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GRA - Q1 2015 W. R. Grace & Co Earnings Call

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OVERVIEW:

Co. reported 1Q15 sales of $721m and adjusted diluted EPS of $0.82.

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the first-quarter 2015 W.R. Grace and Company earnings conference call. My name is Tracy, and I will be your operator for today. (Operator Instructions) I would now like to turn the call over to Tania Almond, investor relations officer. Please proceed, ma'am.

Tania Almond - *W.R. Grace & Co. - IRO*

Thank you, Tracy. Hello, everyone, and thank you for joining us today on April 23, 2015. With me on the call are Fred Festa, Grace's Chairman and Chief Executive Officer, and Hudson La Force, our Chief Financial Officer.

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 of 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 details on the risks that could impact Grace's future operating results and financial conditions.

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 our website. Our comments on forward-looking statements and non-GAAP financial measures apply to both the prepared remarks and to the Q&A.

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

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

Great. Thanks, Tania, and good morning to everyone. We appreciate you joining our call.

We started the year as expected, and we are on track to meet our 2015 business goals. We achieved good earnings growth with improved gross margin and adjusted EBIT margin and very good cash flow performance, driven by lower networking capital days. With better earnings and lower working capital investment, our adjusted EBIT return on invested capital increased to 32%, reflecting the high quality and value of our businesses. Our team is managing the effects of lower oil prices and a stronger dollar well and turning this into a competitive advantage where we can.

In Catalysts Technologies, we are seeing increased demand for transportation fuels and polyolefin plastics, which should lead to stronger catalyst demand later this year. For refining customers, we have developed new FCC catalyst products that offer good performance at a lower price point. Commercial trials have begun with several customers, and early feedback is positive.

In materials technologies and construction products, we started seeing lower raw materials cost in Q1, and we will see larger benefits beginning in Q2. While currency is a significant headwind to Q1 and the year, we are mitigating the effect with tactical changes in how we manage our supply chain and leveraging our flexible manufacturing operations.

Stepping back from a more fundamental perspective, we are seeing a number of positive indicators. Refineries generally operated at high utilization rates with good margins in Q1, although we did see some of our customers take extended turnarounds in the quarter.

Petrochemical customers also operated at high rates, with good demand for their products. Our ART joint venture had a good quarter and is on track for double-digit earnings growth this year.

In March, I visited Abu Dhabi, where we have completed phase 1 of our new FCC catalyst manufacturing plant. Detailed engineering for phase 2 is underway, and we expect those operations to begin in 2018. The facility, located in Kizad industrial zone, approximately 70 kilometers outside of Abu Dhabi, will serve refineries throughout the Middle East.

In materials technologies, we saw good demand for our engineered materials products in North America and developing Asia. In Europe, demand improved from fourth-quarter levels. We are cautiously optimistic about demand in Europe in the second half.

Construction products had double-digit demand growth in North America and developing Asia, reflecting good fundamentals in those markets. Across our businesses, we are starting to see the benefit of lower raw material costs and operating expenses. Our supply chain and restructuring initiatives are well underway. In Q1, we incurred $10 million in restructuring costs for workforce reductions that began in the quarter. These actions will produce over $20 million in annualized savings by the end of the year.

Let's turn to our plan to separate Grace into two industry-leading public companies. We continue to strongly believe that the separation is the right next step to continue our track record of increasing shareholder value. We have received positive feedback from investors, customers, partners, and employers. Both companies will be better positioned to capture their distinct growth opportunities and to optimize their cost structures. We remain confident that both new Grace and new GCP will benefit from improved strategic focus, simplified operating structures, and more efficient capital allocation.

Since we announced the plan in February, we have mobilized our separation teams and are on track to complete the separation within the roughly 12-month time frame we outlined. The next visible milestone will be in late summer, when we file our Form 10 with the SEC. This filing will include the audited carve-out financial statements from new GCP. We are excited about the benefits of this separation and will continue to provide updates as we move through the process.

And, yes, of course, I am just as excited about the ongoing opportunities we have in all three of our businesses. We have well-defined growth projects in each business and good investment in productivity opportunities across our operations. Our strong cash flow gives us the ability to make these investments, pursue bolt-on acquisitions, and continue returning capital to you.

I will now turn the call over the Hudson to review the quarter and our outlook in more detail.

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

Thank you, Fred. First-quarter sales were $721 million, down 3% as reported and up 3% at constant currency. Currency reduced sales by about $44 million, or 6%. Adjusted EBIT was $117 million, up 5% as reported and up 15% at constant currency. Currency reduced earnings by about $11 million, or almost 10%.

Adjusted EPS was $0.82 per diluted share, up 7% and up 19% at constant currency. Adjusted free cash flow was up 32% to $87 million, driven by a very good working capital performance.

As many of you know, Grace has a low cash tax rate that we expect to continue until 2021. In Q1, this resulted in a $20 million favorable impact to cash flow equivalent to $0.27 per share. For the full year, we expect the impact to be about $120 million, or about $1.65 per share.

Let's turn to catalysts technologies on page 6.

As you know, our catalyst business is driven by end-user demand for transportation fuels and plastics on a global basis. With the decrease in oil, fuel, and plastics prices over the last six months, demand for our customers' products is starting to increase. In fact, the US Energy Information Administration recently reported a 2.7% increase in gasoline demand over the past six months compared to 0.2% in the prior six months. Industry sources are also reporting strong demand for plastics. Overall utilization rates remain high for our customers especially in North America.

With healthy industry fundamentals, catalysts technologies had good volume growth in Q1. FCC catalyst volumes increased 3% in the quarter, and specialty catalyst volumes were up 7%. One of our largest customers took an extended unplanned outage during the quarter, which reduced our FCC catalyst sales by almost 2%.

Year over year, segment earnings grew 4%, or about 11% at constant currency, reflecting higher sales volumes and no UNIPOL acquisition costs. Operating margins increased 120 basis points.

Sequentially, segment earnings decreased, reflecting typical seasonal volume patterns in our FCC catalyst business, more normal specialty catalyst and licensing sales after a strong fourth quarter, the stronger dollar, and some higher operating costs. So segment gross margin was down slightly in Q1. We continue to expect segment gross margin for the full year to be in line with full-year 2014.

The ART joint venture contributed $6.2 million to segment operating income, compared with $3.7 million last year. ART remains on track for double-digit earnings growth for the full year.

Let's turn to materials technologies on page 7.

Materials technologies had a significant impact from currency this quarter, with sales lower by 9% and earnings by 10%. Volumes were down year over year but up sequentially, with good demand in North America and developing Asia and better demand in Europe. Although earnings were lower, cash flow performance was very good, with segment cash flow up double digits over last year.

Gross margin increased 30 basis points primarily on improved pricing. Operating margin decreased 20 basis points on lower operating leverage in the quarter.

Please turn the page 8 for construction products.

GCP had good sales volume growth in FCC and SBM, with sales volumes up double digits in North America and developing Asia. Segment sales volumes in Europe and Latin America were mixed, with strength in some markets offset by weakness in others. Sales in SBM also benefited from an improved product pipeline and better performance in our residential waterproofing business. Segment gross margin of 35.8% increased 140 basis points primarily due to higher sales volumes, improved pricing, and lower cost. Segment operating margin increased 170 basis points.

Earnings grew 16%, or 25% at constant currency. GCP continues to track to our mid-cycle margin targets of 16% to 18%.

Net debt at the end of the first quarter was $1.9 billion, and net debt to adjusted EBITDA leverage was about 2.5 times. Our adjusted EBIT return on invested capital was 32% compared with 27% a year ago, a 500-basis-point increase.

Let's touch on our outlook, and then we will open the call for your questions.

As Fred mentioned earlier, we are on track to meet our 2015 business goals, and we are affirming our 2015 constant currency outlook. We expect 2015 adjusted EBIT to be $675 million to $705 million on a constant currency basis, an increase of 8% to 13%. And we expect adjusted EPS to be $5.05 to $5.45 on a constant currency basis, an increase of 14% to 23%.

Assuming current exchange rates, including the euro at $1.07, we would expect a currency headwind to adjusted EBIT of about $60 million into adjusted EPS of about $0.55 per share. Our supply chain initiatives, global manufacturing flexibility, and restructuring actions helped mitigate some of the currency headwind but do not fully offset it.

Several factors make this year's second half stronger than the first half. Currency impacts saw results immediately, while the benefits of lower oil prices, including better catalyst demand and lower raw material costs, will come over the course of the year. Similarly, the benefits of our productivity initiatives and restructuring actions will impact the second half more than the first half.

We also have a major turnaround in our Curtis Bay catalyst and materials plant in the second quarter. This turnaround, which occurs every three years, and other anticipated maintenance and manufacturing costs will reduce Q2 earnings by about $7 million. The timing of UNIPOL licensing revenue was also a factor in Q2. Q2 2014 was a very strong licensing quarter, while this Q2 should be a normal quarter.

We continue to expect at least $430 million in adjusted free cash flow for the year.

Overall, we are on track to meet our 2015 business goals. Sales are shaping up as we expected, and our cost and restructuring initiatives are on track. Fundamentals are good in the catalyst business. And weather aside, fundamentals were good in Q1 in the construction products business and could improve as the construction season gains momentum.

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

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Mike Ritzenthaler, Piper Jaffray.

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

I'm curious about the FCC catalyst pricing outlook for the rest of 2015, with volumes up nearly 4% and supply relatively tight against across the industry. Can you help us reconcile the flattish pricing with things like customer trialing and industry growth and what reasonable expectation might be for 2015?

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

Well, Mike -- and this is Hudson -- in your analysis, you've got some of the key points. We are operating at high utilization rates in the FCC catalyst business. We do think that will continue to tighten as the year goes on. We do have products on trials with customers right now which, as you know, are at a little bit less than full commercial pricing. I think those dynamics will play out over the course of the year. I think we will see some positive pricing in catalysts this year. And I think you'll see that as the year goes on.

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

Let me just add on to that, Mike. If you think about it, six months ago there was a panic around the FCC and around catalysts around this -- where oil prices doing, what is going to happen. I think if you look -- and we were pretty bullish on the effect that it wouldn't be a dramatic effect. And I think if you look at the pattern over the last six months or so and where we believe, our Company -- Grace is built to handle high oil, low oil prices. We've got multiple operations that can make a full range of catalysts around the globe. And we've got a very good customer technical group and a very good customer relationships that enable us to change those dynamics.

So we will go through the year. I think we will have a better perspective coming into the third quarter and to be able to update you on those industry dynamics as we go. But it's an important point. I wanted to emphasize that point.

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

No, that makes sense. Just a question about raw materials. I was wondering if it was possible to somehow quantify the raw material benefit that we saw in Q1. And then I read a snippet this morning about the China Ministry of Finance scrapping export taxes on rare earth. And as you're looking at raws for the next several quarters, whether we can expect to see -- I think you alluded to in your prepared comments about maybe the raw material tailwind gathering some momentum. Maybe that compounds with lanthanum prices potentially coming down. Just some thoughts on that front.

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

Couple thoughts, Mike. On rare earth specifically, rare earth costs are so low now that they are really not -- it's an important ingredient in our product, but it's not nearly the economic cost that it was two or three or four years ago. And so the tax policy change in China really won't have an effect on us that would be visible.

I think, more broadly, we do expect to benefit from lower raw material prices this year. Order of magnitude, it will be less than 1% of sales. And the other point I will say is that we did see some of that in Q1. We probably saw 15% or 20% of what we'll see for the full year in Q1. It will gather momentum, I think is the way you said it, over the course of the year.

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

Okay, very helpful. Thank you.

Operator

Brian Maguire, Goldman Sachs.

Brian Maguire - *Goldman Sachs - Analyst*

Just a question on the construction segment. The pricing there was a little bit weaker than I would guessed given the volume strength and particularly the robust conditions in North America and Asia you talked about. Just wondering how much of that is you guys having to pass through some of the raw material benefit pretty quickly versus maybe some competition from -- you have got two pretty big European-based guys who maybe are getting the currency tailwind that you guys are suffering as a headwind. Any pressure from them on pricing? Or how should we expect pricing in that segment as the year goes on?

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

You've got to -- you are seeing the consolidation of all the pricing. The underlying fundamental dynamics are good for pricing opportunities in North America and where the business is. What we're seeing is some of that pressure because of the inflationary dynamics in Latin America that are eating up some of that side of it.

Our demand -- if you look at construction across the globe, even in the first quarter, January we came out of the box very strong. So, harsh winter in the northern hemisphere in North America. And then if you think Turkey and Euro-Asia, it was dramatic. Our volume dropped dramatically in February and then bounced back strong in March. This is -- these are very positive signs that we are seeing around the construction activity. And our cement customers announced some pricing this quarter.

So I think the fundamental is good. There is fundamental, good economics across the world in construction for some possible price increases. The piece that we are watching closely is continental Europe and is the stimulative effect of some of the things that are happening in the banking sector. Will that re-stimulate some of the construction activity in Europe? If that's the case, construction will have a very, very good year.

Brian Maguire - *Goldman Sachs - Analyst*

Okay. And following on that point, any -- what's the outlook for acquisitions in that segment? Seems like you had some success in the past with some smaller bolt-on deals. Given the positive outlook for that segment, are you guys more inclined to do deals now?

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

I don't think it's changed our outlook. We've done them around the globe as well. And we continue to be inquisitive on that side of it, and we will if those good opportunities come up. We're going through the spin-out now, so a number of resources are dedicated to that, but not to the effect that we find something good, we would buy -- we would buy that.

Brian Maguire - *Goldman Sachs - Analyst*

Okay. Just one last one, if I could. The catalyst customer issue from the turnaround you talk about, are you going to -- any hope of getting that volume back later in the year, or was that just sort of lost in the quarter?

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

It's already backed. They are back and operating again. If your question is can you catch all of that volume up or not, it will depend on how hard they run. In going into the second quarter, the refineries are running pretty hard right now.

Brian Maguire - *Goldman Sachs - Analyst*

Great. Thanks very much.

Operator

John Roberts, UBS Global Asset Management.

John Roberts - *UBS - Analyst*

Nice quarter. Your earnings guidance is affected by currency, but you have maintained your free cash flow guidance. Can you talk a little bit about why free cash flow is not as affected by currency's earnings?

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

The big piece, John, is the flexibility that we have with our manufacturing operations, and supply chain in turn, to move tactically to take advantage of stronger currencies and weaker currencies. That's an important mitigator when we think about this from a cash flow perspective versus an earnings perspective.

The other piece of it is we are focused on managing our working capital, as we always do, and we've got earnings -- excuse me, levers on earning -- I'm sorry, levers on working capital that we don't always have on earnings in terms of tighter inventories and things like that.

John Roberts - *UBS - Analyst*

And then as a follow-up, it looks like you are rolling into a very easy comp in construction products in the upcoming quarter. If I look at the two-year comp to sort of smooth out some of the comparisons here, the first quarter had a 6% two-year comp. To kind of have the same two-year comp in the next quarter, it looks like you have to be double-digit there. Is that -- is the comp easy enough this upcoming quarter that the year-over-year might be double-digit (multiple speakers)?

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

I haven't looked at it from a two-year perspective, John. We had double-digit growth in Q1. And as Fred said in his remarks, we feel like we have good momentum in the construction business.

John Roberts - *UBS - Analyst*

Thank you.

Operator

Laurence Alexander, Jefferies.

Laurence Alexander - *Jefferies LLC - Analyst*

Good morning. Question about the FCC catalyst business. What's your sense of where returns are versus reinvestment levels for world-scale projects? And can you tie that to how you think the market will evolve in the 2017 to 2020 plus time frame once the career ramps up? Are you going to be jockeying for share at that facility, or do you see sort of a tighter pricing cycle as the industry tries to get back to reinvestment-level economics?

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

Good morning, Laurence. It's Fred. Obviously we see that the reinvestment economics are there in 2018 because we are going to put that facility in the Middle East. The dynamics around that will be gauged by how many of the new units in the Middle East come up, how fast the capacity ramps, and so on. But from our perspective, what you've got to keep in mind is we have got three major FCC operations, and then a partial operation around the world being a fourth, that we have very much flexibility of how we can run those operations.

So we don't have one big operation that we've just got to run flat out at all the time. So my point is where the demand is coming, where the demand for these products will be will be in the Middle East, will be in Asia, and we are investing to keep up with that. And we have the ability to throttle back on some of our other operations to be able to keep all of our customers and keep that demand/supply balance.

Laurence Alexander - *Jefferies LLC - Analyst*

And then secondly, can you give an update on where you're at in terms of your strategy by going after adjacencies in other parts of the refinery either in terms of product launches or things that we should watch for to tell us when that adjacency has become more material over the next couple of years?

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

I believe that, with the whole volatility around oil, that there are opportunities, and those opportunities are going to present themselves across the customer base that we serve. Meaning is a catalyst operation or is certain product need to stay with the refinery, or is it better suited to be the catalyst manufacturer on that side? I think those opportunities are coming. I think you should look -- when you look at us, look for us executing when those opportunities come. And at the same time, you will see us continue down the path we've done around our specialty catalyst side, with the acquisition of UNIPOL. And we are looking across that whole polyolefin catalyst and other pieces of that supply chain.

Laurence Alexander - *Jefferies LLC - Analyst*

Thank you.

Operator

Mike Sison, KeyBanc.

Mike Sison - *KeyBanc Capital Markets - Analyst*

Nice start to the quarter -- or for the year.

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

Thanks, Mike.

Mike Sison - *KeyBanc Capital Markets - Analyst*

In terms of FCC, I guess if I exclude the outage, volumes up about 5%. Given the new environment, and you talked about demand getting better, is mid-single digits the type of volume growth you could see out of FCC this year?

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

I wouldn't forecast at that level, Mike, but I think it will be higher than it has been. We have traditionally said 2% to 3%. The data that we shared about the EAI release, we've seen just in North America almost a 2.5% increase in the demand for transportation fuels since the oil price started to drop. And that feels like it should sustain. So I think it takes us maybe from that 2% to 3% range to the 4% to 5% range -- or 3% to 4% range in North America -- globally. To have that kind of volume growth, we need Europe to come up as well.

Mike Sison - *KeyBanc Capital Markets - Analyst*

Got it. And then you talked about trialing in FCC and as being a piece of some of the growth, what are you hearing from your customers? Do you think post the trialing effort, Grace will get a lot of that business or benefit from what you are doing there?

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

Mike, it's Fred. I think we will capture our fair share around that. I think there is a lot of interest. There's a lot of interest especially from the integrated suppliers, integrated back to oil because with the oil pricing dropping in that pressure on that side of it. So I am confident we will get our fair share of that side.

Mike Sison - *KeyBanc Capital Markets - Analyst*

Okay. And then last one, you talked about a separate entity post the separation that are growth projects or just initiatives that maybe you could accelerate as separate companies. Anything in particular for either the businesses that you could maybe start working on now? Or anything particular that sort of stands out as growth projects that are kind of exciting once you are separated?

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

Yes, listen. We're working on a lot of those. As they get closer, we will announce those. On a broader base, as I said, I think in construction -- around construction chemicals, to have an industry leader out there purely focused on construction chemicals and some building products, I think offer some industry consolidation opportunities. On the side of catalyst and materials, I think there's going to be some opportunities as the low oil and the volatility around that shakes out, and people look at what assets they want to have and what assets would be better off for a catalyst for a specialty player on that side of it. And there's nothing that has happened since we made the announcement that would change my thinking on that at all.

Mike Sison - *KeyBanc Capital Markets - Analyst*

Great. Thank you.

Operator

John McNulty, Credit Suisse.

John McNulty - *Credit Suisse - Analyst*

Can you quantify a little bit in terms of what the income hit was around the unplanned customer outage? I know you've highlighted it was about 2% of sales. Can you give us a little bit of color as to what was on actual earnings line?

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

You can probably do the math, John. It's a normal margin account. It was -- it's low million dollars of earnings, but I don't want to be that specific with a specific customer in mind. But it's normal margin. It's probably normal margin is all you need to know.

John McNulty - *Credit Suisse - Analyst*

Okay. So then I guess the question I have is when I look back to 1Q 2014, you had a 25% operating margin, but that was including about a $6 million headwind because of some outages around weather that you had to deal with last year. So if you exclude that, you had a 27% margin. So when I look at 1Q this year, despite less trialing, some decent volumes, your operating margin actually took a bit of a dip. So I guess I'm wondering what are some of the drivers behind that because it doesn't seem like the unplanned customer outage is necessarily accounting for all of it. So maybe you can help connect some of the dots there.

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

It was a piece, but it wasn't everything, John. Our product mix was strong last year between FCC and SC. Not quite as strong this year from a margin perspective.

The other point I will share is we did have some unexpected manufacturing costs this year. They weren't zero. We actually had some weather issues on the -- in the mid-Atlantic. One of our plants was down for a couple of days on a gas outage. It wasn't as big as a natural gas supply outage. It wasn't on the scale of last year, and -- but we did see that in incur some of those costs this year.

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

Let me also add to that. You have to step back and look at our materials -- our short-cycle businesses. In the first quarter of last year, our short-cycle businesses were running very good. Europe was -- Europe had just come out in the fourth quarter, and it was extremely strong. As you know, the second -- in the third quarter and fourth quarter this year, our short-cycle material businesses in silica and Darex, they fell off the cliff from that standpoint.

What we've done in response to that is restructured a lot of those costs down to that level of volume -- the restructuring actions we took in the first quarter and so on.

I'm cautiously optimistic. If these short-cycle businesses and materials can come back, based on some of the stimulative effects that are happening in Europe, we've got our cost position lower on that side from the restructuring. We've got some good opportunities there. But you have got to put it in perspective. That's the big piece of that side, on that material side of it.

John McNulty - *Credit Suisse - Analyst*

Great. Thanks very much for the color.

Operator

Chris Kapsch, BBT Capital Markets.

Chris Kapsch - *BBT Capital Markets - Analyst*

I have a follow-up on just the trends you're seeing in FCC demand and mix. And this may also get at the comment you just made in response to John's question about product mix. But -- so coming at it more from a mix versus pricing, I guess when oil prices were higher, you were having pretty good success like with your new product introductions, I believe, heavier resid, and also propylene yielding catalyst. So now with oil prices being down, just wondering if, as refiners shift around their crude slate mix, if you are seeing adverse mix associated with maybe shifting away from those new products. I'm just wondering if -- how you see mix playing out for the balance of 2015 in this -- against this new oil price backdrop.

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

You've got some of that dynamic continuing. The geographic location of it has changed a little bit. You are seeing a lot of heavy resid oil being processed in Asia. So we've got a lot of activity around that product -- around our heavy resid upgrading products there. You've got a lot of activity around the propylene yield type products in the Middle East. And where you are seeing more of the trialing on some of the lower end products is happening in North America.

So again, it's a mix of it. And I think that those locations or dislocations are going to continue throughout the year. And for us, as well as the industry around catalyst, we have got to be as flexible as we can, both with our product introductions and the new trials with our customers, to be able to help them through that. And that's generally a good thing.

And a lot of change keeps happening. They keep coming to us, and they are asking questions, and that's a good thing.

Chris Kapsch - *BBT Capital Markets - Analyst*

Okay. And if I could just follow up, on some of your bullish comments about demand for transportation fuels, kind of focused on North America. Obviously, intuitively Asia is a nice, secular story for growth in transportation fuels. I'm curious about Europe because European refinery rates have been down. But now, with lower oil and also with the lower euro, just wondering if there's any signs that there is -- the utilization rates there are picking up at all, if demand is picking up there for transportation fuels at all. Or is it too early to see anything positive going on there?

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

We are seeing just very small positives but not enough to really move our needle. As you know, gasoline or fuel prices generally are much higher in Europe, and so the proportional benefit of the lower crude cost doesn't flow through to the consumer quite at the same magnitude that it does in North America and Asia. And it may come later in the year. If it does, I think it's going to come more from European macro than crude prices itself.

Chris Kapsch - *BBT Capital Markets - Analyst*

Right, fair enough. Okay. And then just one quick follow-up on the silicas business, you mentioned, I think, sequential pickup in Europe in the first quarter versus the fourth quarter. I'm just wondering if you could provide any color around that. Is it seasonal, or is there any specific end markets where you are seeing a little bit better demand? Thank you.

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

In some of the industrial end markets, some of the coding side of it, not necessarily the consumer end markets yet. We are hoping -- not hoping -- we are expecting to see some of the consumer end markets start picking up in the second and third quarter. Those will be somewhat seasonal, but also from better demand. But it was the industrial side, which generally is a positive.

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

Maybe to put a little more context, we saw big drop in demand in Europe in August. It continued weaker as we finished Q3 and started Q4. And then by the end of Q4, it started to get a little better. And it was a little better still in Q1. That's the six- or nine-month pattern that we are seeing.

Chris Kapsch - *BBT Capital Markets - Analyst*

Great. That's helpful. Thanks, guys.

Operator

(Operator Instructions) Jim Barrett, CL King.

Jim Barrett - *C.L. King & Associates - Analyst*

Fred, can you talk about the residential SBM business up in North America? Was that a direct function of the winter-related storm damages on roofs, or is it too early to see the major benefit from that?

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

I think there will be a benefit from that. It is a bit early, but we did. We saw good demand pick-up in the residential side both from a product as well as distribution out there. So a lot of that product does go through our distributors, and they seem to be stocking that inventory up. So they are obviously a little bit closer to the customers than we are, but we think that's a good sign, Jim.

Jim Barrett - *C.L. King & Associates - Analyst*

Good. And then secondly, could you give us more color on how Darex packaging did in the quarter and what your outlook is for that business for the remainder of the year?

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

Yes, I mean, it was -- I don't have the exact numbers off the top of my head. I know it was down, and it was down even after adjusting for constant currency, just a couple of points on that side of it. For us, we're trying to -- we are running it to make sure it generates the amount of cash that we need. I think the big hit on the Darex side was around the Latin America side as well. Latin America from that perspective did slow down.

So we are working very hard on the cash and on the inventory side. Cash was very strong in it.

So, again, net net, it met our expectations. As we look out for the rest of the year, if we get some stimulative effects because of some of the things that are happening in Europe, in Latin America, that is consumer driven, and that could have some opportunities.

Jim Barrett - *C.L. King & Associates - Analyst*

Thank you very much.

Operator

Mike Ritzenthaler, Piper Jaffray.

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

Just a couple of quick follow-ups, one on ROIC. How much of the year on your improvement in ROIC would you say is attributable to better execution versus items like abating purchase accounting for UNIPOL and things like that? And how does that factor into your month-to-month management of the businesses?

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

The biggest single driver was earnings growth in the second half of last year as the catalyst business lapped the year before volume downturn. That was the biggest piece, Mike.

We did see improvement. I think the second biggest piece was improvements in working capital. We reduced our working capital by four -- I want to say four or five days; I've forgotten the exact number. Tania is telling me four -- four days, March 31 versus December 31. And that was a piece of it. And then there are other things running through the P&L, but those are the two biggest pieces, catalyst earnings and working capital.

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

Let me add my point to it. Because I do believe we are executing better this first quarter than we executed last first quarter. If you remember, last year we talked about we needed to get the operational issues fixed on the hydroprocessing side. Those are behind us. We needed to sort out our Verifi, and there are other things.

So just stepping back, I think the Company is executing better than we did a year ago. You should expect us to execute better in the second half as well. So that's what we're all about.

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

Sure. Absolutely. Just wanted to drill into ART a little bit more. So how did ART foot with your expectations going into the quarter? And I guess in particular, how does your outlook for ART this year foot with the narrative that HP volumes maybe particularly lumpy in 2015 with refinery utilization being so high because the project is being -- some regeneration products being pushed out?

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

It met our expectations both from internally how we operated but what the market is doing. There are big orders coming, as you said. But over this -- from what we can see from this period of time really from 2015 to 2018, we see a pretty good demand pattern especially on the hydroprocessing side. We don't have as much -- we're not as close on the distillate side. But from what we can see, the hydroprocessing side of it and around the hydrocracking -- we've got good demand out there. Some of the big projects we are talking about, those would happen probably after -- by the time they come in and so on would be 18, 19, 20, and we'll have to see.

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

Fair enough. Thanks again.

Operator

Ben Kallo, Robert Baird.

Tyler Frank - *Robert W. Baird & Co. - Analyst*

Hi guys. This Tyler Frank on for Ben. Thanks for taking the question. I was just wondering can you touch on the productivity improvements in restructuring that's currently going on there and how we should think about just the cadence of earnings growth throughout the year? I know you touched on it a little bit earlier. And then a quick follow-up after that.

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

Okay. Tyler, from a productivity perspective, these are the routine things that we do in our manufacturing operations and our back-office operations every year. They tend to build over the course of the year. And then -- and similarly with the restructuring actions, we've taken actions in Q1. There was a very small benefit in Q1. That will build. It will be bigger in Q2, bigger still in Q3, bigger still in Q4.

The way we've quantified it, we said we would be exiting 2015 at about a $20 million annual run rate in terms of savings. I would expect that we get almost all of that in Q4, meaning about $5 million. It was close to zero in Q1, and you can probably draw a line between those two points across the year.

Tyler Frank - *Robert W. Baird & Co. - Analyst*

Got it. And then in terms of just the repositioning expenses, how should we think about that in terms of the Company split?

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

Sure. So in Q1, we accrued I think it was $7 million in repositioning expenses related to the separation. That was split among our advisors. We have bankers, attorneys, accountants helping us do this work, and that's what those costs were for. You will certainly see that in Q2; it will be a big a number in Q2. And it will continue through the separation date.

Tyler Frank - *Robert W. Baird & Co. - Analyst*

Great. And then just one more quick follow-up. How should we think about the mechanics? And maybe if you guys can just provide a little bit of clarity on after the stock splits and the break-up on -- are there any lock-up periods or things like that?

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

It's premature to have that discussion, Tyler.

Tyler Frank - *Robert W. Baird & Co. - Analyst*

Okay. Thank you.

Operator

Bill Gibbons, Locust Wood Capital.

Steve Errico - *Locust Wood Capital - Analyst*

This is Steve Errico actually for Bill. Hi, guys. Congratulations on a great quarter. I may have missed this earlier, but were there any blackout periods or anything that may have dampened your stock repurchase activity in the quarter? And could you comment at all on the pace of that going forward? Thank you.

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

This was a regular quarter from that perspective, Steve. There were no special blackout periods or anything like that, no.

Steve Errico - *Locust Wood Capital - Analyst*

Okay, great. Thank you.

Operator

Okay. There are no questions at this time. So thank you for your participation in today's conference. This concludes your presentation. You may now disconnect. Good day.