THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

GRA - Q2 2014 W. R. Grace & Co Earnings Call

EVENT DATE/TIME: JULY 23, 2014 / 03:00PM GMT

OVERVIEW:

GRA reported 2Q14 sales of $838m and adjusted EPS of $1.22.

CORPORATE PARTICIPANTS

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

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

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

CONFERENCE CALL PARTICIPANTS

Brian Maguire *Goldman Sachs - Analyst*

Mike Ritzenthaler *Piper Jaffray - Analyst*

John McNulty *Credit Suisse - Analyst*

Robert Walker *Jefferies & Company - Analyst*

Ben Kallo *Robert W. Baird & Company - Analyst*

Jim Barrett *CL King and Associates - Analyst*

Chris Kapsch *Topeka Capital Markets - Analyst*

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

PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Q2 2014 W. R. Grace & Co. earnings conference call. My name is Sarah and I will be your operator for today. (Operator Instructions). And just as a reminder, this conference is being recorded for replay purposes.

I would now like to turn the conference over to Mark Sutherland, Vice President of Investor Relations.

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

Thank you, Sarah, and hello, everyone, and thank you for joining us today, July 23, 2014, for a discussion of Grace's second-quarter 2014 results released this morning. Joining me on today's call our Fred Festa, Grace's Chairman and Chief Executive Officer; and Hudson La Force, our Senior Vice President and Chief Financial Officer.

Our earnings release and corresponding presentation are available on our website. To download copies, go to grace.com and click on Investor Information. A link to the slide deck is available under the Events Navigation tab.

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

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

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

And with that introduction, I will now turn the call over to Fred.

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

Great. Thanks, Mark, and good morning to everyone, and thank you for joining us. I'm very pleased with the progress we made this quarter, and the momentum we've created to start the second half of the year.

In the second quarter, our sales grew 4% and adjusted EBIT increased 8%. When you look at our catalyst technologies, sales grew 8%. Our UNIPOL polypropylene licensing and catalyst business had a strong quarter, contributing $30 million to sales and $11 million to segment operating income, after acquisition-related cost of about $1 million. The integration is complete, and we're on track to deliver our synergies.

In addition, our specialty catalyst business had good sales volumes as feedstock-advantaged polyolefin producers in North America and the Middle East operated at high plant utilization rates. Based on our current order visibility, we expect this business to grow nicely in the second half of the year.

In our FCC business, the fundamentals are trending favorably. Our FCC volumes were up slightly from the strong year-over-year ago quarter. Sequentially, volumes increased 10% due to good penetration of our new products and increased sales addition rates.

We see continued good demand for a refining catalyst, driven by global growth in gasoline demand, the use of heavier feedstocks, and the growing use of FCC units to produce propylene for petrochemical feeds. US refineries are seeing strong utilization rates, approaching 90%, and are cost-advantaged. As noted last quarter, utilization rates for European refineries are below 80%. But we saw good sequential improvement in FCC demand as customers adjusted their operations to improve profitability. Catalyst technologies had very strong gross margins this quarter, helped by strong FCC catalyst volumes and above-average UNIPOL licensing revenue. This shows the progress we've made in restoring our margins.

Materials technologies also had a very solid quarter. With 3% topline growth, the business delivered an 11% increase in operating income. The engineered materials business was up almost 7%, or 2 times projected global GDP, due to strong demand growth in coatings and consumer applications.

Packaging technology sales were up mid-single-digits in North America and Europe, but those increases were more than offset by lower sales in Asia and Latin America. Sales growth for this segment is meeting our expectations, and the business is consistently demonstrating progress in its new product and productivity programs. We expect this business to continue to improve sequentially through the year.

In our construction product segment, we saw good growth for specialty construction chemicals; but specialty building material sales were below expectations, especially in North America. Specialty construction chemicals performed as expected, with 7% growth in advanced regions, including 6% growth in North America and 5% growth in Western Europe. Demand was flat for FCC products in Latin America, possibly due to the World Cup, reducing emerging region growth. Specialty building material sales were off 7% in North America.

US commercial construction activity has been weaker than we expected. We've seen delays in projects and lower residential re-roofing activity. We expect better sales in the second half, although we'll need to see improved commercial construction and infrastructure spending in the US and other markets. The drivers seem to be in place, and we're focused on delivering our project pipeline.

We have good momentum as we start the second half of the year. Our improvement in catalyst technologies, continued strength in materials technologies, and good opportunity in construction products makes me confident that we'll achieve our second-half goals for growth, margins, cash flow, and return on invested capital.

With that, I'll turn it over to Hudson to give you some more specifics on the quarter.

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

Thank you, Fred. Please turn to pages 4 and 5, and we'll start with a quick review of Grace's overall results for the quarter. Sales were $838 million, an increase of 4% from last year. Segment gross margin was 38.6%, an increase of 80 basis points. Adjusted EBIT increased 8% to $166 million. Adjusted EBIT margin increased 70 basis points to 19.8%. And adjusted EBITDA margin increased 100 basis points to 23.9%.

Adjusted free cash flow was $178 million for the first six months, up $21 million or 14% from the year-ago period. Adjusted EBIT ROIC was 27%, and on track to exceed 30% this year. Adjusted EPS was $1.22, based on diluted shares of 76.8 million. Per-share earnings included $0.11 of non-cash interest accretion on the DPO, and $0.50 related to the difference between our full-year book and cash tax rates. Together, these two non-cash items total $0.61 per share.

Let's turn to catalyst technologies on page 6. Second-quarter sales for catalyst technologies were $313 million, up 8% from last year. Sales volumes increased 9%. FCC catalyst sales volumes increased 1%, versus a strong Q2 last year, and 10% sequentially. Specialty catalyst sales volumes increased 33% year-over-year, largely due to the UNIPOL acquisition, and double-digits sequentially.

Catalyst gross margin was 43.6% for the quarter, up from 42% in the prior-year quarter. The increase was due to higher licensing sales, improved FCC volumes, and improved pricing in our polyolefins business.

Looking forward to Q3, we expect licensing sales to return to more typical levels, and our FCC volumes will be affected by a 10-day partial turnaround at our Lake Charles facility.

Segment operating income was $98 million, a 4% increase from last year. The strong UNIPOL results offset $6 million in lower ART income. Q2 was ART's strongest quarter last year, but we expect it to be the weakest quarter this year.

FCC market fundamentals are trending favorably, with high refinery utilization rates in the US and some emerging regions more than making up for lower rates in Europe. These high refinery utilization rates, plus the effect of new refineries, increased use of heavy crudes globally, and increased production of propylene, are all driving demand for FCC catalysts.

We project capacity utilization for higher-technology FCC catalysts to continue to tighten through year end. We're pleased with the performance of our new FCC catalyst technologies, introduced to address our customers' requirements for processing shale and heavy resid feeds and propylene maximization. Customer adoption rates are ahead of our plan.

We made good progress improving the profitability of our ART joint venture in Q2, and expect much better second-half results. We've reduced costs, and are making other changes to make the business more effective and more profitable.

Looking forward for the segment as a whole, we expect a stronger second half. We'll continue the sequential recovery of our market position in FCC catalysts; we've completed the integration of UNIPOL; and we expect much better sales and earnings in ART. We continue to expect low-double-digit growth for segment sales and earnings compared with 2013, and full-year operating margin in line with 2013.

Let's move to materials technologies on page 7. Second-quarter sales for materials technologies were $236 million, an increase of 3% from last year. Sales of engineered materials increased 7%, due to a 4% increase in sales volumes, favorable currency translation, and improved pricing. Sales in advanced and emerging regions grew at similar rates, with good demand in coatings and consumer market applications.

Sales of packaging technologies declined 1%, as lower sales volumes more than offset improved pricing. Sales in emerging regions have been volatile for several quarters in this business. With the uncertainty in demand growth, we have focused more on margin improvement and returns on investment in this business. The segment gross margin was 35%, up 130 basis points, driven by improved pricing, lower manufacturing costs, and higher sales volumes.

Segment operating income increased 11% to $50 million. Segment operating margin was 21.1%, up 150 basis points from the prior-year quarter.

Last quarter, we advised of difficulties we were experiencing importing raw materials into Venezuela. Since then, we have mitigated some of these issues. But sales are down from last year, due to this material availability issue and other local economic factors. We expect continued uncertainty in this market, and will update you again as circumstances change. Venezuela represents about 2% of segment sales.

Please turn to page 8 for construction products. Second-quarter sales for construction products increased 2% to $289 million. Pricing improved 2%, and sales volumes increased 1%, partially offset by unfavorable currency translation. Sales of specialty construction chemicals increased 4%, led by 7% growth in the advanced economies, including 5% to 6% growth in North America and Western Europe. FCC product sales in the emerging regions increased only 1%, largely due to flat demand in Latin America.

Sales of specialty building materials decreased about 1%, primarily due to a 7% decline in North America. Fred covered this business in his remarks, but I want to add one more point. As our global SBM business has grown, it has become more focused on larger commercial and infrastructure projects. Since sales are tied to the start and continuation of these projects, we have seen more volatility in our SBM order patterns. We're actively investing in improved processes and tools to help our commercial teams manage these project pipelines.

Segment gross margin declined 60 basis points to 36.2%, primarily due to higher manufacturing costs and weak product mix. Segment operating income was flat with last year, at $45 million. In addition to weak SBM performance, earnings growth was affected by $2 million in one-time items last year, including the favorable settlement of a patent dispute and the sale of chemical dispensers following an account transition. Excluding these one-time items, segment operating income would have increased about 5%, and segment operating margin would have increased about 40 basis points.

We are repositioning our Verifi process control technology business. Market adoption has been below our expectations, and the business is not producing the returns we want. As a result, we have decided to operate Verifi as a more targeted niche offering, and have reduced our investment in growing the business. In Q2 we recorded a $10 million asset impairment charge and a small restructuring charge.

With year-to-date construction spending weaker than we expected, we have become more cautious in our outlook for our construction products business. While we see positive leading indicators, like improved cement and concrete prices, other industry data suggest that nonresidential building and infrastructure activity, especially in the United States, is below the pace we expected. Our own business is providing mixed data, with strong SCC demand and improved pricing, but weak SBM demand in the US.

Q2 saw 20% sequential growth from Q1. This is normally a positive sign of strong construction growth, but following a very weak Q1, this sequential improvement was less than we expected. Until we see stronger demand signals, we have reduced our construction products growth estimate to mid-single-digits for this year.

At the Grace level, adjusted free cash flow for the six months was $178 million, 14% ahead of last year. Capital spending for the first six months was about $80 million. We've lowered our capital spending estimate for the full year to $160 million to $170 million, as we optimize the timing and priority of our growth and productivity investments.

Cash on the balance sheet at June 30 was $284 million, with net debt of approximately $1.9 billion. Net debt to trailing 12 months adjusted EBITDA is about 2.7 times as of June 30. In Q2, we spent about $173 million to repurchase 1.8 million shares, at an average repurchase cost of about $94 per share. Year to date through yesterday, we have spent $257 million to repurchase approximately 2.7 million shares. When our stock price declined in Q2, we increased the rate of repurchases. In recent days, with the increase in our stock price, we have reduced the rate of repurchases, consistent with our disciplined capital allocation model.

Following emergence, we took a fresh look at retiree benefits. In Q2, we announced the termination of certain retiree benefits that were no longer economic for us to provide. In Q2, we recorded a gain of $7.9 million related to these changes. Of this amount, $4.7 million is included in adjusted EBIT as the amount related to current employees and retirees of current businesses. The remaining $3.2 million is excluded from adjusted EBIT, as it relates to retirees of divested businesses.

Let's discuss our outlook, and then we'll open the call for your questions. When we set our adjusted EBIT outlook in February, we noted that it was a broader range than usual due to higher uncertainty about the macro environment and emerging region growth. At this point in the year, we have better visibility to the full year and are narrowing our adjusted EBIT outlook to $620 million to $640 million, consistent with our comments on our April earnings call.

We're more positive about catalyst earnings, but more cautious about construction earnings. We expect Q4 earnings to be higher than Q3 earnings, due to two factors in our catalyst technologies business: the Lake Charles turnaround will affect Q3 but not Q4; and we expect ART sales to be higher in Q4 than in Q3.

With that, we'll open the call for your questions.

QUESTION AND ANSWER

Operator

(Operator Instructions). Brian Maguire, Goldman Sachs.

Brian Maguire - ***Goldman Sachs - Analyst***

Just wanted to start off asking about pricing in catalyst, and FCC in particular. I think it was down again about 2.5% in the quarter. I know it's been an area that's been under some pressure lately. But just wondering what your outlook is for that for the rest of the year, and what factors might cause it to see some positive pricing again.

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

Yes, Brian, this is Fred. You've got to look at FCC. We portrayed our total catalyst pricing as down 2.6%, which has UNIPOL and everything else in it. FCC catalyst, sequentially, first quarter to second quarter, was essentially flat. It was just down less than 1% on that basis. And that's really just some of the trial pricing. So we have seen a stable level on the FCC pricing side of it.

Brian Maguire - ***Goldman Sachs - Analyst***

Okay, great. And then just on the earnings in catalysts for the quarter, I think they came in a little bit better than you had been indicating. Prior, you talked about them being a little bit down year-over-year. Just curious what some of the factors behind that margin improvement was, and whether they are sustainable.

And then just thinking about the full year, I think you would have done $99 million or so without the $1 million acquisition costs in the quarter. It looks like, at that level, you are already run-rating a pace for about 12% growth for the year. Is that about the right number to be thinking about?

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

Well, let me give you some qualitative -- we felt very good about our catalyst performance in the second quarter. Some of the productivity that hit; our adoption in our FCC; new products. Going from trial to permanent is about 90%, which is very good. And we're seeing some good experience on that side of it, coupled with the specially catalyst side. You put all that together, and despite having ART down $6 million, we had some very nice growth, very nice growth.

So, what will it be for the second half of the year? We expect it to continue to be positive and continue to grow. We've got very good order pattern, in looking out at our specialty catalyst volumes. We feel good about the FCC side of it, as Europe has stabilized. And the UNIPOL acquisition is doing just what it said.

And on the last point, all the progress we've made over this last 3 to 4 months around ART gives us the confidence that it will return back to the levels in the late third quarter, and dramatically in the fourth quarter.

So, I know I didn't answer your question on what percent it's going to be.

But Hudson, maybe you've got the numbers.

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

Brian, we've said that we expect full-year catalyst growth to be low-double-digit sales and earnings. And you can factor that into your thinking, of course.

Brian Maguire - ***Goldman Sachs - Analyst***

Okay. I'll get back in the queue. Thanks.

Operator

Mike Ritzenthaler, Piper Jaffray.

Mike Ritzenthaler - ***Piper Jaffray - Analyst***

Can you help me reconcile the organic volume growth in catalyst? So, volumes were up 8% or 9% overall. But if UNIPOL (technical difficulty) 10%, if I'm reading the press release correctly, one might conclude that there had to be some volume decline somewhere else in the portfolio. But FCC was up 1%, specialty -- both of these were up year-over-year. Is that correct, and how do those two numbers fit in, organically and inorganically?

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

Yes, I think you're doing the analysis right, Mike. The legacy SC business was down slightly versus last year. This was order patterns. And so you get a year-over-year compare there. The way we think about it, really, is how is the business operating sequentially? We had very strong sequential growth in FCC catalysts.

As you know, last year in Q3 was the down quarter in FCC catalyst. From Q3 to Q4, from Q4 to Q1, from Q1 to Q2, we've seen very strong sequential progress in that business. I think FCC from Q1 to Q2 was up 10% sequentially. In SC, the same analysis: from Q1 to Q2 this year, the SC business was up double-digits sequentially. And so, as Fred said in his comments, we feel very good about the momentum we've got in those two businesses going into the second half.

Mike Ritzenthaler *- Piper Jaffray - Analyst*

Yes, that makes sense. And then on construction, quickly, we found the construction volume growth year-over-year particularly strange. And your prepared comments I think helped clarify some of that. But is there something more tangible that can help explain the North American performance? And maybe the spirit of the question is how transient those effects might be, and whether they're likely to continue to be volatile like this for, as far as you can tell?

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

Yes, if you look at the chemical side, which is generally the precursor, the chemical volumes were very good in North America, up 6%. And we're getting pricing on that side, and our customers on the cement piece, as well. We've got a number of large projects on the commercial infrastructure side in North America that we've got visibility where, from an architectural side, our product's been spec'd in. It's the timing of when these projects get released, and when they get funded, started, released, and so on, on that piece of it. And we're trying as much visibility as we can.

Overall, where we sit today, we think it is a timing-related issue. It's not a suddenly these projects have stopped issue. We haven't seen that. And if they had stopped, we would probably see it on the chemical side. So, at this point, we're looking at it as timing of these large projects.

When we look outside North America, we're similar. We've got the large project in Australia that has been -- the Wheatstone, the LNG project -- that's a huge project. There's been a lot of publicity on it. It's been a little bit slow, a little bit delayed on that piece.

The only one that does perplex us a little bit, to be candid, is the residential, re-roofing business we have in North America. Given the tough winter, we thought it would have been a big pick-up at this time. And we're getting varying factors on it. Do we have enough -- are there are enough subcontractors to do it -- the pick-up? Is it a timing on stocking the channel? But that's how we're looking at it.

Mike Ritzenthaler *- Piper Jaffray - Analyst*

Okay. Fair enough. Thank you very much.

Operator

John McNulty, Credit Suisse.

John McNulty *- Credit Suisse - Analyst*

So, with regard to the catalyst business, it sounds like you're getting maybe even better than expected, or better that you were expecting, in terms of traction on some of the newer products that are coming in. And they've been commercialized, and you're actually getting them purchased pretty solidly here.

So with that in mind, should we -- how should we be thinking about the pricing and/or price mix for the catalyst business as we push into the second half of the year? Should it be positive, moderately, solidly? How should we be thinking about that?

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

I think there are two ways to think about it, John. One is as these products move through the adoption pipeline, from trial phases into full commercialization, that there's an improvement in pricing there. Typically, a trial is done at a different price than the final commercial prices. We should benefit from that as we move through the adoption cycle, as I said.

I think the other thing that obviously we're focused on is, as the FCC catalyst market tightens -- it is tightening -- we think it will tighten further. That gives us an opportunity to do some targeted pricing, where we've got the clear value-add with our customers on these new technologies.

John McNulty *- Credit Suisse - Analyst*

Okay, fair enough. And then with regard to the ART platform where you were highlighting some weakness that you're seeing there, can you walk us through what the major issue is? And then also your thoughts on the timing of when we might see this weakness slow up, and maybe even reverse itself.

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

Yes, let me just reiterate. The market dynamics are strong on the hydroprocessing side, both from the distillate, the clean fuel side, as well as hydrocracking and as well as the fixed bed side. Our issue was some of the product development costs that we were experiencing got out ahead of our self in some of the new products, as well as some of the operational issues that we highlighted in the first quarter.

We feel those operational issues are behind us. We also feel that we've got the cost in the new products matched, and we'll see the recovery in the second half of the year, and more predominantly in the fourth quarter. So it's not a market issue. It's more of our own internal issues.

John McNulty *- Credit Suisse - Analyst*

Okay, great. Thanks for the clarity.

Operator

Robert Walker, Jefferies.

Robert Walker *- Jefferies & Company - Analyst*

I just wanted to clarify a few of the comments on FCC. What progress, percentage-wise, have you made in recovering the volume that you lost last year? Have you got it all back? If not, when do you expect to, and by when?

And then on the new products, what are they making up now in terms of percentage of FCC sales? And where do you think they can get to?

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

Rob, we said that we would finish this year having fully recovered our market position, and we're a little bit ahead of that pace. And we said that the new products would make up about 10% of catalyst sales by the end of the year, and we're a little bit ahead of that pace.

Robert Walker *- Jefferies & Company - Analyst*

Okay. And then maybe just to clarify on the pension change, what do you expect for pension expense going forward? Does this adjustment lower that?

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

Yes, just to clarify: this was no change to our pension. This was related primarily to healthcare benefits. And so you won't see this come through the pension line. You'll see it come through the corporate cost line. And I think the best way to model this is -- there's obviously some benefit in Q2. Some of that benefit will continue into the second half. But the way I'd model it is to take first-half corporate costs, basically keep them flat with second-half corporate costs.

Robert Walker *- Jefferies & Company - Analyst*

Okay. Can I ask one more? Just some clarification on your comment on around the pace of buybacks. Why slow at this level? The market is up 8% since your stock peak at $104. And you've won [steering win] back their lost volume. Are there better uses of cash out there, or why slow now?

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

This is driven off of a pretty disciplined allocation model that we have, where the rate of repurchase is tied to the value we think we create by doing those repurchases. And as the stock dropped in Q2, we saw an opportunity to accelerate. And I think as the stock is a little bit more normal level right now, certainly recovered much of what happened after Q2 earnings release, we're back to a more normal rate of share repurchase. Maybe another way to summarize it is, we think of Q2 as an acceleration, and what we're doing now -- back to a more normal pace.

Robert Walker *- Jefferies & Company - Analyst*

Okay, that's fair. Thank you.

Operator

Ben Kallo, Robert W. Baird.

Ben Kallo *- Robert W. Baird & Company - Analyst*

Hudson, just on the tempo of Q3 and Q4, it sounds like -- and Fred, too; maybe your thoughts here would be appreciated. It sounds like everything is -- Lake Charles is pretty standard. So you get that turnaround in Q3 and Q4, so not a lot of risk around that. Or you tell me if I'm wrong. And then the ART coming into Q4 returned to a better level to make that higher -- earnings higher in Q4. Can you talk about visibility there?

And then outside of those businesses, anything that you can see as risk to Q4 earnings with slippage or -- you talked about some big projects in the construction side. So if you could elaborate more on the back half of the year, and timing there.

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

Ben, let me start. I'll give you some color. We've got a 10-day turnaround. We do these turnarounds every couple of years, and so on. So we feel good about it on that side. We've got very good visibility on the ART recovery piece of it, both the internal operations side of it, the cost piece, as well as the orders. We do have an increase in our SBM piece of construction in the back half of the year based on those projects, on the project visibility we have. So if those projects -- if there's a dislocation of those projects, or so on, we'll see that.

I think we're going to get a very good look on the SBM side of it during this third quarter here, on some of these major projects from that standpoint.

But that's -- Hudson, anything?

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

No, I wouldn't add anything. I think you hit it, Fred. The Lake Charles turnaround is something we know how to do. The order lead time on ART is long, and we've got that good visibility. And as we said earlier, the momentum in construction feels like it should be good, but we do see more variability in SBM, and we've got to be mindful of that.

Ben Kallo - ***Robert W. Baird & Company - Analyst***

Great. That's all I have, guys. Thanks.

Operator

Jim Barrett, CL King and Associates.

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

Fred, in the construction business, can you discuss the -- remind us the relative gross margins between the two major product lines, chemicals and building materials?

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

Yes, building materials is higher. It almost approaches our catalyst business gross margins.

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

Okay. And you did mention it briefly, but is all of the 2.4% improvement year-over-year in pricing and mix at GCP -- is it all concentrated in construction chemicals?

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

The majority of it is, but we have also received some pricing on the SBM products.

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

I see. Okay. And then finally, you mentioned several times the timing of large projects. Given the international nature of that business, are we speaking of a dozen or less projects? Or is the number several dozen? Can you give us a broad range of just how many projects in any given quarter move the needle for that segment?

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

Yes, we actively track 75 to 100 projects at a point in time. And if you look at projects that could possibly slip, you're talking 10 to 20, in that range. These are generally big projects and big orders, and so on. And where they've got to be placed at the -- if it's going to Australia, where that shipment's got to be at that point, and so on.

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

Okay. That's helpful, and thank you very much.

Operator

(Operator Instructions). Brian Maguire, Goldman Sachs.

Brian Maguire - ***Goldman Sachs - Analyst***

One of your big competitors in catalysts announced a big acquisition earlier this month, taking them a little bit further from the catalyst space. Just wondering if, in your experience historically or prospectively, you think that that will have any impact on the competitive dynamics in the market, or customers' relationship with that competitor. Basically, is there an opportunity for you guys to maybe innovate better, or take some share, as they are a little bit distracted here?

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

Listen, they have a very good catalyst business, and they've got very good management around that, so I don't see that as being any distraction. And they will continue to move this industry forward with innovative new products that add value to our customers. And I don't see any difference there.

Brian Maguire - ***Goldman Sachs - Analyst***

Okay. And then I know you recently had a management change, or a new leader from your catalyst segment. Just wondering if you expect any changes internally or strategically, just the way you operate that business.

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

Yes, Al Beninati joined us. We are very excited to have Al. As you know, we had the President of Catalysts position open, open for a while. The individuals under that, all those vice presidents and general managers, are very solid on that side, and I don't expect any changes as we go forward.

We are fortunate to have Al, and the energy and discipline that he brings. And that will also free up Greg Poling. A lot of his time was being spent there, and I'm sure he'll be reviewing the pipelines in the SBM businesses even more.

Brian Maguire - ***Goldman Sachs - Analyst***

Great, thanks very much.

Operator

Chris Kapsch, Topeka Capital Markets.

Chris Kapsch - ***Topeka Capital Markets - Analyst***

I had a follow-up question on the year-over-year positive variance in the gross margin in the catalyst business. It was impressive at 160 basis points. What I'm wondering is, how much of that was from the inclusion of presumably high-margin licensing revenues from the UNIPOL acquisition? And what would have that variance looked like if you had excluded the benefit from those sales?

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

Chris, this is Hudson. You're right; the licensing sales do come through at very high margins. That's a part of it, but it's not everything. We're seeing very good performance in our catalyst businesses, not just from a commercial perspective, but from an operating perspective as well.

Chris Kapsch - ***Topeka Capital Markets - Analyst***

Okay. And then the traction that you're getting in the new product introductions, I'm just wondering -- this success you are having, is it more skewed towards the propylene maximization catalysts, or the heavy resid catalyst introductions, or is it across the board?

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

Yes, it's really across the board. Our ACHIEVE -- well, I'm not going to get through all the product names -- but for the shale oil, we've seen very good pickup on that side of it. On the heavy products, we've introduced a number of new products that are out there -- Midas Gold being one of them, and some of the others. And then as well in the propylene maximization, certain regions with our new products. So, it's really those three areas, and probably equally weighted.

Chris Kapsch - ***Topeka Capital Markets - Analyst***

When you have a trial ongoing -- and just how long does it typically take for a refiner to validate the performance where they perceive benefit, and then transition from trial quantities over to commercial? And then on these products that you've introduced, once they do convert to commercial, is the pricing at a premium to the legacy products? So should we see a mix benefit? Maybe are you starting to see that actually, on a sequential basis, going forward here?

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

Yes, let me answer the second part first. Generally, the prices that we've gotten on the new introduction products, the new products, have been somewhat higher than the older products. Now, the transition is really variable. It depends on the size of the unit. We've had transitions as short as one month, and as long as nine months. It really varies by -- based on the amount of the unit; the size of the unit; the amount of catalyst they may already have in inventory; how they want to feed it, the feed changes, and so on. So, it's all over the map on that side.

Chris Kapsch - ***Topeka Capital Markets - Analyst***

Okay. And then just one last one, and I have to bring back the topic of lanthanum. I know it's been a while now since lanthanum has normalized. But it probably takes a while for refiners to migrate back to higher lanthanum-containing products. And just wondering how -- has that fully progressed? And does that influence your price or mix whatsoever if, in fact, they are transitioning back to the higher lanthanum-containing products?

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

We see some customers wanting to add rare earth weight to their catalysts. But it's not a significant trend, and nothing really that impacts the way we're operating the business.

Chris Kapsch - ***Topeka Capital Markets - Analyst***

Okay. Thank you, guys.

Operator

Mike Ritzenthaler, Piper Jaffray.

Mike Ritzenthaler - ***Piper Jaffray - Analyst***

Just a couple of quick follow-ups for me. On the polyolefins catalyst business over all, I guess I was curious about two things: whether the $10 million in synergies from UNIPOL, in the course of its delivering $30 million of additional segment income this year, has been revisited at all. And whether 5% growth in the legacy olefins catalyst business in 2014 -- if it seems any more or less conservative at all, given the 2Q results.

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

The 5% growth in the specialty over 2013 -- remember, we had that big lap in that big, large tolling agreement in 2013 that we didn't have in 2014 on that side of it. Sequentially, our specialty catalyst volume -- this is the non-UNIPOL side -- is going to be up mid-teens on that side. So, when you take it from that perspective. So we feel good about that side of it.

THOMSON REUTERS

What was the first question? I lost my train of thought.

Mike Ritzenthaler - ***Piper Jaffray - Analyst***

(multiple speakers) it was on the synergies, and the potential accretion this year. Just if any of that stuff has been revisited in your model recently.

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

We look at it every day, to be perfectly -- not to be coy about it -- to be perfectly candid about it. But we feel good about the $10 million that we got the synergies on that side of it. And as we go through our plans over the second half, we'll be challenging our business again, as we always do, to continue to look at more opportunities.

Mike Ritzenthaler - ***Piper Jaffray - Analyst***

Sure. And one last little point of curiosity for me. On the competitor question that came up just a minute ago or two, they launched a new modeling platform and I'm wondering how that compares with, or competes with or whatever, on Grace's -- the pilot skid that's had decades of success.

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

Yes, I'm, candidly, not familiar with the new modeling platform. I know that, given our pilot plant and the unit we have here continues to be the industry gold standard from our customers coming to us, as well as engineering companies and others. So, I'm not exactly sure what that's referencing.

Mike Ritzenthaler - ***Piper Jaffray - Analyst***

Okay, fair enough.

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

It hasn't come up in any of our business reviews.

Mike Ritzenthaler - ***Piper Jaffray - Analyst***

Sure, sure. Thank you.

Operator

Chris Shaw, Monness, Crespi, Hardt.

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

I jumped off for a bit, so I apologize if I'm repeating anything. Can you guys talk about your own M&A pipeline or appetite right now, and what's out there with the multiples? Are they favorable? And do you think you can get something done anytime soon?

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

Our appetite for acquisitions remains strong. We haven't backed off the appetite at all. As we said last quarter and through other meetings that we've had, we believe the pricing for a number of these assets remains very high. And we want to be able to ensure that we can deliver on our risk-adjusted rate of returns on these. And at some of these high pricing, that's not as obvious to us on that side. But our appetite remains strong. We continue to look at a number of assets. We'll continue to be very aggressive in the smaller bolt-ons, and we'll see what comes up on the larger scale.

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

On the catalyst side, do you think it's any advantage that one of the other bidders is probably preoccupied for a year or so?

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

I don't know. I'd be just speculating on that. I really would.

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

And then -- again, I don't know if it was mentioned -- but for the third quarter, FCC volumes, I know you have a really easy comp on FCC volumes for third quarter, but you also have the outage. Net-net, do you think FCC volumes will be up, or can you not tell just yet?

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

We've said what we're going to say about Q3, Chris.

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

All right. Thanks, guys.

Operator

All right, great. And it looks like there are no further questions in queue.

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

Okay, thank you, Sarah. I'd like to thank everyone for joining the call this morning. And if there are any questions that require direct follow-up, please contact me on my direct line, which is 410-531-4590. And, again, we want to thank everyone for joining us this morning on the call. Bye.

Operator

This concludes today's conference. Thanks for your participation. You can disconnect, and have a great day.