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Univar, Inc. (UNVR)

Q1 2019 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, ladies and gentlemen, and welcome to the Univar Solutions' First Quarter 2019 Earnings Conference Call. My name is Julie and I will be your host operator on this call. At this time, all participants are in a listen-only mode. After the presentation, we will conduct a question-and-answer session. Instructions will be provided at that time. [Operator Instructions]

I will now turn the meeting over to your host for today's call, David Lim, Vice President of Corporate Development at Univar Solutions. David, please go ahead.

David Lim
Vice President-Corporate Development & Investor Relations, Univar, Inc.

Thank you and good morning. Welcome to Univar Solutions first quarter 2019 conference call and webcast. Joining our call today are David Jukes, President and Chief Executive Officer and Carl Lukach, Executive Vice President and Chief Financial Officer.

This morning, we released our financial results for the first quarter ended March 31, 2019 along with a supplemental slide presentation. The slide presentation should be viewed along with the earnings release, both of which have been posted on our website at univarsolutions.com.

During this call, as summarized on slide 2, we will refer to certain non-GAAP financial measures, for which you can find the reconciliation to the comparable GAAP financial measures in our earnings release and the supplemental slide presentation.

As referenced on slide 2, we will make statements about our estimates, projections, outlook, forecasts or expectations for the future. All such statements are forward-looking and while they reflect our current estimates, they involve risks and uncertainties and are not guarantees of future performance. Please see our SEC filings for a more complete listing of the risks and uncertainties inherent in our business and our expectations for the future.

With that, I'll now turn the call over to David for his opening remarks.

David C. Jukes

President, Chief Executive Officer & Director, Univar, Inc.

Thank you, David and good morning everyone.

It's been a very busy few months since we last spoke, but I'm pleased that our first quarter results were solid and reflects improving profitability in our USA business, pockets of strength in our international businesses and one month of contribution from the Nexeo acquisition. We also continue to work to navigate some headwinds and choppy demand in the marketplace and Carl will discuss our first quarter results in depth shortly.

Just 10 weeks ago, on February 28, we closed the acquisition of Nexeo Solutions, ahead of our initial timeline and on March 1, launches a new company, Univar Solutions. We executed a seamless day one transition with zero disruption to our customers and suppliers, launched a new brand for our company and began the process of shaping the Univar Solutions' culture as a values-based, purpose driven enterprise, focused on superior returns.

We also began immediately executing on our integration plan, which I'll discuss in detail later. Just six weeks ago, in keeping with our vision to be the most valued chemical and ingredient distributor on the planet, we completed the divestiture of Nexeo's plastics distribution business to allow us to concentrate our full energy on our core chemical and ingredient distribution business. We realized attractive growth proceeds from the sale of $650 million, which we used to pay down debt.

Over these past 10 weeks, our confidence in the strategic rationale and value creation opportunity has only grown as we've seen tangible evidence of our enhanced value proposition and have improved visibility into achieving the synergies that result from combining these two businesses. I'm excited by the opportunity we have to streamline, to innovate, and to grow. We have the opportunity to streamline business processes for our customers, suppliers and ourselves, removing redundancies, eliminating bottlenecks and structurally reducing our cost base. This creates a sustainable competitive advantage and a win-win for our customer and supplier partners that will serve as another driver of accelerating long-term growth.

We're only two months into the process, but our team, made up from people from both legacy organizations, is already working in a highly collaborative fashion to optimize our processes and increase asset utilization. When we complete our integration, we'll be an even more flexible and agile organization with a clear path to earning increasing returns on invested capital. We have the tools, resources and thought leadership to be an innovator in our industry, not only with the products we supply, such as our expanding range of natural ingredients, but with our enhanced digital tools. These are changing how we interact with our customer and supplier partners.

Utilizing the suite of digital products coming out of our continued investments in this area, it'll allow us to provide our customers and supplier partners with market intelligence and analytics to help predict trends and uncover insights into the supply chain, creating opportunities to streamline, innovate and grow.

At Univar Solutions, we have an even stronger product portfolio from some of the best brands in the world. With this new strength and scale, we're standing up two new markets is dedicated, focused industries, homecare and industrial cleaning and lubricants and metalworking that adds to our already wholly dedicated presence in personal care, food ingredients, pharmaceuticals and coatings.

We have formulation expertise in our 17 solution centers across the globe that help customers innovate while promoting our suppliers brands. And our sellers are energized and excited about the opportunity in front of them to grow their careers and their book of business, and crucially have the products, support and bandwidth they need to drive growth.

While we're excited about our growth potential, it's important to remind you about the degree of stability inherent in our business. While we'd love to have perpetual tailwinds across all businesses and across all geographies, this obviously does not reflect reality, but we do have many value creation opportunities that don't require a robust demand environment. And our model is able to generate strong free cash flow through the cycle.

Now let me turn the call over to Carl. He will walk you through our first quarter results in detail and then I will close with some comments on the progress of the integration.

Carl J. Lukach

Executive Vice President & Chief Financial Officer, Univar, Inc.

Thanks David and good morning everyone. I'm pleased to say that with the launch of our new company, it's a new dawn and a new day for Univar Solutions. We want to clearly communicate to you the metrics and milestones that you can track so that you can be as excited as we are about the growth and value capture that lies ahead. The key metrics are, gross profit, adjusted EBITDA, cash flow and return on capital. We will also report on our leverage and synergy capture from the Nexeo acquisition.

I'd like to start by saying that overall we are pleased with our performance in the quarter. As David said we successfully achieved a number of milestones related to the transaction and are excited about our progress to-date. When it comes to our financial performance there are a number of puts and takes this quarter and in last year's first quarter that make it difficult to understand our underlying business performance. I will take you through that. But first let me give you an overview.

It was a challenging quarter in all of our global markets with choppy demand from industrial end markets. However, we grew our gross profit dollars by 5% currency neutral, expanded our gross margin and improved our conversion ratio.

Our U.S. business improved and we continued with solid performance in EMEA. Growth in our USA and EMEA segments, however, was offset by a significant decline in EBITDA in Canada and challenging conditions in our LATAM segment. Our cash flow was strong in the quarter due to a much lower build of networking capital and our return on capital deployed was steady at 23%. Our leverage ratio was 3.9 times and we are just getting started on synergy value capture from the Nexeo acquisition. Against that business performance, we had a number of one-time costs in the quarter that I need to take you through. With that, let's get started.

In the first quarter, we reported a GAAP net loss of $0.43 per share. This loss included a charge of $0.44 per share for acquisition, integration and severance-related costs. It also included a one-time charge of $0.31 per share for the previously disclosed settlement of a long-time dispute we had with the U.S. government related to the import of saccharin between 2007 and 2012.

Adjusted earnings per share for the quarter, was $0.33 compared to $0.42 in the prior year. Our adjusted earnings per share in the quarter were negatively impacted $0.03 by FX and $0.03 by a higher tax rate. Prior year first quarter benefited $0.04 per share from a previously disclosed product cost adjustment in our USA segment. Adjusted EBITDA of $160 million in the quarter was unfavorably impacted by $5 million of FX and included one month of results from the legacy Nexeo Chemicals business. This compared to a $166 million in the prior-year first quarter, which included the one-time $8 million product cost adjustment benefit.

Gross profit dollars increased 5% currency neutral to $496 million and gross margin expanded 50 basis points to 23%. Growth was the result of improving execution in our sales force, more favorable product and end market mix, and one month of contribution from legacy Nexeo Chemicals. Adjusted EBITDA margin increased sequentially 10 basis points, or 7.4%, and net synergy contribution in the quarter was minimal.

Turning to our USA segment, adjusted EBITDA increased 6.5% as a result of contributions from the Nexeo acquisition, higher margins driven by favorable changes in product mix and improving sales force execution. Excluding the impact of the one-time product cost adjustment last year, adjusted EBITDA grew 17%. Organic volumes declined 4.6%, reflecting lower sales of bulk commodity products compared to last year's first quarter.

With some obvious outliers like the coatings market which remains somewhat sluggish, overall the demand environment in the USA segment, while choppy was healthy. Gross margin increased 30 basis points compared to last year and 100 basis points excluding the impact of the product cost adjustment which lowered our cost of sales in the year ago. Outbound freight and handling costs as a percentage of sales decreased sequentially 30 basis points as our execution is improving, but we're still 20 basis points higher than last year. We managed our operating costs well in the quarter, keeping them flat with the prior year. And our conversion ratio increased 100 basis points to 31.6%, normalized for the product cost credit last year.

Our commercial and supply chain teams are actively integrating the operations and product flows of legacy Nexeo and legacy Univar to capture synergies. Supplier, customer and product supply chains as well as financial data flows are being combined. As a result, we are looking at our USA business holistically as one Univar Solutions and are rapidly losing the legacy identity of the pre-merger former businesses. For example, customers who bought from both companies previously, no longer have deliveries coming from two separate warehouse locations in two separate trucks. Supply chain and facilities optimization is an exciting part of our overall value capture effort and is well underway.

Turning now to our Canada segment, adjusted EBITDA fell 26%, or 23% currency neutral, despite near double digit growth in our core Industrial Chemicals business. A significant drop in demand for chemicals from the Canadian energy market was the largest factor, reflecting a government directed cut in oil sands production in Alberta, as well as softness in certain bulk commodity chemical markets in Canada.

In addition, demand from the agriculture market during the first quarter was soft as growers continue to absorb excess stocks from the prior two-year drought conditions. We are not satisfied with the decline in our short-term results. With focused management action and prudent cost management, we expect to see an improvement over the coming months and we have already started to see this happen in April.

Our EMEA segment grew adjusted EBITDA 2% excluding the impact of currency in a challenging and weakening macroeconomic environment. This is the 22nd consecutive quarter of currency neutral EBITDA growth for our EMEA segment and is a testament to the restructuring actions and change in strategy that we took several years ago. Our more modern ERP system in EMEA, equivalent to what legacy Nexeo was using, allows us to be more nimble and agile in a fluctuating demand environment.

Gross profit dollars increased 2% excluding the impact of currency and gross margin expanded 100 basis points, driven by more favorable product and end market mix along with solid sales force execution. We had strong growth in our local chemical distribution business and certain focused industries, most notably the food ingredients.

During the quarter, we estimate that Brexit boosted our first quarter adjusted EBITDA by about $2 million from customers in the UK, ordering and holding higher than normal levels of inventory. We expect this timing benefit will reverse in the second quarter. We are being disciplined with our spending as we navigate through this period of high uncertainty, affecting industrial production across EMEA.

In our LATAM segment, strong performance in our Brazilian ag business and modest contributions from the Nexeo acquisition, were offset by lower demand from Brazilian industrial chemical markets. Higher prices for change in mix, improved sales force execution, and certain products shortages were largely offset by lower volumes, as a result of soft economic conditions and the product shortages. Our Brazilian customers seem to have adopted a wait and see approach to business as the country heads into a vote on governmental public finance reforms.

In Mexico, economic conditions deteriorated through the quarter, as uncertainty and sluggish industrial conditions dampened demand. With that said, however, we expect the first quarter to be the low quarter of the year as a result of cost actions we've taken and new wins in our Brazil ag business.

Moving now to cash flow, change in net working capital with a cash outflow in the quarter of $92 million, which due to our lower sales compared to last year was about $140 million less than last year. This provided operating cash that helped fund our transaction closing costs and the legal settlement that we called out in our earnings news release. Cash interest expense in the quarter was $40 million. We now expect cash interest for the year to be around $140 million, down from our prior guidance of $150 million.

Cash taxes in the quarter were $10 million. We're reducing our full year forecast of cash taxes from $70 million to now $50 million. While our cash tax forecast is reduced due to the onetime costs related to the Nexeo acquisition, our effective tax rate for adjusted EPS in the quarter of 31.8%, was higher than the prior year first quarter of 25% and was a $0.03 per share headwind to adjusted earnings per share. The higher rate was due to the timing of the one-time costs in the first quarter. We expect the rate will taper down during the rest of the year and settle out at about 30% for the year, as we said last quarter.

Underlying capital expenditures to maintain our facilities and grow our business were $17 million in the quarter, unchanged from the prior year. We are reducing our full-year forecast of CapEx from previously $115 million to now $100 million and this excludes the one-time spending that will likely occur when we combine and optimize the legacy Univar and legacy Nexeo facilities footprints in the U.S.

During the quarter, we paid an expense transaction fees of $50 million related to the acquisition of Nexeo and $38 million of integration and severance costs. We also paid $18 million of debt refinancing fees, which were capitalized and will be amortized over the term of the financing.

We continue to earn an attractive return on our capital, which underscores the quality of our business. Our return on assets deployed of 23.6% was roughly unchanged from the first quarter last year. Our ROIC, defined as adjusted net income divided by net assets deployed, was just under 10%, down from 10.6% at this time last year, reflecting the addition of Nexeo Chemicals assets deployed to our balance sheet. We expect our ROIC will increase as we successfully execute our integration and synergy capture plans

At quarter end our leverage ratio was 3.9 times. And our near-term priority, use of cash is to continue de-levering to below three times. During the quarter we refinanced our $1.4 billion ABL facility due in 2020 with a new $1.7 billion facility due in 2024 to increase our liquidity and extend the maturity of the debt. In February, we raised $1.3 billion of new debt at favorable terms to complete the acquisition. And one month later, paid down $650 million of debt using the gross proceeds from the plastic sale. We continue to expect our leverage ratio to be approximately 3.5 times by December this year.

Turning now to guidance. For the full year 2019, we continue to expect to earn $740 million to $760 million in adjusted EBITDA compared to $640 million earned in the prior year. This guidance includes 10 months of earnings from the Nexeo Chemical business and approximately $10 million in estimated net realized synergies. We still expect to generate $300 million to $350 million in free cash flow, inclusive of the $63 million saccharin settlement and before one-time integration and transaction fees. The negative impact of the settlement is expected to be partly offset by lower cash taxes, lower cash interest and lower capital expenditures.

For the second quarter of 2019, we expect adjusted EBITDA to be between $195 million and $200 million up from $173 million earned in the second quarter of 2018, as we expect dyssynergies to be realized a bit faster than the cost saves.

With that David, I'll turn it back to you.

David C. Jukes

President, Chief Executive Officer & Director, Univar, Inc.

Thanks. Carl. Since closing the Nexeo acquisition, we've moved immediately from planning to execution. As said before, we're keenly aware of the magnitude of effort this integration will take and have an excellent team, and a detailed, thorough and comprehensive plan, they're working swiftly but methodically, to execute on. We've move to capture synergies quickly whilst also providing internal reassurance to employees and continued service to our suppliers and customers. Diligent planning and executing a pace are the keys to success and we are operating at pace.

After successful and seamless day one, our priority has been to ensure stability and have the right leaders with a clear accountability in place to drive results. We announced the key leadership team immediately after close and I've formalized the organizational structure, down to the director and general manager level. We will have the whole organization structure finalized by the end of this month.

Our commercial teams have been successful in working with customers to allay any concerns they may have and minimizing any customer and supply disruption. Meanwhile, our fellas are highly motivated and excited by the opportunity in front of them to grow their career and their book business with a fast moving industry leader with a vision of redefining chemical distribution standards.

As we stated before, the acquisition resulted in some supplier and customer dyssynergies, which are included in on net synergy guidance of a $100 million. To unpack that for you and to give you some milestones we can track together over coming quarters, that number was made up of approximately $130 million in cost savings and $30 million of customer and supplier dyssynergies. This is anticipated in our planning. As expected, we're seeing those dyssynergies up-front as we manage our way through the portfolio of product choices we have and are successfully working to mitigate and offset those impacts.

We're pleased to say, we've not seen any surprises to-date and I'm delighted that we've had the opportunity to expand our relationship with some of our existing partners and industry leaders, such as Dow, ExxonMobil, Olin and Shell. As yet, we've not included or enumerated the commercial upsides from such things as cross-selling and improved sales efficiency in any of the guidance we've provided. Having said that, seller attrition remains at the low levels we observed post-deal announcements and territory redesign for our sales force is underway. We've given this a very high priority and expect to complete it in the coming weeks, liberating and expanding sales force to drive for profitable growth. We'll then be able to develop detailed commercial growth plans with our supplier partners and are confident we have many opportunities to drive value and growth for them and our customers.

As we've mentioned in the past, we're moving the legacy Univar business on to the legacy Nexeo IT platform to leverage the benefits of a modem ERP system. This will create additional process efficiencies and provide the backbone we need to fully realize our digital strategy. We've completed a fit/gap analysis and are on track to complete mapping legacy Univar's master data on the legacy Nexeo platform. We have a comprehensive plan that's been fully pressure tested by external experts and expect to start moving sites on to the platform later this year. We'll manage the IT migration program in five ways, starting in the fourth quarter and extending through 2020.

Our network optimization plans are also on track. We'll be moving business from sites that will be closed to other sites in close geographic proximity. We have detailed plans in place to manage the transition to provide our customers with a high level of service they expect from us. As we stated before, much of our site consolidation program will follow the IT migration program. However, there will be some facilities that we'll be able to close later this year.

Finally, we are realizing indirect procurement synergies, leveraging our combined spend. Pre-close, we work inside a cleanroom to develop combined spend data. Since close, we've been able to go to market very quickly on our combined transportation spends and are expecting to realize savings, regaining lost ground from the 2018 transportation market tightness.

We remain confident in our ability to capture $100 million in net synergies, including $130 million in hard cost savings and have a disciplined process with clear milestones, detailed scorecard and action plans by function to track against all our synergy targets.

While we're focused on integrating Nexeo, we're also advancing key initiatives to grow our business. We're taking an omni-channel approach to grow select product lines in markets and shaping customer coverage appropriately, and we're leveraging our digital capabilities to reach and service a wide range of account sizes. Meanwhile, we continue to expand our product portfolio and have signed significant new distribution agreements with Novozymes and CEAMSA amongst others with many more in the pipeline.

As we zoom in on integration and growing our core chemical and ingredient distribution business and as we mentioned in our last call, we will actively evaluate our portfolio of businesses in order to ensure we maintain our focus and to make sure with the right owner to allow our businesses to fulfill their potential.

As a result, I'm pleased to announce that David Lim will be transitioning from his dual IR and M&A role to focus solely on portfolio managements. I'd like to thank David for his many contributions and I look forward to working with him in this new role. I'm delighted to announce his replacement is Heather Kos. As some of you may already know, as an experienced Investor Relations Officer and a recent recipient of the Chicago Crain's Notable Women in Manufacturing Award. I hope you'll all have an opportunity to get to know her in the coming days and I'm excited that we continue to attract such high quality talent to Univar Solutions.

While we have much work ahead of us, it's an exciting time to be at Univar Solutions. Our teams are genuinely excited, highly motivated and driving hard to capture the tremendous opportunity we have in front of us. Our supplier partners too are excited and right behind us. They recognize the power of the platform we are developing to grow their business, combining the best product portfolio in the industry with the largest, targeted, industry-focused, technically skilled and supportive sales force in North America.

As I said at the opening to my comments, this has been a busy period for all of us at Univar Solutions. We bought a company, sold another and created a new one in the process. We launched a new brand, a new culture and managed this down through face to face meetings with over 1,200 sales and commercial leaders globally. We've restructured the leadership team down to four levels below me, a team with clear goals and accountability. We began executing on our integration plan and realized our first synergies. We paid down debt and refinanced our borrowing. We signed new supplier authorizations while expanding others. And we delivered earnings in line with expectations despite choppy demand and adverse effects. This is a proven team of experienced professionals with a clear plan and the ability to execute.

Now, as Univar Solutions, we will continue to streamline, innovate and grow, redefining chemical distribution to achieve our vision of being the most valued chemical and ingredient distributor on the planet.

Thank you for your attention. And with that, we'll open it up to questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] David Begleiter from Deutsche Bank. Please go ahead. Your line is open.

David Huang
Analyst, Deutsche Bank Securities, Inc.

Q

Hi. This is David Huang here for David. I guess, first, can you discuss in more detail of the improvement in sales force execution you have seen so far? And can you also roughly quantify the benefits of that in Q1?

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.

A

Sure, we can – we can do that. Thanks for the question. Our sales force, as you know, we turned over quite a bit of that in the legacy Univar organization in 2017 and our sales force is maturing and developing well. The attrition from both companies – accelerated attrition from both companies – is reduced since the deal announcement and the legacy Nexeo sellers are really bringing a fresh perspective into the organization.

Collaboration levels between the two teams are extremely high and the teams are now highly motivated. Energy levels are very high following a sales meeting – a joint sales meeting that we had with them about three, four weeks ago. And so the teams have a very clear vision of what they need to do. We continue to invest in training and developing our people. Growing our people to grow our business is a core value of Univar Solutions, so we can see to – see that paying off. And now, really the priority is to finalize the sales territory realignment, so we can liberate an expanded sales organization on to the marketplace to drive more growth.

Carl J. Lukach
Executive Vice President & Chief Financial Officer, Univar, Inc.

A

As far as quantifying the impact of that in the first quarter, it's hard to put in – the exact precise number on that – but it certainly contributed to the margin increase that we saw and the gross profit dollar growth.

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.

A

Yeah. If you look at how we target the sellers, the sellers as you know are very clearly targeted to sell and drive the products that we're focused on, particularly in our focused industries. We saw good growth in our food ingredient business, in our personal care business there. I point to the improvements in our gross profit and the improvements in our gross profit margin as examples of really good execution from an improving sales organization.

David Huang
Analyst, Deutsche Bank Securities, Inc.

Q

Thank you. And then, second, on your comment, portfolio options, where are the some keys areas of focus businesses for you when you think about portfolio optimization or strategic transfers?

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.

A

Well, look, we have a wide portfolio of really good businesses. Within Univar Solutions, we're very focused on being the most valued chemical and ingredients distributor on the planet. And so, just like we did with the Nexeo Plastics business, which is a good business, we'll take a look at these businesses, all our businesses and see whether we are the best home to allow them to fulfill their potential.

So very, very, very, very early in the process. But I think that we owe it to the businesses, we owe it to all our businesses to make sure that we can provide the right support, capital and direction to allow them to fulfill their potential. But we've got a portfolio of really good businesses. There's nothing on – there's no fire sales going here – we're very happy with the portfolio we have. It is a question of how may we resource them appropriately to allow them to fulfill their potential and are we the best home to do that.

David Huang
Analyst, Deutsche Bank Securities, Inc.

Q

Okay. Thanks.

Operator: Robert Koort from Goldman Sachs. Please go ahead. Your line is open.

Ragnhild Stoeer
Analyst, Goldman Sachs & Co. LLC

Q

Thank you. This is Ragnhild Stoeer on for Bob. As you reiterated your full year EBITDA guidance, I was wondering if you could maybe comment on the upside risk there and if there are any specific events or trends that could potentially lead to you raising this?

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.

A

It's nice to ask for a raise. Look, I think, we're very focused on delivering our commitments. One of our values at Univar Solutions is we do what we say. So, we're very committed to focusing on our commitments. One of those commitments is to deliver $130 million in hardcore synergies and we're very focused on that. We're very focused on the ERP integration and transition process that will go through 2019 and 2020, which will drive growth. We're very focused on the realignment of sales territories which we need to do to liberate the sales organization to drive growth. We haven't enumerated the cross-selling opportunities that we might have from the new organization, or the efficiency gains that will happen in the organization. So, we're very focused on delivering on what we said we're going to do. That's where our focus is and that's what we're going to do.

Ragnhild Stoeer
Analyst, Goldman Sachs & Co. LLC

Q

Thank you. And then in Europe, your EBITDA declined and you noted some softening macro environment. I also noticed that one of your peers missed on Europe this morning. So, could you maybe comment on the dynamics you see here and what you see going forward?

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.

A

Yes. I mean, I think, in Europe our EBITDA on a currency neutral basis was up a little bit. The macroeconomic trends in Europe are very confusing. But we have a very robust business in Europe. It's a very well-oiled machine. It knows what playbook to play depending on how the market is operating. It's very geographically diverse and it pivoted some years ago to more consumer demand-focused products like pharmaceuticals, like food ingredients, like personal care, and has done exceptionally well in those. But we have a very well-oiled machine there which can run equally well in second gear as it can in fifth, and it knows what playbook to play. So, whatever the market conditions there, I have great confidence in that team's ability to navigate their way through them.

Carl J. Lukach
Executive Vice President & Chief Financial Officer, Univar, Inc.
A

I'd just add to that, David, the additional factor too in our performance, we had very good cost control by the management team there in Europe, going through these choppy uncertain demand signals from the economy. So, the combination of all that led to a good currency neutral result in a very challenging market.

Ragnhild Stoeer
Analyst, Goldman Sachs & Co. LLC
Q

Thank you.

Operator: Laurent Favre from Exane. Please go ahead. Your line is open.

Laurent Favre
Analyst, Exane BNP Paribas
Q

Yes, good morning, all. The first question is around the $10 million of net synergies that you mentioned. I think, Carl, you're hinting that number starts being negative I guess in the first quarter – in the second quarter, and then we see the net positive towards the end of the year. Can you give us a bit more details around the negative or the dyssynergies? I mean are you expecting to see the full minus 30% in the first 12 months of integration? And as for the cost cuts being very close to $40 million run rate towards the end of the year, so $40 million minus $30 million being the $10 million net, that's the first question.

Carl J. Lukach
Executive Vice President & Chief Financial Officer, Univar, Inc.
A

Sure. Laurent, thanks for that. Yeah. Think of it as two gears moving at the same time. The first one is the gross cost synergies and as David said, we're very much on track there and confident in being able to capture those savings. The dis-synergies around supplier – supplier dis-synergies primarily are, as we expected happening sooner. And so you've got those two interacting quarter-by-quarter, it's hard to be precise quarter-by-quarter, but yes we expect in the second quarter the dis-synergies will outweigh the cost savings in the second quarter. But as then you progress to the third quarter and then the fourth quarter, those two would turn net positive and give us a net positive result of $10 million for the year.

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.
A

Yeah. If I just add to that – just add some color to that, if I may. We're very confident of the $130 million in hardcore cost savings and that's why we wanted to pull that out so you track that very clearly. But the dyssynergies are frontend loaded, we always said they'd be frontend loaded, but there is nothing in there that surprises us. There's nothing happening that we didn't expect to happen or make happen. So, it's just a case of the transition between supplier X and supplier Y, or the transition between customer X and customer Y that's doing that. So there's nothing in there that's a surprise to us, there is nothing that's unplanned, it's just merely a case of managing the moving parts. But our synergy execution is working well, our team are working well. And yes, as Carl said, in Q2, it'll be a headwind but that will be reversed as the year goes on. But there is nothing happening that we didn't anticipate.

Laurent Favre
Analyst, Exane BNP Paribas

Q

Thank you. And the second question is around David Lim's new job and new focus. I mean, given the assets to migrate the legacy business towards the new IT platform, doesn't make sense to migrate all the businesses towards the new IT platform and then think about portfolio, or should we assume that you don't need to wait for the full integration to be done to sell some non-core businesses?

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.

A

Well, look, we'll make those decisions as we go along. Our primary focus is to move the legacy Univar business onto the legacy Nexeo platform and our focus is on the core chemical ingredient distribution business. And as we said, we'll do that in a series of waves and starting in Q4 of this year. There are businesses which we have – which are on that platform already – there are businesses outside that platform. We have a wide portfolio of businesses. We also have experience like we have with the plastics business of carving out a business pretty quickly and pretty readily to be able to stand it up as a standalone entity. So, David, will be looking at all factors as we review our portfolio for any possible divestitures or further acquisitions as we continue to develop out.

Laurent Favre
Analyst, Exane BNP Paribas

Q

Thank you.

Carl J. Lukach
Executive Vice President & Chief Financial Officer, Univar, Inc.

A

Thanks, Laurent.

Operator: Steve Byrne from Bank of America. Please go ahead. Your line is open.

Luke Washer
Analyst, Bank of America Merrill Lynch

Q

Hi. This is Luke Washer on for Steve. I wanted to touch on the – again, kind of elaborating a little bit more on looking at evaluating your portfolio, I just wanted some expansion on this. Does this seem more and I know you're in the early stages, but it is more of a kind of a U.S.-centric initiative following the Nexeo merger and are you looking at certain key metrics when evaluating these businesses?

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.

A

Well, I mean, I appreciate your interest to try and drill in further down on to this. Heather joined us on Monday, David is still here shuffling bits of paper and hasn't even started on his thoughts yet. We have a wide portfolio of businesses and some of those businesses – none of those businesses are bad. We don't have bad businesses. We had bad years, but we don't have bad businesses. And so, we have some good businesses and we're going to evaluate whether when we think about our capital allocation, the right thing to do is to invest in those businesses and their growth or whether they'll be better supported and sustained by someone else.

The plastics business is a clear example of a really good business that actually was probably better in someone else's hands than in our hands and we sold that, we got good proceeds from that and we're able to pay debt down. So David will at some time in the very near future, stop shuffling these papers, start shuffling a fresh set of papers, think about what the options are for our businesses. But none of them are distressed, none of them are bad and there's no fire sale going on here. So if you see nothing happen for the next six, nine months, don't necessarily be alarmed about that. We're making really good value judgments about whether we are the right home and the right sponsor to allow the growth of the multiple franchises that we have.

Carl J. Lukach
Executive Vice President & Chief Financial Officer, Univar, Inc.

A

If I could add on to that just in terms of metrics. I mean, certainly what – the overall goal would be to maximize economic income for the portfolio and return on capital. So that will always be in our mindset as we make these evaluations. Each one of these businesses has an investment per growth profile and as all good portfolio management would do, we will look at maximizing turns on these investment options.

Luke Washer
Analyst, Bank of America Merrill Lynch

Q

Makes sense. Thank you. And just touching on the macro, it seemed, entering this year that you were one of the few companies not calling for a second half rebound. Now four months into the year, how have your thoughts changed on the macro side and the outlook for the second half year?

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.

A

I don't think they have. I think, there's as much uncertainty around as there was at the turn of the year. So, as the Chinese trade war going to end this week, I mean I don't know. When's Brexit is going to happen, I don't know. When France is going to stop being in flames, I don't know. There's so much uncertainty around. I don't see any reason to hope for a second half rebound. We certainly don't plan for a second half rebound. Hope is not a strategy. No, our strategy is to manage through what we see at the moment, what we see in front of us at the moment is pretty choppy demand and we have growth projection and plans which are fit for that market. If the market changes, we'll adjust our strategy appropriately.

Luke Washer
Analyst, Bank of America Merrill Lynch

Q

Make sense. Thank you.

Operator: Jim Sheehan from SunTrust. Please go ahead. Your line is open.

Peter Osterland
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Good morning. This is Pete Osterland on for Jim. What is driving the favorable mix shift in the U.S. this quarter? Is that related to the addition of Nexeo or was there something else specific in the quarter? And do you believe that this is sustainable heading into the second quarter?

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.

A

Well, it isn't. It isn't to do with Nexeo, although we believe the Nexeo will be highly accretive for us as we go forward. Nexeo had a split between a commodity business and a good specialty portfolio, good differentiated portfolio and that portfolio added to the legacy Univar portfolio, is allowing us to build up strength in key markets like food ingredients and personal care and farm ingredients. I mean, the two markets which have really been impacted for us, I think, everybody for coatings. I mean, the coatings market where we sell a lot of bulk solvents has been negatively impacted and we're seeing projects being delayed, projects being put back. I don't believe we've lost business or lost share there, but we are seeing some projects delayed and put back. And then, the energy business, the upstream business where we don't play as much anymore. And certainly, we're looking for profitable growth and some of those markets don't offer the profitable growth that we would want.

So, I think, there will always be a balance between the differentiated and non-differentiated products that we have. Clearly, we're very focused on putting more business towards consumer markets like food ingredients, farm ingredients, personal care, which tend to be more robust through the economic cycle. And I'd point to our EMEA business as an example of what that looks like through the cycle.

Peter Osterland
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Thank you. And then on the agriculture end markets in the U.S. and Canada, could you see a tailwind on a year-over-year basis in the second quarter if some of those weather impacted volumes from the first quarter are delayed?

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.

A

Well, we don't have a business in the U.S.; it is in Canada. And yes, it will be a tailwind if we get the right weather and yes, it will be a headwind if we don't. So, not being a weather forecaster, I'm not actually prepared to commit anything at the moment, other than we have a view and we've taken a, kind of modest view, with supply chain is still well-stacked. And what we are doing is improving the quality of our business in there, to more robust kind of products which are less weather dependent. And the deal we announced with Novozymes will be a substantive deal that will deliver in 2020 in a much more robust area of the ag market.

Peter Osterland
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Thank you

Operator: Laurence Alexander from Jefferies. Please go ahead, your line is open.

Daniel Rizzo
Analyst, Jefferies LLC

Q

Good morning. It's Dan Rizzo on for Laurence. How are you?

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.

A

Good, thank you. How are you?

Daniel Rizzo
Analyst, Jefferies LLC

Q

Good. I know David is just getting started, but have you gotten inquiries from potential suitors in the past, prior to Nexeo, for assets that they think is attractive. Is it something it's been ongoing for a couple of years?

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.
A

Look, I think, people regularly offer us things for sale or offer to buy things from us. So, there's no particular acceleration. There's no change in the external environment which is causing us to think about how we manage our portfolio. Managing a portfolio is something that any healthy enterprise does, and particularly as you want to zoom in and focus on winning. We know very clearly where we want to win and where we want to grow. And so, it's a question of focus for us now and then a question of cash allocation, whether we can support the growth demands and the growth aspirations of a wide portfolio of businesses that we hold.

Daniel Rizzo
Analyst, Jefferies LLC
Q

Okay. And then in terms of your Canadian ag business, is there a particular type of product that you guys focus on, like pre-emergent herbicides or insecticides, or is there – or are you kind of spread out?

Carl J. Lukach
Executive Vice President & Chief Financial Officer, Univar, Inc.
A

Yeah. Dan, we're spread out. We've got a full portfolio of products there from herbicides to insecticides and fungicides, and even a little fertilizer in there too, and even a little seed. So it's pretty widespread.

Daniel Rizzo
Analyst, Jefferies LLC
Q

Okay. Thank you very much.

Carl J. Lukach
Executive Vice President & Chief Financial Officer, Univar, Inc.
A

Sure.

Operator: [Operator Instructions] Duffy Fischer from Barclays. Please go ahead, your line is open.

Duffy Fischer
Analyst, Barclays Capital, Inc.
Q

Yeah. Good morning. First question is, just trying to understand how much of the upper tier of management from Nexeo is going to be feathered into the new Univar. So, maybe David, if you could kind of talk about your top tier 1 and 2, if that's 30 people in the new Univar. What would be the split? How many are historic Univar versus how many are Nexeo?

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.
A

Well, no one is being feathered in. We've made very deliberate choices about the people that we want to lead this company, people who reflect the values that we have for our new company, our new Univar Solutions. So, if we think about the operating committee – the top leaders who manage this business – Brian Herington is Chief Commercial Officer, Pat Jerding is Chief Information Officer. That's who legacy Nexeo employees who are to be very impactful to our business. Many of the C-suites from legacy Nexeo, of course, went on to do other things. So that wasn't as much to choose from there.

If I go down to the next layer of the U.S. management team, we have what, two, three. We have Joey Gullion now running our focused industries which is the large growth part of our business. We have Dan Matheny running our solvents business. So, we have Tracy Diel with our marketing business. So, we have a number of legacy Nexeo employees. But, I mean all of us, used to work somewhere and now all of us have worked for Univar Solutions for about 10 weeks. And that's really what we are focusing on; that's who we are.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Okay. And then, just the second one, around the accretion from Nexeo, so Carl, in the $160.1 million adjusted EBITDA for the first quarter, how much of that would have come from the Nexeo accretion? And then, how should we think about the run rate EBITDA generation of Nexeo kind of right at the deal close. I mean, what was the run rate for this year going to be if it was standalone?

Carl J. Lukach
Executive Vice President & Chief Financial Officer, Univar, Inc.

A

Duffy, okay, let me try to rough that out for you, but I have to say upfront that the eggs are scrambled. We are very, very actively integrating these two companies' former supply chains because there are immediate cost synergies available to us and so we're not wasting time to grab those. But, to try to help out with that in this first quarter, you know that we expected legacy Univar to earn $140 million to $145 million and for legacy Nexeo to be roughly flat with last year. And the way it came out in the $160 million is that the legacy Nexeo came in about, as expected, to the best we could identify that and Legacy Univar came in a little bit better than expected, with that really coming in the U.S.

If you look at – compared to last year, $166 million that legacy Univar did, you would adjust for the one-time product adjustment credit that we had of $8 million, the FX headwinds that we faced, a $5 million and then take into account the lower Canadian earnings of $5 million, currency neutral and that should take it to about $148 million roughly for legacy Univar in the quarter. And so as I said, it came out as we expected when we went into it, but Duffy, I have to say this is the last quarter that we'll be able to rough that out for you, we really are losing visibility on the historical performance of those companies as we merge the supply chains.

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.

A

I mean, Duffy, just let me add on to that, I mean just two things. And I think, we said in the script we started moving on integration immediately. And as I said earlier on, we're now one company, its Univar Solutions. Now to reinforce, the eggs are unscrambled, can't put in the shell for you, and we're not even trying, because it's pointless. We're focused on the commitments that we've made for synergy capture, for gross profit growth or EBITDA growth, free cash flow, they are these things that we're focused on delivering this Univar Solutions.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Great. Thank you guys.

David C. Jukes
President, Chief Executive Officer & Director, Univar, Inc.

A

Thanks, Duffy.

Operator: Thank you. We have now reached the end of our Q&A session. I will now turn the call back over to Univar Solutions team for closing comments.

David Lim

Vice President-Corporate Development & Investor Relations, Univar, Inc.

Thank you, ladies and gentlemen, for your interest in Univar Solutions. This does conclude today's call. If you have any questions, please feel free to reach out to the Investor Relations team. Thank you.

Operator: You may now disconnect.