be up between 35% and 40% sequentially with improved volume and margins. Asia volume continues to be a variable right now. However, we have good visibility to demand in all other regions for this segment.

Overall, we expect Grace Q2 earnings to grow between 9% and 13% sequentially, and Q2 adjusted EPS to grow between 14% and 21% sequentially. For the year 2016, we continue to project corporate costs between $65 million and $70 million, and pension expense to be about $12 million, down from our $20 million previous estimate. This improvement stems from the change in measurement of service and interest cost described in our recent 10-K.

We are adjusting our capital investment profile for 2016 to be between $130 million and $140 million based on the revised timing of customer investments. As a result, we expect 2016 Adjusted Free Cash Flow to be at least $250 million, including the favorable impact of our low cash tax rate and including transaction costs for the BASF catalyst acquisition. We expect Adjusted Free Cash Flow to be balanced equally between the first-half and second-half, despite earnings phasing.

We are maintaining our rigorous and disciplined approach to cash generation and to capital allocation management, with the expectation of continuing to deliver value to our shareholders.

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

## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions) John Roberts, UBS.

**John Roberts** - *UBS - Analyst*

So, on Takreer, is the delay there just on the makeup catalysts? Or have you already delivered the full initial load and you just can't recognize it until they get fully commissioned? Because you said they operated for a period, so it sounds like you fully delivered at least the initial load?

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

Yes. John, it's Fred. Yes, none of our catalysts are in that unit. What we've delivered for the customer requirements is the inventory to be stocked in the country to be ready for delivery when the unit does go commercial. So, we have no sales -- no sales in Korea.

**John Roberts** - *UBS - Analyst*

What are they using to do the test runs?

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

They are using the catalyst that the engineering company contracted with.

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

That's with a different supplier, John.

**John Roberts** - *UBS - Analyst*

Okay. And then they just clean that out completely? They shut down and replace with yours when they come back up?

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

Or blend it back in, yes.

**John Roberts** - *UBS - Analyst*

It will be blended --?

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

And this -- yes. And this is customary, how units do start up. They will start up with -- you know, the engineering company is responsible for starting up units. They choose what catalysts they want. And then the units turned over to the customer, and the customer has arrangements with whatever supplier they want to run it.

**John Roberts** - *UBS - Analyst*

Okay. And then on the BASF transaction, I know you said you have a confidentiality agreement, but when you say flexibility that you've acquired, does that imply significantly underutilized capacity? So the ultimate revenue potential for what you acquire might be materially different than the trailing results?

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

Yes. I mean it really implies two things. It implies that we've got -- we are acquiring manufacturing capability that we don't have today, that we've had to outsource -- or outsource to others that we'll bring inside. And it also implies that it's going to give us some sprint capacity to be able to supply our customers, where today, we are a little bit limited.

**John Roberts** - *UBS - Analyst*

Yes. Thank you.

**Operator**

Mike Sison, KeyBanc.

**Mike Sison** - *KeyBanc Capital Markets - Analyst*

Nice quarter there. In terms of FCC pricing, you talked a little bit more positively, I think, than you have in the past. Can you sort of walk us through the three-year plan and how that phases in over this year into the next couple of years?

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

Well, Mike, this is Hudson. As we said in the prepared remarks, we do think this starts out slow and gains momentum over time. We expect -- we are seeing progress right now. We expect to report a small improvement in catalyst pricing for Q2 -- the sequential between Q1 and Q2.

We're seeing better bid prices in the market, and it just feels like this is heading in the right direction. We are not going to be more specific than that, as we've said before, but we've got our detailed plans in place now and we're executing them.

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**Mike Sison** - *KeyBanc Capital Markets - Analyst*

Great. And then I think for Q2, you said refining catalyst operating income growth would be up mid-single -- low-single-digits? Is that right?

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**Tom Blaser** - *W.R. Grace & Co. - SVP and CFO*

I think it was mid-single-digits. Mid-single-digits, yes.

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**Mike Sison** - *KeyBanc Capital Markets - Analyst*

Mid-single digits? And that assumes Takreer doesn't contribute much and then the full-year assumes Takreer contributes maybe in the second-half? Is that kind of the way to think about it?

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

Yes, that's the way to think about it, Mike.

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**Mike Sison** - *KeyBanc Capital Markets - Analyst*

Okay. Great. And then last question will be on the BASF transaction. How big is your polyolefin franchise now? And are you the number one player in total now? And is there opportunities to acquire more assets from other players who are captive as well?

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

Mike, this is Hudson. I think order of magnitude, the business is around $400 million in sales; maybe just a smidge under that. In polyethylene catalysts, I believe we're number one now. The acquisition will enhance that, I think. In polypropylene catalysts, we're number two now. I think the acquisition enhances that, but doesn't change our rank in the market.

And I'm sorry -- I've forgotten the third part of your question.

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

Yes, let me -- I'll answer. Does it create other opportunities? -- was the question. You know, as I said Investor Day, I think as the landscape changes, that there will more opportunities to extract businesses from some of the majors that may want to shed those through a top-notch catalyst supplier. And we'll continue to work those across all the catalyst pieces. And that's what we're doing -- just as we did here with the BASF acquisition.

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**Mike Sison** - *KeyBanc Capital Markets - Analyst*

Okay. Great. Thank you.

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**Operator**

Laurence Alexander, Jefferies.

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**Dan Rizzo** - *Jefferies LLC - Analyst*

This is Dan Rizzo on for Lawrence. You said that you exited some product part lines that cost $35 million in the quarter. Are there going to be any future exits you are contemplating?

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

There's nothing that we're planning at this time. These were some small, very niche product offerings that we had in our Materials Technologies portfolio that, frankly, as we reviewed the portfolio, they weren't delivering the growth or profit expectations that we had. And we wanted to take those costs out and really focus the portfolio. But we've done that work and there's nothing else that we're looking at right now.

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**Dan Rizzo** - *Jefferies LLC - Analyst*

Okay. Thanks. And then you indicated that you've captured some raw material cost deflation in the quarter. Has that since ended? I mean, are raw material costs now kind of ticking up, just given the changing dynamic?

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

No. Those deflation benefits will continue through the year.

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**Dan Rizzo** - *Jefferies LLC - Analyst*

Okay. And then one last question. In Materials Technologies, I think it was down slightly in Europe, but I think your outlook was a little bit more positive. Was it just a blip or deleveraging? Or just what's kind of going on there?

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

We -- for the last -- I'll say two quarters; may even have been three quarters now -- we've been positively surprised with demand in Europe. It's small -- we used to say green shoots years ago. Small -- what's the right way to say it? -- small positive surprises in the demand that we're seeing in Europe. It's not anything I'd describe as robust, but we've consistently been positively surprised with the results in Europe.

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**Dan Rizzo** - *Jefferies LLC - Analyst*

All right. Thank you, guys.

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**Operator**

Chris Kapsch, BB&T Capital Markets.

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**Chris Kapsch** - *BB&T Capital Markets - Analyst*

It's Chris Kapsch. Hey, in the catalyst segment, just curious on catalyst, the 460 basis points of year-over-year margin improvement, do -- order of magnitude, could you just talk about what were the -- what was more important there, the productivity or this raw material deflation capture?

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

Yes, Chris, it's Fred. I mean, two-thirds of it were really the productivity. I mean you may recall last year, we turned around two major units in Lake Charles as well as major work in Worms. And some of that operational excellence and productivity, I mean we've done a bang-up job there. And I'll give the guys a lot of credit at Curtis Bay as they took down the -- that capacity and shed those costs and so on.

So, listen, we were pleasantly surprised, but -- and we continue to be very pleased with how that's working. And we've got some good line of sight to some other projects and we'll continue to hold those margins. So we feel good about that.

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**Chris Kapsch** - *BB&T Capital Markets - Analyst*

Okay. And then just one quick follow-up on Takreer. Just the performance guarantee run -- I think you said it hasn't started yet. When it does start, how long does a run like that typically take for them to validate the operating performance of the unit?

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

Chris, it's Fred and I'll let Hudson, if he wants to add any comments to it, he is obviously following this very closely. It really varies. I mean we've seen some units do the performance tests and startups with a week time. We've seen others, others a longer time from that standpoint. We've been given the performance date -- it's in the second quarter. The test run; we've been provided that. But that's really as much as we know now.

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

I don't have anything to add. I think Fred got it exactly right.

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**Chris Kapsch** - *BB&T Capital Markets - Analyst*

Okay. Then just the reaffirmation of the EBITDA guidance range for the full year -- just I know there's some pluses and minuses here, but I wanted to -- the adjustment that you made with respect to your pension cost expectations, that was not contemplated in the prior guidance; is that correct?

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**Tom Blaser** - *W.R. Grace & Co. - SVP and CFO*

That's correct.

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**Chris Kapsch** - *BB&T Capital Markets - Analyst*

Okay. And then so just wondering what -- so you also have incremental benefit, I guess, from the current FX environment benefit from the pension, so I'm wondering what really is the offset here? Is it primarily Takreer? Is it a little bit of the uncertainty in Asia around Materials Tech, combination thereof?

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**Tom Blaser** - *W.R. Grace & Co. - SVP and CFO*

It's really both of those things, Chris.

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

Yes. And I'd add a little comment to it. I mean, we've got a big step-up in materials in the second quarter, 35% to 40%. We've got some very good visibility, so we feel good about that. But our year is backend-loaded as we said at Investor Day.

And we've got good visibility on the ART side of it on those orders, which is heavily loaded. Same thing on our specialty chemicals side of it. So we'll give you another update at the end of the second quarter.

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**Chris Kapsch** - *BB&T Capital Markets - Analyst*

Okay. Thanks, guys.

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**Operator**

Christopher Parkinson, Credit Suisse.

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**Ken Debrune** - *Credit Suisse - Analyst*

This is [Ken Debrune] on for Chris Parkinson. Just on the pricing front, you mentioned that some of the decline was due to metals deflation, but can you comment if there were any regional price difference -- any regional price pressures? And how would you think about that going forward?

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

This is Hudson. Nothing that I would highlight from a regional perspective. These are prices that are individually negotiated on a customer-by-customer basis. What we did see in Q1, I'll clarify, was not Q1 pricing activity. This is the effect of -- a carryover effect of pricing activity in the second-half of last year.

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**Ken Debrune** - *Credit Suisse - Analyst*

Great. And just going forward, based on the acquisition, you paid down a little bit more debt, and you've recently declared a new dividend. How should we think about your appetite or willingness to do buybacks going forward?

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**Tom Blaser** - *W.R. Grace & Co. - SVP and CFO*

Good question. We're going to continue a regular programmatic approach to our share buyback. I think what you've seen in the first quarter at that level -- recall we did have a shorter period available to do buybacks, but we plan to continue that regular programmatic approach to the share buybacks.

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**Ken Debrune** - *Credit Suisse - Analyst*

Great. Thank you.

**Operator**

Bob Koort, Goldman Sachs.

**Bob Koort** - *Goldman Sachs - Analyst*

Good Morning, Fred as you guys start to put these price hikes through on FCC, would you expect, after what's been a pretty benign environment for your customers from a pricing standpoint, for an increase in trialing and other activities, to try and maybe resist those price hikes? Or do you think it's just going to sort of be business as usual?

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

You know, we're a customer as well as a supplier. And we always resist those. But I think it's -- again, it's the strategy we laid out early on, on this side of it, was we've got to bring them value. We've got to bring them value through the reformulation, demonstrate that value, and capture that price as we go. We've been able to do that.

And again, not to reiterate our overall strategy, but it was -- take out the 10,000 tons of the least productive product, which we've done on the capacity side, reintroduce some new products, start working it customer-by-customer on the formulation side. And as you do that over a period of time, it will be just the norm. And that's what we found in the past.

**Bob Koort** - *Goldman Sachs - Analyst*

And on Takreer, from the outside, it seems remarkable, given the scale of that unit, that the customer would change catalyst suppliers in the E&C handoff. How common is that in the industry? And what was the secret sauce you guys have that was able to dislodge the incumbent catalyst provider there?

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

Bob, this is Hudson. It does happen that the customer will choose a different catalyst supplier than the engineering house. And the secret sauce, frankly, is product performance. Takreer ran a rigorous performance evaluation on the catalyst, and in the final analysis, they believed our catalyst would perform best in their unit. And as soon as they take over the unit, we expect to begin supplying our catalysts.

**Bob Koort** - *Goldman Sachs - Analyst*

Thanks. And one real quick one, if I might. With China not being as growthy as it used to be, is there any risk of your catalyst competitor there, that seems to be more of an in-country supplier, could actually start to seek out some of your markets in other geographies?

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

We can't say that there is no risk, but their catalyst technology doesn't perform at the level that our catalysts do. And with all catalyst businesses, our customers are really paying for technology and performance. Price is not at the top of their catalyst selection criteria. And as long as we maintain that technical lead, we'll be okay.

**Bob Koort** - *Goldman Sachs - Analyst*

Great. Thank you.

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**Operator**

(Operator Instructions) Chris Shaw, Monness, Crespi, Hardt.

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

Within catalyst, the headwind from -- the volume headwind from trimming down Curtis Bay of 5% this quarter, is that the kind of headwind -- you know, 5% each quarter for the rest of the year, that you expect? Or is there something that changes in that?

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

Chris, I'm sorry -- I missed the first part of your question. Could you repeat it, please?

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

Yes. There was a 5% volume headwind in the first quarter in catalyst, and most of it was Curtis Bay. Is that the sort of level that will impact the rest of the quarter throughout the year?

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

Thank you, I have it. No, the Q1 headwind was bigger -- not just really related to Curtis Bay. We had a very large customer that went through a significant turnaround in Q1. They are up now; that won't repeat throughout the year. And then the other factor in Q1 is we supplied no catalyst to Takreer, and we expect to supply some as we go forward. So, simply no, the Q1 headwind isn't representative of the full-year.

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

Okay. Thanks. And then did the Curtis Bay shutdown -- is there an immediate margin benefit besides switching out your lowest margin customers or product sales -- but is there an immediate -- do you usually write off the asset and is there immediately like a benefit to gross margin as well?

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

There was no asset write-off. These were assets that were significantly depreciated. But we do get a margin benefit from customer mix -- as we shed, lower-margin customers -- and the Lake Charles and Worms plants are more cost-efficient than the Curtis Bay plant. And so there's a mix shift benefit just in terms of where our products are being manufactured.

We did do cost reduction in Curtis Bay as part of this. And that's probably running through the gross margin line as well.

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

Okay. Thanks. And then just finally -- not sure how much you could say on this -- in the polyolefin catalyst business, I'm trying to get an idea of how concentrated is that industry? Just maybe like you tell me what sort of market shares you had in your businesses prior before you actually acquired the new assets?

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

Chris, it's Hudson again. I won't comment on specific market shares in these industries, but it's a market with a fair number of competitors. It's -- you need two hands to count all the competitors in this market.

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

Okay. Thanks. That's helpful. Thanks a lot.

**Operator**

Tyler Frank, Robert W. Baird.

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

Thanks for taking the question. Just a quick follow-up -- can you break down the 5% volume decline for me? What percentage of that was from Curtis Bay and what percentage of that was from the customer turnaround?

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

All three were contributors, Tyler, but we won't give you the specifics. None was bigger than the others. They are roughly equal effects but I'm not -- I don't intend to be precise on that.

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

Got it. Okay. And then as Takreer further challenges ramping up, what markets do you think might be able to absorb that volume, just based on what you're seeing in terms of demand patterns? And would you still expect to run at sort of that mid-90's utilization rate in the second-half?

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

That's a good question, Tyler. The overall market is growing, of course. And we've grown in the last year or so at a rate that's faster -- I'm referring to the FCC catalyst market right now -- at a rate that's been faster than the historical levels. Demand for transportation fuels has dropped and that creates opportunities in the marketplace.

We're getting good response from customers on our catalyst technologies and the reformulations that we're bringing to them. So we think that creates opportunities for us. But it's not all about sales growth either. We would certainly be looking at costs if there was a delay here.

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

Okay. Are there -- I guess you had mentioned that you see other opportunities out there in the market. I mean, are there -- I guess can you just discuss what those opportunities could be or point to specific markets on where you are seeing strength?

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

Well, I'm not going to be specific about customers or regions, but generally, this market is growing now and that creates opportunities for us. As we've looked at the -- implementing our pricing strategy, part of that has been to be quite selective on bids and how we're participating in those processes. There's enough bid activity and demand for new technology in the market to allow us to cover, if there was a delay in Takreer. But I'll say again, this wouldn't only be about sales; it would also be about costs.

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

Got it. Okay. Thank you.

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**Operator**

Jim Barrett, CL King & Associates.

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**Jim Barrett** - *CL King & Associates - Analyst*

Fred, a question for you on the BASF deal. I realize you are limited in what you can say. There was a mention in the press release that you need to consult with employee representatives. Is that Spanish law? And is that solely due to a change in ownership they need to be consulted?

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

Yes, that's exactly right, Jim. Don't read more into it than that. It's just customary.

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**Jim Barrett** - *CL King & Associates - Analyst*

And given I can count on two hands the number of competitors in the space, would it be reasonable to assume that the regulatory risk is fairly modest to moderate?

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

That's exactly what we believe.

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**Jim Barrett** - *CL King & Associates - Analyst*

Okay. And just moving on to China for a moment, have the competitive dynamics changed there? I heard your comment that the 40% drop was due to a function of reducing inventories in the channel, but aside from that, has the competitive dynamics changed in that market, along with the economic downturn there?

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

You know, I don't think the competitive dynamic has changed dramatically. What has changed is their willingness to carry inventory in cash. We have seen it come out of the cycle, a number of inventory. And that's in our silicas -- across the silicas business, and we also have good visibility in from the units we've licensed in the polypropylene side.

But I think it's a willingness to box the cash a lot tighter. And that's what we've seen. I think that will probably continue. As Hudson or I said -- I can't remember, or Tom -- we were encouraged by a little bit of bounce-back in the silica side in April here, and we've reflected in our second quarter. But I think that's what's changing.

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**Jim Barrett** - *CL King & Associates - Analyst*

Thank you very much.

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

Thanks, Jim.

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**Operator**

Thank you. And this does conclude our question-and-answer session for today. I would now like to turn the call back over to Tania Almond for any further remarks.

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**Tania Almond** - *W.R. Grace & Co. - IR Officer*

Great. Thank you, Sonia. And we just want to thank everyone for joining the call today. If you have any follow-up questions, you can reach me at 410-531-4590. Thanks very much and have a great day.

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**Operator**

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

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