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GRA - Q4 2014 W. R. Grace & Co Earnings Call

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OVERVIEW:

Co. reported 4Q14 adjusted diluted EPS of $1.37. Expects 2015 adjusted EPS to be $5.05-5.45.

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PRESENTATION

Operator

Good day ladies and gentlemen and welcome to the Q4 2014 W.R. Grace Earnings Conference Call. My name is Steve and I'll be your operator for today. At this time, all participants are in a listen-only mode. We'll conduct a question-and-answer session towards the end of this conference. (Operator Instructions) As a reminder, this call is being recorded for replay purposes.

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 Steve. And hello everyone and thank you for joining us this morning. Joining me on the call are Fred Festa, Grace's Chairman and Chief Executive Officer, and Hudson La Force, our Chief Financial Officer.

We made three announcements this morning, and will discuss each one on this morning's call. We've reported Q4 and full year results, announced a new $500 million share repurchase authorization, and announced our plans to separate Grace into two independent public companies. The earnings release, separation announcement, and corresponding presentations are all available on our website. To download copies, go to grace.com and click on Investors.

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 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 on our website. These 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 turn the call over to Fred.

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

Great. Thanks, Tania, and good morning to everyone. We do appreciate you joining the call earlier than scheduled. We have a lot to cover on today's call. We'll discuss our fourth quarter and 2014 results, our outlook for 2015, and our plan to separate into two independent companies.

We finished 2014 strong and have great momentum as we start the new year. Fourth quarter sales grew 4%, or 7% currency adjusted, and earnings grew 21%. Adjusted EPS was $1.37 per diluted share, up 26%.

For the full year, we achieved solid sales growth of 6% and earnings growth of 14%, with over $450 million of adjusted free cash flow. We expanded gross margins and adjusted EBITDA margins for the fifth consecutive year, demonstrating the strength and quality of our businesses. Return on invested capital is over 30% again, after a dip last year following the UNIPOL acquisition.

In times of increased volatility and uncertainty, we know investors prefer companies with strong business models and cash flow that will be proactive in responding to change. Our flexible global manufacturing operations, strong product technology portfolio, close customer relationships enable us to quickly adapt to changes in our operating environment.

On the cost side, we are moving aggressively to capture the benefits of lower raw material cost, and adjusting our manufacturing and supply chain operations to capture the benefit of weaker currencies in Europe and the emerging regions. The ability to design, manufacture, and run complex supply chains in different regions gives us a unique advantage during periods of high currency volatility.

In addition, in the fourth quarter, we began restructuring activities that will reduce 2015 costs by $15 million to $20 million and improve our organizational alignment and agility. And, of course, we remain laser focused on cash. Our operating and capital allocation discipline keeps me confident in our ability to continue generating strong cash flow. We've recently completed our first $500 million share repurchase authorization and this morning announced another $500 million authorization.

This is an exciting time at Grace. We are very focused on achieving our business goals this year, including the planned separation. Hudson will review the quarter and our outlook and then will discuss the spin.

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

Thank you, Fred. Fourth quarter sales were up 4% or 7% on a currency adjusted basis. Sales in North America were up 10%, and sales in the emerging regions were up 7%, currency adjusted. Currency reduced overall sales by about $25 million, or 3% in the quarter. Adjusted EBIT was $168 million, an increase of 21%. Currency reduced earnings by about $8 million, or 5%.

Adjusted EPS was $1.37 per diluted share, up 26% from last year.

For the full year, adjusted EBIT was $626 million, an increase of 14%, and adjusted EPS was $4.43 per share. Adjusted free cash flow was $452 million. 2014 cash flow includes a favorable impact of $142 million or $1.87 per share due to Grace's low cash tax rate.

Let's turn to Catalysts Technologies on page 7. As we discussed during the October call, our FCC business is primarily driven by end user demand for transportation fuels on a global basis. Our analysis shows a strong correlation between the demand for transportation fuels and the demand for FCC catalysts. Other factors, like FCC unit utilization rates, feedstock quality, and propylene production also have correlations to FCC catalyst demand. Absolute crude prices and refinery margins have little, if any, correlation to our FCC catalyst business.

Generally, lower feedstock costs, including lower crude prices, are good for end market demand. And that is exactly what we are seeing in the latest statistics. The recent reports show higher gasoline demand in Q4 in North America.

The drop in crude prices affects individual customers in different ways. Some will change the way they optimize their refineries based on the availability and cost of crude. We are commercializing a slate of new FCC catalysts to meet those changing needs. These products will be launched starting in Q1, and will complement the products launched over the last two years that were designed for customers running heavy feeds or shale feeds.

We've demonstrated over many years that our ability to innovate, to meet changing customer requirements is what creates sustainable value for our FCC catalyst business, whether that value gets measured in higher volumes, higher prices, or higher margins.

Turning to Q4 results, Catalysts Technologies had a strong quarter with good customer demand and very good margins. FCC catalyst sales volumes increased 6% year-over-year. Segment gross margin increased 690 basis points due to favorable mix, strong licensing sales, and lower manufacturing costs. This will not sustain for 2015, but we do expect full year 2015 gross margins to be in line with full year 2014 gross margins.

Let's move to Materials Technologies on page 8. For MT, sales in North America were up year over year, but down about 3% in Europe, currency adjusted. The stronger dollar reduced sales by over 4% for the segment as a whole. Despite the weaker topline, gross margin increased 130 basis points on lower manufacturing costs and improved pricing.

Please turn to page 9 for Construction Products. GCP sales increased 4% or 7% currency adjusted. Sales in North America grew 8% and sales in the emerging regions were up 7%. Earnings increased 12% with improved pricing, good operating leverage and lower manufacturing costs. Segment operating margin was 15.2%, up 110 basis points from last year. For the full year, GCP earnings and margins exceeded those reached at the prior peak in 2007.

Let me touch on the balance sheet and then our 2015 outlook. Cash at year end was about $560 million, with net debt of $1.9 billion and net debt to adjusted EBITDA leverage of 2.6 times. While the stronger dollar is a headwind to earnings, it improves our balance sheet by reducing the dollar cost of working capital and debt carried in euros and other currencies. Actions we took during 2014, including moving cash early in the year and issuing debt in other currencies, produced benefits of about $70 million in 2014.

This week, we cash settled the warrant for $490 million as expected. The settlement was funded using $240 million of cash on hand, and $250 million from the delayed draw term loan put in place for this purpose at emergence. The settlement has no net effect on leverage.

Let's turn to page 10 for our outlook. Because of uncertainty about the path and level of exchange rates, we are giving our outlook on a constant currency basis, assuming our 2014 average exchange rates, including the euro at $1.34. We'll also give you the sensitivities you need to understand how changes in exchange rates will affect our reported results.

On a constant currency basis, we expect adjusted EBIT to be $675 million to $705 million, an increase of 8% to 13% compared with 2014. And we expect adjusted EPS to be $5.05 to $5.45 per share, an increase of 14% to 23% over last year.

Assuming current exchange rates, including the euro at $1.14, we would expect a currency headwind to adjusted EBIT of about $50 million and to adjusted EPS of about $0.45 per share.

A $0.01 change in the dollar against the euro changes adjusted EBIT by about $2 million on an annualized basis, and a $0.01 in the dollar against our other currency exposures changes adjusted EBIT by about $1 million on an annualized basis.

Other assumptions in our outlook are consistent with the framework we reviewed in our March Investor Day. We assume sales volume growth of 1.5 times global GDP with a global GDP assumption of 3%. We expect gross margins to continue to grow with improved pricing, productivity, and product mix.

We expect our 2015 adjusted tax rate to be 35% with a cash tax rate between 10% and 15%. With the settlement of the warrants this week, our U.S. Federal NOL is now about $1.6 billion. With the NOL and other tax attributes we have, we do not expect to pay U.S. Federal income taxes until 2021.

We are targeting adjusted free Cash flow of at least $430 million, including capital expenditures of about $175 million to $180 million and the benefit of our low cash tax rate. The currency headwind will be significant in Q1. The dollar has strengthened about 17% since Q1 2014 and that will impact earnings for the full quarter.

We have taken a number of actions to improve results, including the restructuring begun in Q4 and the manufacturing and supply chain actions we discussed earlier. These actions will have small benefit in Q1 and bigger benefits in later quarters. Given this, we expect Q1 earnings to increase low-to-mid-single digits compared with Q1 last year.

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

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

Great. Thanks, Hudson. Now let's turn to the separation announcement starting on slide 4. As Tania mentioned, we posted a presentation regarding the separation to the Investors section of our website this morning. We'll be referring to that deck during this part of the discussion. I want to take a moment to reflect on how we got here, and why now is the right time to separate these businesses.

Over the past decade, we have created significant shareholder value by focusing on our customers, driving innovation and growth, and executing a disciplined capital allocation strategy. Over that time, we have made significant changes to improve our Company. We've grown sales, earnings and cash flow and more than doubled our return on invested capital.

We continuously assess our options for creating shareholder value. And after a comprehensive review, the Board and the management team have determined that separating into two companies is the best approach for Grace to continue to create value and grow. The time is right to create two strong, independent companies that will benefit from improved strategic focus, simplified operating structures, and more efficient capital allocation.

Turning to slide 5, we expect to create two industry-leading public companies: New Grace, which will consist of our Catalysts Technologies and Materials Technologies business segments, excluding the Darex Packaging business, and New GCP, which will consist of our Construction Products business segment, as well as Darex Packaging.

New Grace will be a global leader in process catalysts and specialty silicas with a focus on growth, margin expansion and strong cash flow. With its material science expertise and complex manufacturing capabilities, New Grace will continue to deliver high-value, differentiated technologies to maintain its global leadership positions and drive additional growth and margin expansion.

New GCP will be a global leader in cement and concrete chemicals, specialty building materials and can sealants and coatings, with strong brands and positions. New GCP will aim to leverage its independent company platform and strong free cash flow to accelerate its growth in the global construction product segments and maintain its segment leadership positions in can sealants and coatings.

Including Darex in the new company provides significant value to New GCP, including higher and more stable cash flows and margins. With Darex, New GCP can support higher financial leverage, giving it additional flexibility to pursue its growth objectives. Both companies will be led by experienced and proven leadership teams and supported by skilled employees dedicated to driving growth and delivering value to our customers.

I will continue as Chairman and CEO of New Grace, and Hudson will remain CFO of New Grace. Greg Poling, Grace's President and Chief Operating Officer, will become President and CEO of New GCP. Further details about the management teams and the ultimate corporate names will be announced later in the transition.

On slide 6, you'll see why this separation makes so much sense for Grace. Each company will have industry leading market and technology positions, with strong free cash flow and high returns on invested capital. Given the unique capabilities of each business, we expect them to benefit from a sharper focus on their unique customers and growth opportunities.

Given the different profiles and priorities of the two companies, capital allocation will be more efficient, especially for New GCP. Both companies will benefit from simplified operating structures, improved management focus, and an optimized functional support. And both companies will have the financial flexibility to pursue growth and M&A opportunities. Importantly, we believe the separation will create two unique and compelling investment opportunities with distinct investment identities and simpler investor thesis.

Now I'll turn the call to Hudson to give an overview of the businesses and provide some details on the separation.

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

Thank you, Fred. Turning to slides 7 and 8, we expect New Grace to have a best-in-class financial profile with strong cash flow and margins and the ability to pursue strategic bolt-on acquisitions, as well as acquisitions to expand its high margin, high-performance specialty portfolio.

Based on 2014 sales and earnings, without making any adjustments other than allocating current corporate costs to the two new companies, New Grace would have sales of about $1.8 billion, adjusted EBITDA of about $500 million and adjusted EBITDA margin of about 28%. Catalysts Technologies would be just over 70% of sales. Including our ART joint venture sales, New Grace sales would be about $2.2 billion with Catalysts Technologies just over 75% of that total.

New Grace is expected to have net leverage at the time of the spin of about 2.0 times to 2.5 times adjusted EBITDA. New Grace will retain most of the tax attributes of existing Grace, and we expect it to have a low cash tax rate of about 10% to 15% after separation.

Let's move to slides 9 and 10. With its global footprint and high margins and strong cash flow, New GCP will be well positioned to capitalize on its growth opportunities, including acquisitions in construction products. Darex will give New GCP better operating leverage and added financial flexibility. The two businesses already share many operating sites across the globe.

New GCP would have about $1.5 billion in sales, with adjusted EBITDA of about $260 million and adjusted EBITDA margin of about 17%. Construction Products would be about 75% of sales. New GCP is expected to have net leverage at the time of the spin of about 3 to 3.5 times adjusted EBITDA, and an effective cash tax rate of about 25% to 30% after separation.

Slide 11 summarizes some of the transaction details. We expect the transaction to be structured as a dividend of New GCP shares to Grace shareholders, and we expect it to be tax-free to Grace shareholders for U.S. Federal income tax purposes. We expect to complete the transaction in about 12 months and we will keep you updated as we progress during 2015. While each company will be separately capitalized, we expect the combined leverage to be about the same as for existing Grace.

I'll now turn the call back to Fred for closing remarks.

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

Hopefully, you can tell by our voices that we are very excited about the spin and our business opportunities this year. We're well positioned for success in 2015, and have set an exciting new strategic direction for the Company. The spin will create two strong, independent companies with improved strategic focus, simplified operating structures and more efficient capital allocation. Both companies will offer compelling investment opportunities for our shareholders. We have a long and strong track record of creating shareholder value, and this separation is consistent with the commitment to continue to create value.

With that, Operator we will open up the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) John McNulty, Credit Suisse.

John McNulty - *Credit Suisse - Analyst*

Thanks for taking my question and congratulations, sounds like a great new episode for you guys. I guess a couple of questions on the core businesses and then maybe one on the split. On the core business, the pricing in catalysts, we finally saw a tick up in the fourth quarter and they had a lot of trial pricing earlier in the year. I guess, are you through the majority of that headwind and I guess how should we be thinking about what kind of a headwind that was in 2014 and maybe how it lightens up in 2015?

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

John, you mean in terms of -- this is Hudson -- in terms of the trial pricing headwind?

John McNulty - *Credit Suisse - Analyst*

Yes, the overall trial pricing headwinds and how that may have impacted the 2014 results and how maybe that reverses in 2015.

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

We do know that we had a higher than normal amount of trial pricing during 2014. That we think will moderate as we head into 2015. As we mentioned during the prepared remarks, we do plan to launch some additional new products in response to the changing environment for our customers. So we would expect those products to be on trial pricing as they get introduced with our customers. As we think about the year-over-year changes in our P&L and catalysts, we want to watch volumes, we want to watch prices and margins and at the end of the day what we're most focused on is growing the earnings in that business. We would expect to see improvements in all three of those metrics, but exactly how that mix is going to be, we'll have to watch as we see the customers adopting these new products.

John McNulty - *Credit Suisse - Analyst*

And then on -- in the construction segment, kind of looking at how pricing has improved throughout the year, I guess how should we be thinking about that in 2015? And have you reached a tipping point in terms of kind of a level of demand that really can drive pricing going forward?

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

Yeah, John, this is Fred. The market conditions are very good. They're very good in North America. They're good in Asia as well as Latin America, Europe somewhat mixed. You know, our customers are stronger. You're seeing our customers drive pricing in cement, the fundamental underlying material and we will continue to work with them and we will continue to down our price in that segment throughout the year.

John McNulty - *Credit Suisse - Analyst*

And then maybe just on the split, just one or two questions there as well. In terms of the incremental costs that will be layered in corporate, that type of thing, I guess how should we be thinking about what -- combined between the two entities, what that incremental cost level maybe kind of when you -- once they're spun off?

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

It's day one, so it is early, but we do have a goal. We do have a goal that we know we're going to add some corporate cost on the GCP side, but we also have a goal to ensure that it's neutral across the Company. So we'll have to -- we'll have to synergize through the rest of New Grace, but our goal is to find those synergies and keep it flat.

John McNulty - *Credit Suisse - Analyst*

And then just one last question. Can you walk us through how we should be thinking about the cash flow of the new construction co or GCP? And then also, it's interesting that you've added the Packaging business to it, because it does seem like it gives it some stability, but can you kind of give us some color as to how that business, like the packaging portion of it has moved historically, whether it -- in times of good times or bad times, just so we can kind of get some clarity as to the stability of that platform?

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

Yeah, adding Darex to it gives it some stability around the cash, as we've said. It also, as you may know, shares many common facilities. It overlaps in raw material, and the business models are very similar. As you know, the construction chemical business tends to be seasonal and having Darex in it, it balances out that seasonality. So, very little capital in those two businesses required, strong EBITDA, so good steady cash flow.

Operator

Brian Maguire, Goldman Sachs.

Brian Maguire - *Goldman Sachs - Analyst*

Fred or Hudson, could you comment on whether or not you tried to sell the construction or Darex business before going the spin route and whether there were buyers interested in it? And then just a clarification on the NOLs, since it sounded like most of those would be staying with the kind of the catalysts, the [early old] Grace, will the lack of as much US income from separating them push out the timeline of recognizing those NOL benefits and does that change the present value math there?

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

We continuously look at all of our strategic options, and after a thorough review with the Board, the tax-free spin makes the most sense for creating shareholder value for both companies as well. So, we feel this is the most efficient and effective way to do this.

Hudson on the NOLs --

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

Brian, your analysis is right. The NOL will stay with New Grace. We do think it will continue to shelter income through about 2021.

Brian Maguire - *Goldman Sachs - Analyst*

The pushing out of some of the US income to the spin co, that won't have any of the NOL attributes associated with it, Is that correct?

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

No. New GCP will have a -- what I'll describe as a regular tax rate. I think we put 25% to 30% in the materials.

Brian Maguire - *Goldman Sachs - Analyst*

And maybe give an idea of what you think that the Construction and Darex business could do better on their own that they couldn't do within the existing portfolio? Are there [giving] more opportunities for acquisitions or organic growth that they just haven't been able to pursue in the last couple of years?

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

Yes, as you run a conglomerate of portfolios, you're always making trade-offs and at the end of the day, the trade-offs are made at the corporate level. Having GCP and Darex -- New Grace separate, I believe you will see New Grace pursue a very active and robust acquisition profile in the industry segments around construction. That will be a big push. I also believe that you will see a less complicated overhead structure associated with that business, just given the complexities of it. So, again, we're excited about it and after a lot of deliberation, a lot of looking at it, we feel very good where we're positioning.

Brian Maguire - *Goldman Sachs - Analyst*

And just one last one if I could on the catalyst -- the new catalyst products you're plan on introducing. Could you comment just on the nature of the innovation there? I think we've heard some from some other folks that customers were looking to maybe trade down a little bit on their catalysts. Is this in response to that and maybe reducing your cost for making the catalyst, to hold margin in that environment or functionally is there some kind of a new value that you're providing to the refineries?

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

We want to be responsive to the cost pressures that our customers are getting, based on the changing slates of crude, and we'll work with them on trading off maybe some activity of these catalysts versus cost production. So, that's around the new prices -- or new products that we're looking at.

Brian Maguire - *Goldman Sachs - Analyst*

Okay, thanks very much.

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

Four of those new products will be introduced in the first quarter.

Operator

Laurence Alexander, Jefferies.

Laurence Alexander - *Jefferies - Analyst*

Two questions, first, can you give a little bit more detail on what you're seeing in the order trends for material technologies and particularly what you're seeing coming into the first quarter by end-markets? And secondly, what are the cash costs for separation? I mean, you'll have to do some restructuring to offset any stranded cost, so what's the sort of net cash outlay we should assume over the course of 2015, 2016 to implement this?

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

Good morning Laurence, it's Fred. Let me give you some perspective on the materials side. We saw around the materials business strong demand, both in the US and in Asia in the fourth quarter, a tail-off -- significant tail-off in the fourth quarter. As we look in January, again it's early in the year, we saw a small pickup in Europe, not a dramatic pickup, but nonetheless a small pickup. So we're cautiously optimistic that some of the things that are happening in Europe will continue to create some of the stimulus.

Hudson, I'll let you --

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

Laurence, we will certainly have transaction costs and restructuring costs as part of this. As Fred commented earlier, it's day one and we're not able to comment publicly on exactly what we think those costs will be, but we'll certainly keep you posted as we better define them over the coming months.

Operator

John Roberts, UBS.

John Roberts - *UBS - Analyst*

You're supposed to wait till after the activists goes into your stock before you do the split. You used the term net leverage to EBITDA and not net debt to EBITDA. Is there a reason for the change, the different language there?

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

I may have misspoken, John. The metric I meant to quote was net debt to EBITDA.

John Roberts - *UBS - Analyst*

And you mentioned that there was integration between Construction Products and Darex and that they share several sites. Are there integrated material streams between -- common to the businesses as well? I mean, how separable are those two businesses?

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

No, there are common streams, both -- especially on the oil-derived products.

John Roberts - *UBS - Analyst*

And does the NPV of the NOLs go down materially at all, because you'll use them a little more slowly, since [growing] on one side of the Company?

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

We don't really know for sure, John. As I responded to Brian's question, our best view is that we'll continue to use that NOL through 2021. But again, that's something that we'll fine tune as we go forward in the next few months and we'll keep you all posted on that.

Operator

Mike Ritzenthaler, Piper Jaffray.

Mike Ritzenthaler - *Piper Jaffray - Analyst*

Just a couple questions on the spin. I guess I'm just curious about the -- trying to get a sense of New GCP's geographic footprint. Obviously, you've got in the slides the pie chart there, but how much of Darex business is Europe and emerging markets? Just kind of curious about what that composition will look like.

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

Yeah, it's very similar to the Construction. It almost overlaps directly on that geographic pipeline -- on that geographic representation.

Mike Ritzenthaler - *Piper Jaffray - Analyst*

And then a couple of questions about the quarter and the outlook. On your expectations for UNIPOL in 2015, can you just kind of qualitatively bring us through how specialty catalysts and UNIPOL's overall contribution in catalysts earnings growth in 2015 matches up?

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

Mike, this is Hudson. We see the polyolefin catalyst business growing in line with demand for plastics. We think that's roughly 5% a year. We would see that for both the legacy polyolefin catalyst business and the catalysts that we -- the additional part of the portfolio that we picked up with the UNIPOL acquisition. On the licensing side that business is lumpy. We had a strong licensing year in 2014, and we'll have to see, we've got a number of opportunities this year, but it's too early to know for sure exactly the timing of those opportunities.

Mike Ritzenthaler - *Piper Jaffray - Analyst*

Yes, that makes sense. And then maybe just a follow-up on ART, are there any expectations that ART might be a little bit lumpier than usual, given the move in crude prices? I mean, could refineries try to stretch the life span of their nickel catalyst spreads?

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

Yes, it's a possibility, but as you saw, we had a very strong fourth quarter in ART, which we were talking about all year to getting it back on the pace and our expectations for ART in 2015 are double-digit growth and we've got pretty good visibility on it.

Operator

Mike Sison, KeyBanc.

Mike Sison - *KeyBanc - Analyst*

In terms of 2015, you gave us what -- New Grace EBITDA is new GCP. Can you help us bridge the gap, what exactly -- or can you correlate the growth you have for 2015 to the new segments in terms of what type of constant currency growth you expect from each?

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

Mike, just to be clear, the data we gave for New Grace and New GCP this morning was just taking our 2014 P&L and splitting it into two pieces. In terms of giving forward-looking information on New Grace and New GCP, we're just -- we're not ready to do that this morning. I'm happy to talk about our expectations for Grace for 2015 of course.

Mike Sison - *KeyBanc - Analyst*

And then in terms of the pension -- underfunded pension, how does that split between the two segments -- two businesses?

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

Yes, Mike, it's a good question. Our pension is very well funded, this is the US pension I am referring to, it's 90% funded. That benefit obviously goes to employees in both organizations. Our intention would be to split that plan between the two companies, but that's something that we're going to have to work on over the coming months.

Mike Sison - *KeyBanc - Analyst*

And then just a quick one on FCC catalyst, you had a strong second half in that business. Can you talk about how the first half sort of looks in that business? And then in terms of pricing, what are your thoughts there as you head into 2015 as the industry tightens up a bit?

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

Mike, it's Fred, morning by the way. We saw good demand in the fourth quarter. We're starting the year with demand -- demand has been steady. We haven't seen any dislocation through any of the oil volatility. Our first half will generally be a very good first half. Now, does the first half always reflect turnarounds and other incidences? Sure. But everything that we see so far that we'll have some steady progress in the first half of this year.

Operator

Roger Stitz, Bank of America.

Roger Stitz - *Bank of America - Analyst*

For the warrant settlement, was the $250 million delayed drawn post the December 2014 balance sheet?

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

Yes we drew it last week.

Roger Stitz - *Bank of America - Analyst*

The bonds, the current bonds, will they go with New Grace, or stay with New Grace?

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

Yes, they will stay with New Grace.

Roger Stitz - *Bank of America - Analyst*

So what will happen with the term loans, will they be -- I mean it looks like you will need to [do something like] this, but refi them at about the same amount level and then issuing new term loans or I guess potentially bonds at New GCP, leaving little other debt at New Grace?

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

Yes, that's essentially right. We do expect New GCP to borrow fresh debt capital at the time of the spin. We would expect New Grace to substantially pay down the current credit, term loans and there'll be a process associated with that as we get closer to the actual spin.

Roger Stitz - *Bank of America - Analyst*

A question on each of those. Do you think you'll actually completely take out those term loans, so there is no secured debt, or material secured debt at New Grace?

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

No, I would expect New Grace to still have some secured debt, the exact amount we'll be able to better estimate as we move forward. But I think there'll still be something.

Roger Stitz - *Bank of America - Analyst*

And for New GCP, maybe it's early to thing about the capital, how it's financed, but do you think it might just be loans or do you think you might look at doing some bonds there, high-yield bonds there?

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

Too early for us to really make that estimate, [Rodger].

Roger Stitz - *Bank of America - Analyst*

Last question, any view of the rating agencies thinking in terms of what New Grace's rating might look like, are you focusing on strong BB or do you think there is a opportunity to be IG?

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

We have started discussions with them, but it wouldn't be appropriate for me to comment. I wouldn't want to be ahead of their thinking on that.

Operator

Jim Barret, C.L. King & Associates.

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

Good morning and congratulations on the announcement this morning.

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

Thanks Jim.

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

Fred, my first question, the Abu Dhabi FCC catalysts and additive plant, could you give us an update as to when that will come on stream? What are your current assumptions? Any changes in the outlook, given what's happened to the price of oil?

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

No, we're going through the engineering on it now. We've got some infrastructure going in. You'll see silos if you drive by there and I encourage you to drive by there, Jim. You would see silos that are coming out of the ground and so on, but our expectations are, you know, by the end of 2017, this plant will be up and running.

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

And the number of FCC units being built in the region, are they still the same as your original assumption?

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

Yeah, the Takreer is the big unit. We see no change in it. I know there is other units being talked about. I think once all the oil volatility settles out, I think business will be as usual, but we'll look. We constantly continue to look at it.

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

Moving onto GCP, a number of cement and concrete manufacturers are taking healthy price increases. Has Grace announced pricing for their concrete and cement products in North America?

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

Yes, we have. We're selectively working with our customers, as well as in other regions around the world. The market has become healthier and it's a good time on the construction side for all.

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

And are those price increases somewhere between what, 5% and 10%?

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

Jim, I don't want to speculate, because we're working through that with our customers now. We'll give you a better flavor as we hit the high construction season in the second quarter.

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

Okay, Fred, my last question. My recollection was that Grace Construction Products especially had a number of petroleum-related inputs. Will there be material savings in terms of input cost for that business in 2015.

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

Yes.

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

And therefore that, in and of itself, aside from pricing should help margins, right?

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

We would hope so, yes.

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

Jim, the GCP's raw materials are about one-third derived from crude, obviously not first level derivatives, but down the supply chain.

Operator

Chris Kapsch, Topeka.

Chris Kapsch - *Topeka Capital Markets - Analyst*

A few questions. Just on the tax-free nature of the spin, just wondering if, assuming it happens say January 1, 2016, does that -- in order to preserve the tax free ruling, does that preclude either entity from being subject to a change of control for like a period of two years, can you comment on that?

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

Chris, there are tax rules that address those types of issues. It's not something that we would want to get into in a call like this, but there are some rules that address that, and you know our focus is on executing what we've announced this morning. We are excited about this opportunity. We think it sets up two very strong companies to pursue their growth agendas, that's what we're focused on.

Chris Kapsch - *Topeka Capital Markets - Analyst*

And if you -- looking at new co, the Catalysts business with some -- the materials tech, putting the 2 to 2.5 times leverage on that entity, and given that entity will have sort of the lion's share of benefit from the low tax rate, you're effectively freeing up a little bit of capacity for M&A it appears. I am just wondering, can you talk about what were the focuses in terms of what type of targets and what the capacity might be, what the bite size potential would be, and would it be something more complementary to the existing businesses? Are you thinking does this split also open up the possibility for doing more acquisitions in kind of like the white space catalyst market?

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

I think the opportunities on the M&A side are going to be abundant as we go forward. I think this whole dislocation in oil is going to open up opportunities across companies on that side of it and we're going be well positioned to take advantage of that. I also believe the split will open up some opportunities around the materials space, around the silica space and the other inorganic materials to take advantage. So, we're going to be -- we will be, as we've always been, aggressively looking at those acquisitions to add growth to it and we will be in a good position to do that.

Chris Kapsch - *Topeka Capital Markets - Analyst*

And then sort of conversely on the GCP side, with a little bit more leverage and I understand it's less capital intense, but that entity won't have the benefit of the low tax rate it sounds like going forward. So just wondering, what's the ideal capital structure for that entity and is there really any capacity for M&A? I thought you mentioned that they would also be pursuing an M&A pipeline, but it just seems like, given the leverage, there is not as much capacity there or opportunity there?

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

Now there is. Don't misconstrue that. With a leverage of three times and as you know, it has very little capital, these businesses on an M&A side, the GCP side, offer themselves up for a substantial synergies when you acquire these type of businesses. They're primarily light asset intensity with a high customer cost to serve and as you go combine two of these companies, you generally get very quick, very good synergies on the cost to serve side. So, no, we're very much focused on growing this through acquisition.

Chris Kapsch - *Topeka Capital Markets - Analyst*

And then just finally, just in the fourth quarter results of the catalyst business, very impressive gross margin performance and operating margin performance. You mentioned a couple of the drivers there. I was just wondering, given the timing of the UNIPOL acquisition [last year] or I guess in end of 2013, I'm wondering how much the high margin royalty stream from that business contributed to that margin variance or maybe if you could just talk about the contributors to that year-over-year performance in general? What buckets contributed there?

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

Let me -- I'll address it on to the full year. Chris, this is Hudson. UNIPOL added a point or maybe 1.5 points to gross margins for the year. The licensing business does bring a strong margin with it. The polypropylene catalyst is a higher margin than our FCC catalyst and that's about the rough order of magnitude. What we saw in Q4, it was, we did have additional licensing sales in Q4. We saw good productivity flowing through the P&L. And we had a strong mix between polyolefin and FCC catalysts.

Operator

Patrick Duff, Gilder.

Patrick Duff - *Gilder - Analyst*

Congratulations, by the way. It's great news. First, going on the slide you provided for the GCP business, it looks back-of-envelope free cash flow for that segment in 2014 would have been, ballpark, $150 million out of the $450 million. Is that kind of a good way to look at that just looking at the capital intensity and prospective debt? I am not trying to pie down to $150 million exactly, but just ballpark?

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

Yes, that's the right ballpark, Pat.

Patrick Duff - *Gilder - Analyst*

Second, you'd called out the flexible manufacturing footprint, particularly, I'm thinking about the catalyst business and with the volatile currency markets too, how much real flexibility do you have to move some of the sourcing between your different manufacturing facilities that some of your competitors do not have that advantage? What can you actually take advantage of there?

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

Yes, it's a great question, Pat. As you may know, the majority of catalysts sold outside of direct Europe is US denominated, into Asia, into the Middle East. We have, as you know, a state-of-the-art catalyst plant that can make FCC catalysts, specialty catalysts, as well as silica based in Worms. It's our newest, most productive facility that we have, and our ability to make those products in Worms with the currency -- with the currency arbitrage that's going on, and sell those products around the globe does give us an advantage. We need to take advantage of that, we need to set our supply chains up on that side, we need to get our products there, but we do have that inherent advantage and it's a big benefit for us.

Patrick Duff - *Gilder - Analyst*

And then just last one, real quick, 12 months to affect this spin just seems a little bit long. I know you just announced it and there's a lot to do, but is 12 just being conservative, is it possible this could -- transaction could happen a little sooner than that?

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

It is possible, Pat. As you said, it's day one, and we've got a lot to accomplish. It could be a little sooner. It could be a little longer. Just we're going to have to get into it and see. We're excited about this, we want to make it happen as fast as we can. But as you said, there's a lot that has to happen.

Patrick Duff - *Gilder - Analyst*

Okay, great. Well, I know you guys will take care of it. Appreciate it.

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

Thanks Pat.

Operator

(Operator Instructions) Jake Kemeny, Prudential.

Jake Kemeny - *Prudential - Analyst*

Hi, good morning. Thanks for taking the question, but [Rodger] already asked it for me some of that. Thanks.

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

Okay, then why not we conclude the call.

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

Great. Operator, thank you, and we just want to thank everyone on the call again for your flexibility last minute to join us this morning. If you have any follow-up questions, you can reach me at 410-531-4590 or David Joseph at 410-531-8209. Thank you again and have a great day.

Operator

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