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Univar, Inc. (UNVR)

Q4 2018 Earnings Call

CORPORATE PARTICIPANTS

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

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

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

OTHER PARTICIPANTS

Robert Koort
Analyst, Goldman Sachs & Co. LLC

David I. Begleiter
Analyst, Deutsche Bank Securities, Inc.

Kevin W. McCarthy
Analyst, Vertical Research Partners LLC

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.

Steve Byrne
Analyst, Bank of America Merrill Lynch

Duffy Fischer
Analyst, Barclays Capital, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good morning, ladies and gentlemen, and welcome to the Univar's Special Investor Call to review its Fourth Quarter and Full Year 2018 Earnings and also highlight the closing of the Nexeo acquisition and expected 2019 results. My name is Emily, 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 and Investor Relations at Univar. David, please go ahead.

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

Thank you and good morning. Welcome to Univar Solutions investor 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.

On February 8, we released our financial results for the fourth quarter and fiscal year ended December 31, 2018 as well as our first quarter and full year 2019 guidance excluding the acquisition of Nexeo. On February 21, we filed our 10-K for the fiscal year ending December 31, 2018 and last Thursday, February 28, we closed on the acquisition of Nexeo Solutions. Today, we released a supplemental slide presentation that should be viewed along with a news release covering our comments on this call. Both have been posted on our website at univarsolutions.com.

During this call, 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 and 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 and welcome to our first conference call as Univar Solutions. As many of you have seen, we closed our acquisition of Nexeo Solutions on February 28 and will be doing business as Univar Solutions going forward, reflecting a new company that combines the best of the best of Univar and Nexeo Solutions.

I'll have more to say on that later, but first let me briefly summarize Univar's fourth quarter and full year 2018 results and the standalone Univar guidance that we provided to you three weeks ago. We made the decision to give you standalone guidance to be transparent with our projections, provide investors with a detailed update on how we have seen the year progressing. As you saw in that report, 2018 was a year of progress and challenges as we move towards our goal to be the most valued chemical and ingredients distributor in the world.

In 2018, we grew sales 4.6% to $8.6 billion and expanded our gross profit and adjusted EBITDA margins. Adjusted earnings per share grew 16.5% and adjusted EBITDA increased by 7.8% to $640 million. Our asset light resilient business model allowed us to report another year of solid profitability growth, free cash flow generation and cash return on capital.

Whilst our 2018 financial results were solid, they were modest compared to our goals. This is due in part to a number of challenges we faced throughout the year which our teams worked hard to successfully manage. Capacity constraints in the transportation markets led to higher costs and lower availability whilst an uncertain economic environment, especially from September through December, led to cautious customers and oscillating demand during the latter part of the year.

Through these challenges, our supply chain teams performed well as they focused on keeping our customers in stock by delivering products safely and on time. In Canada, adverse weather conditions in our agriculture business and softness in the Western Canadian energy markets led to an 8% decline in segment EBITDA for the year.

Our outlook for 2019 includes an expectation that uncertainty and sluggish demand for most of our end markets will persist as customers remain wary of building their finish product inventory. In the fourth quarter, demand fluctuated in the U.S. sometimes on a weekly basis as a soft October was followed by relatively solid November, only to see December soften again. In Europe, we saw business conditions weaken progressively as uncertainty in the economy led to cautious behavior from customers.

We've seen this uncertainty in many markets continue into January and February, and as the results are being restrained and prudent with our discretionary spending and measured in our outlook. However, against this tepid economic backdrop, we remain excited and focused on executing against our strategy and successfully integrating Nexeo. We have made significant progress on numerous fronts and have clear plans in place to address areas that are taking longer to advance.

One of the places where we have been most successful is the optimization of our supply chain where we've made significant improvements since embarking on our transformation plan. Under Jenn McIntyre's leadership, we have implemented lean programs and indirect procurement, optimized our logistics network, and reduced warehouse costs. We closed a number of Univar sites utilizing a well-developed playbook created over the past two years to execute on our site consolidation plan. Since 2016, these improvements have continued to contribute to a 200-basis point increase in our USA segment conversion ratio defined as adjusted EBITDA divided by gross profit.

As we look forward, we see even greater opportunity to drive efficiencies as Univar Solutions. Over the past few years you've heard us talk about digitizing our business, moving from manual processes to technology enabled company that can provide unparalleled service while lowering transaction costs. We have made meaningful progress, and with the acquisition of Nexeo we expect a significant jump forward.

The Nexeo platform allows us to accelerate our digital transformation by providing an ERP system optimized for chemical distribution that we know and understand well that it's almost identical to the Univar system in Europe. The familiarity and efficiency of the systems design allows us to migrate the legacy Univar business onto Nexeo's platform in a seamless and efficient manner, significantly reducing a key risk inherent in any ERP upgrade.

The global chemical supply chain is digitally immature. Integrating Univar's industry leading e-commerce capability onto Nexeo's advanced ERP systems opens the door for us to create sustainable competitive advantage by making it easier for customers and supplier partners to do business with us and lower our transaction costs. It will allow us to redefine the supply chain with our partners forming an optimized ecosystem that will accelerate growth opportunities.

The U.S. sales transformation which we embarked upon in 2017 is advancing, though it's taking longer than expected. As we track our internal performance metrics by line of business and individual seller, there is no denying we had hoped for a faster pace of improvement. Similarly to us, Nexeo started a sales force transformation program in mid-2015, 18 months before we began our own. The Nexeo team is, in many respects, further along in their journey and we intend to take the learnings from their experience to accelerate growth.

Moving forward, our combined product portfolio is stronger, which gives us greater strength in our focused industries, the food ingredients, personal care, pharmaceutical ingredients and CASE. In addition, we now have the scale to stand up two new focused industries in the U.S. homecare and industrial cleaning and lubricants and metalworking. In conjunction with our greater reach, we will relentlessly drive our sales force execution. Exceeding on each of these fronts accelerates our opportunity for growth and profitability.

Now, let me turn the call over the Carl who will walk you through our 2018 results and 2019 guidance in detail. And then I will close with some comments about the Nexeo transaction and where the combined company is headed.

Carl J. Lukach

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

Thanks, David, and good morning, everyone. While we reported three weeks ago our fourth quarter and full year results, let me start by briefly giving you a refresher on those results as a baseline for understanding our revised 2019 guidance that now includes Nexeo chemicals.

In the fourth quarter last year, we reported net income of $1.2 million and GAAP earnings per share of $0.01. This included a non-cash pension mark-to-market loss of $0.24 per share and acquisition related expenses of $0.10 a share. Adjusted earnings per share of $0.33 and adjusted EBITDA of $144 million were essentially flat with the prior year fourth quarter.

Pricing trend lines and profitability per transaction continued upwards in the fourth quarter, but were offset by a significant decrease in earnings from Canada and lowered demand from global industrial markets. For the full year, consolidated gross margin expanded by 10 basis points improving gross profit by $95 million compared to last year. This, combined with disciplined cost management, led to an adjusted EBITDA increase of 8%.

In the U.S., 2018 was a year of measured progress. Our adjusted EBITDA grew by 7.5% and the segment increased its volumes for the first time since 2014. Our focus on sales force effectiveness continued as more than 300 sales team members completed advanced training courses designed to increase their selling skill set and knowhow. After significant change and reorganization in 2017, we were successful in stabilizing and transforming our sales team into a more effective, motivated growth force. Yet, we know there is much more to do. For the full year, nearly 80% of our growth in delivery gross profit dollars flowed through to adjusted EBITDA and our conversion ratio increased 80 basis points to 33.4%, a solid improvement.

In Canada, 2018 was a very challenging year for us, particularly in the fourth quarter. Double digit growth in our core industrial chemicals business for the year was more than offset by a second consecutive year of adverse weather conditions that significantly reduced demand for agrochemicals. In addition, reduction in demand from the Canadian energy sector led to an overall decline in adjusted EBITDA of 23% in the fourth quarter and down 8% for the year. Recognizing the challenging market conditions, our teams in Canada prudently reduced spending and working capital.

By comparison, our Europe Middle East and Africa segment had a very strong year and grew adjusted EBITDA by 17%. Customer and supplier acceptance of our go-to-market strategy remain strong and our focused industry approach has been well received. Our supplier partners trust our ability to drive higher customer engagement and sales.

In the fourth quarter, EMEA was our strongest growth region as adjusted EBITDA grew 8% currency neutral despite some signs of economic slowdown as a result of Brexit worries and tempered macro growth expectations for the Eurozone.

Our Rest of the World segment grew adjusted EBITDA by 16% in 2018 as our leadership team executed well with Mexico showing improvement and Brazil posting a solid year. In the fourth quarter however, strong performance in Mexico was offset by softness, particularly late in the quarter in Brazil. Adjusted EBITDA grew 4% on a currency neutral basis, but fell 6% on a reported basis due to change in FX translation rates versus last year.

Moving now to cash flow, net working capital was a cash inflow in the fourth quarter of $197 million, reflecting our usual back end of the year release of working capital. Excluding Canadian agriculture, our 13-month average net working capital as a percentage of sales was an industry leading 12.3%, in line with the third quarter and the prior year. CapEx was $35 million in the quarter and $95 million for the year, an increase of about $12 million from 2017.

Our effective tax rate for adjusted EPS in the fourth quarter of 28% was higher than the prior year fourth quarter of 18%, largely due to recognizing for book purposes more benefit in 2017 from utilization of net operating loss carry forwards than in 2018 along with certain impacts from the 2017 U.S. Tax Act. The higher tax rate was a headwind of $0.05 per share in the quarter and $0.27 per share for the full year.

We continue to earn a superior return on investment. Our return on assets deployed increased 190 basis points to 24.7% from 22.8% a year ago. Other return on capital metrics like ROIC, CROCI, our internal Univar value-added metric also improved from last year. We expect these metrics to continue to increase as we implement our plan and proceed with our integration and value capture activities associated with the Nexeo acquisition.

We continue to allocate cash flow heavily towards deleveraging. Since Univar's IPO in 2015, our leverage ratio has declined from around 5 times to 3.5 times at the end of last year. As a reminder, we paid approximately $1.8 billion for Nexeo in cash and stock. Consistent with our focus on our core strength in chemical and ingredients distribution, we led a process to evaluate strategic alternatives for Nexeo's Plastics business, which resulted in an agreement on February 8 to sell the business for $640 million subject to customary closing conditions. We expect the transaction will close sometime in the second quarter and we will use the net proceeds of approximately $650 million before transaction costs to immediately pay down debt. We expect our consolidated net debt to be approximately $2.9 billion after the acquisition of Nexeo and the sale of Plastics.

Following that announcement on February 8, Moody's and Standard & Poor's both upgraded our credit rating. In addition, Fitch launched its review of Univar with a rating comparable to S&P. Including the acquisition of Univar and the sale of Plastics, we now see leverage at around 3.5 times by the end of this year. We plan on deleveraging to below 3.0 times and we'll reassess at that time our capital deployment priorities to maximize value for shareholders. Whether it is through increased investment in digitization, sales force effectiveness, additional smaller scale bolt-on acquisitions, further reducing our debt or directly returning cash to shareholders, our focus will be on achieving the highest risk adjusted return.

Let me finish then by addressing our revised outlook for 2019 which now includes 10 months of earnings from Nexeo chemicals. As a reminder, three weeks ago we provided our forecast for Univar on a standalone basis that generate adjusted EBITDA about in line with 2018 results of $640 million. With the Nexeo transaction closed, we have begun the integration now of customers, suppliers and products, and we will lose the ability to track historic Univar or historic Nexeo results. Therefore, we will not provide updates on standalone guidance going forward.

We laid out our assumptions in the earnings press release on February 8 so I won't go through them one-by-one, but I do want to highlight a few key points. First, we are forecasting slower, flattish industrial production demand for chemicals across all of our segments, down from the historical projections of 1% to 2% growth. Based on what we've seen from customer ordering patterns in the fourth quarter and now again in the first quarter, we think it's prudent to expect continued malaise in demand.

Secondly and as David mentioned, we are forecasting modest improvement in sales force efficiency. We see positive signs of improvement and remain confident in our ability to improve the effectiveness of our sales force, but we have more work to do. As we make progress here, we are mindful of the challenges our sales force will face from an uncertain demand environment.

Thirdly, higher transportation costs were a meaningful challenge to us in 2018 and we are estimating sustained high outbound freight costs per pound for this year as well. We've undertaken a range of actions to mitigate the impact of these costs. And while we have already seen improvements in the fourth quarter as a result of these actions, progress was partially offset by a shift in mix to more bulk chemicals where we rely heavily on common carriers for transportation.

With these assumptions in mind, we expect to earn adjusted EBITDA in a range of $740 million to $760 million in 2019. This reflects 10 months of earnings from the Nexeo chemicals business and approximately $10 million in realized synergies. We expect to generate $300 million to $350 million in free cash flow excluding one-time integration costs of approximately $70 million. As a reminder, we expect one-time costs to be approximately $150 million over the three-year period 2019 through 2021. However, we also expect to largely offset these costs with one-time gains from the sale of excess real estate and working capital improvements.

Regarding adjusted earnings per share, we are in the early stages of measuring the impact of purchase accounting of GAAP EPS for 2019 and therefore are not providing EPS guidance at this time. We expect the first quarter of 2019 to be the weakest comparison quarter of the year, reflecting continued sluggish demand from most end markets, stiffer FX translation impact and tougher comparisons due to a one-time benefit in the first quarter of last year that we called to your attention at that time.

Our management team is fully cognizant of the challenges that can arise in a downturn. We have to find the right actions to take if that scenario develops and we will move quickly, while simultaneously reaping the benefits of the Nexeo acquisition.

David, I'll turn it back to you.

David C. Jukes

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

Thank you, Carl. In 2018, we made significant strides on our journey to become the world's most valuable chemical and ingredient distributor, and the acquisition of Nexeo is a major milestone for us. Since announcing the deal on September 17, joint Univar and Nexeo teams have worked hard to prepare for the close and plan for integration. We created an integration management's office staffed with senior proven executives with complementary skills and cross-functional expertise from both companies, laying out detailed plans and timetables so we could hit the ground running.

To ensure that we are building sound comprehensive plans, we hired world-leading consultants in mergers and acquisitions, human resources and supply chain management. Further, the Compensation Committee of our board has evaluated senior management's compensation and is linking variable incentive compensation to the success of this integration, including our capture of the synergies and importantly our return on invested capital.

As Carl mentioned earlier, we completed our evaluation of strategic alternatives for Nexeo's Plastics business and have reached an agreement to sell it to focus on our core chemical ingredient distribution business. Our team continues to evaluate the possibility of further divestitures to accentuate this focus and ensure we maintain the appropriate business mix long-term.

Over the past few months, we have developed detailed plans assigning leaders to work streams to capture the $100 million in net annual operating synergies [ph] net of any customer and supply dissynergies (00:23:59). These synergies were identified and confirmed through a detailed bottoms up analysis on a function by function, line by line basis, where our integration teams have been able to lay out the specific tasks and timelines to achieve them.

With Nexeo officially a part of Univar, let me walk you through the plans we have in place to integrate the business. In many respects, the Nexeo integration is an extension of programs we already have in place. Our Chief Integration Officer is Jenn McIntyre. For several years now, Jenn has led Univar's extensive internal operational improvements [indiscernible] (00:24:44) consolidation programs.

In her chief integration officer role, she now has drawn on her experience at Univar and her early career in the chemical industry, and has been supported [ph] and schooled (00:24:56) by the senior partners of one of the world's leaders in acquisition integration to ensure we have a robust pressure tested and proven execution plan. As I mentioned earlier, Jenn also oversaw the efficient closure of a number of Univar sites over recent years, and now has the benefit of a proven team and playbook to execute on our site consolidation plans. Nexeo provides another significant opportunity to further optimize our overall supply chain footprints.

We estimate over a quarter of our combined sites in North America are candidates for closure. Our plan is to stop with some smaller sites first and work in manageable ways over the next two years to do this in a methodical way bringing forth transparency with our employees. With Jenn's leadership and expertise in this area, we are confident we will achieve this.

We also see the ability to reduce transportation costs by increasing the density of our routes and utilization of our enlarged fleet and we will implement some lean programs across the combined organization. I have every confidence in Jenn's ability to lead this integration well.

We've already made meaningful progress in our IT integration. We completed a roadmap to systems integration that ensures business continuity, manages migration risk, and meets the needs of the combined business. We are well into the process of analyzing and mapping master data in preparation to load Univar's data onto Nexeo's platform. We expect this process to take a few months and it will run concurrently with our training and change management works streams that we're preparing Univar employees to convert to the Nexeo systems.

The Nexeo IT team also has prior experience successfully integrating acquisitions onto their systems platform including CSD, Archway and Ultrachem. For our current situation, we'll be rolling the Univar locations onto the platform in multiple ways of manageable groups of Univar districts and branches.

Our commercial integration is also underway. Brian Herington who previously led Nexeo's chemical business has taken a leadership role as Univar Solutions' Chief Commercial Officer. In this new role, Brian will lead product management, sales force excellence and programs to work with our suppliers on a global basis. Brian has been leading integration planning for our commercial organization, leveraging his prior experience of successfully integrating a large scale acquisition when which combined a 1,000-person sales force.

We've been clear all long during this process that the sales force is one area we are not looking at for synergies and we will manage our sales force transition carefully. We spent the first part of this year mapping out the sales leadership and I've announced changes deep into the organization to align for growth and success using the robust data driven selection process to ensure we have leaders who epitomize the values of Univar Solutions and bring together the best of the best.

We expect to have our remaining organizational changes completed by the end of the second quarter once our key leaders have a chance to work in their new roles in the combined organization. When the claim teams analyze our combined customer data, we found there are minimal overlaps in customers who purchase the same products at the same locations from Univar and Nexeo. We've created processes to resolve any potential conflicts to reduce the risk of disruption in our sales force.

Most importantly ,the efficiencies we create will result in significant additional capacity within our combined sales force to prospect for new business and deliver growth. We are encouraged so far by the excitement we are seeing from our sellers and are pleased to report that the sales force churn in both companies has declined since we announced the transaction. Our sellers see the power of the combined platform and are excited about the opportunity for each of them to grow their career and their business.

Finally, I must make comments, we are acutely aware of the magnitude of effort this integration is going to take and I'm not taking that challenge lightly. As I previously said, we've been supported by recognized leaders in acquisition integration to make sure we have the most thorough, detailed and robust plan, and the work with our team has been outstanding.

Together with them, this team is committed to getting it right and is intensely focused on achieving an efficient and thorough integration with Nexeo with the absolute minimum of disruption to customers and suppliers. Of course, this will not be completed overnight. We will update you each quarter on our progress.

Overall, 2018 was an exciting year and the fundamental elements of our strategy is stronger than ever. With Nexeo, we have an even greater line of sight and even more levers to create value for our customers, suppliers and shareholders. While there have been and will be bumps along the way, we're making meaningful progress on our initiative, and our model is proving its ability to generate cash flow through the cycle.

Now with Univar Solutions, we have the ability to streamline and further reduce our costs to innovate and lead the digitization of the industry and grow in creating long-term sustainable advantage. Thank you for your attention, and with that we'll open up it to questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Robert Koort with Goldman Sachs. Your line is open.

Robert Koort
Analyst, Goldman Sachs & Co. LLC

Q

Thank you. Good morning. Two questions if I could, David. First, you mentioned that the sales force effectiveness has been maybe behind plan. Can you give us some more specifics on what measurables or what symptoms you see that are causing those conclusions and how to rectify it?

And then secondly, it seems your outlook on the economy, the chemical economy seems far more downward than maybe some of your suppliers and so, I guess, I'm wondering can you characterize it as careful and prudent conservatism or do you think maybe the rest of the world is not seeing things that you guys see more on the frontlines of the distributor, maybe help me reconcile what seems to be maybe a little bit of a parallax in views. Thanks.

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

A

Thanks, and good morning, Bob. Let's address the sales force first. I mean I think, well we've got evidence that our plan is working and we've made significant progress on a number of the key metrics, the financial metrics over the last couple of years. We've said before, I think the U.S. transformation is lagging probably a couple of quarters behind where it needs to be. We've faced a number of challenges on that, I think first is the velocity of price changes last year, it meant that sellers really have to deal with price rather than I'm talking about an extra product to sell or seeing a new customer. And I think also the legacy Univar internal processes and systems were more complicated than probably I appreciated a couple of years ago, and that sucks up time from our sellers to go prospect.

Having said that, we did improve the quality of the sellers, we [ph] turned over (00:32:50) almost all the sales force and our retention levels have been good. We trained several hundred of them, I think 300 went through the development program last year. We've increased the call rates for the sellers by around 20%, 25% and that's all trending in the right direction and very positive.

I think as far as the new organization is concerned, Nexeo allows us to streamline those backend processes which will create more capacity in the sales organization and allow us to grow. And I think secondly with the degree of overlap that we are seeing between the legacy Nexeo and legacy Univar customers, given that we are committed to maintaining the size of the sales force where it is today, the combined companies, we're going to create, I don't know, 20%, 25% free capacity in that sales organization to go grow and go sell to new customers.

And I think most encouragingly since we announced the deal, we have seen a reduction in the attrition of the sales force on both sides. So we have a lot of engagement from all our people. I mean just a huge amount of optimism and enthusiasm and engagement from all our people and particularly our sellers are excited about the opportunities that Univar Solution (sic) [Univar Solutions] (00:34:12) brings and the ability for them to grow their business and to grow their paycheck.

As far as the demand is concerned, I mean demand is up and down, demand is patchy right across the globe. I don't know whether we are seeing something before other people or not. I think certainly looking through a producer lens they see different things than we see typically. But the markets are getting more difficult because of uncertainty in the markets. The European markets are trickier with Brexit, [indiscernible] (00:34:44), Italy, Spain, Germany, they're all more difficult markets than they were this time last year, and the U.S. some weeks are good, some weeks are less good. There's a certain amount of uncertainty in the U.S. markets as well.

We have good strategies to approach that. We have good strategies to deliver on that. And what we are seeing with the big bulk chemical and supplies, customers slowing down a little and we're seeing good mix in Richmond from the focused industry starting to pick up and we're seeing that reflecting in our margins in the first quarter so far. So I think that we will ride the market the best way we possibly can and are pretty encouraged by how we're doing that.

I think the other thing to say is we're going to be pretty prudent about how we outlook. I think that our previous outlooks were based on us running at ten-tenths. I don't think we're going to run at ten-tenths, things happen and we're going to factor those in, so you'll see us being very prudent in our forecast going forward.

Robert Koort
Analyst, Goldman Sachs & Co. LLC

Q

Got it. Thanks for the help.

Operator: Your next question comes from the line of David Begleiter with Deutsche Bank. Your line is open.

David I. Begleiter
Analyst, Deutsche Bank Securities, Inc.

Q

Thank you. Good morning. David, just on how does the implied Nexeo guidance compare to what they did last year? And are you expecting any business loss from Nexeo or Univar from the combination?

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

A

Well, let's address the business loss first, I mean, I think their outlook is pretty – the outlook is pretty flat with the – with last year. But in terms of the customer and supplier reaction, I mean we're seeing – I mean we're just now getting first sight of the data, the data has been in the clean room. So I would assume first slides of the data and the dissynergy risk that we see in that is about what we expected in the due diligence.

On the supply side, we've been out and we surveyed 30 something suppliers as part of the due diligence to see what they wanted, to see what they were looking forward, to see what their thought was, that's been at the upper end of our expectations. So most suppliers are optimistic about the new company, and believe that the enhanced capabilities of both organizations really provide a compelling opportunity. They're excited about the digitization of the business and what that can bring, and the ability that we are going to have to bring them transparency through the supply chain, something that they've long looked for and has been inhibitor of growth.

So from what we've seen so far, it's pretty much in line with where we expected in due diligence and the outlook for Nexeo was roughly flat with last year.

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

A

Yeah, I'll add on to that. David, it's Carl. The way we see this, the industrial production outlook at Nexeo prior to the acquisition was very comparable to what we see going forward in terms of this oscillating demand that we've seen in the last five months. So, very much aligned there.

David I. Begleiter
Analyst, Deutsche Bank Securities, Inc.

Q

Very good. And just on the synergies, $10 million this year. How should they ramp up in 2020 and 2021?

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

A

Well, we – I'll just repeat what we said I guess back in September, we're very much on track with what we said back in September when we signed the contract on September 17. Ramping up to $100 million, we should be cumulatively at in-year savings of about $60 million in 2020. That was our previous guidance, we stick with that. And then in year three, 2021, about $90 million to $100 million. So, and I think as David said, everything we've seen since September gives us even higher confidence in achieving that.

David I. Begleiter
Analyst, Deutsche Bank Securities, Inc.

Q

Thank you very much.

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

A

Thanks, David.

Operator: Your next question comes from the line of Kevin McCarthy with Vertical Research Partners. Your line is open.

Kevin W. McCarthy
Analyst, Vertical Research Partners LLC

Q

Yes, good morning. Just trying to bridge to your new guidance, you put out the $640 million on February 8 and you're calling out $10 million of synergies. So, is it correct to say that you're baking in about $90 million to $110 million for the ten-month period that you'll Nexeo in 2019?

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

A

Yes, that's exactly right, Kevin. It's Carl. That's about $100 million for the Nexeo chemical operations. Just to remind everyone that it excludes their Plastics business which we'll report as a discontinued operations, and about $10 million in synergies between now and the end of 2019.

Kevin W. McCarthy
Analyst, Vertical Research Partners LLC

Q

Okay. And then would you comment on what you're baking in for a volume growth forecast in 2019?

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

A

Generally flattish, Kevin. I mean, based on what we've seen in the fourth quarter and continuing in January, February in that 0% to 1% range which is a notch down from where we were. So as we were saying earlier, we think customers – we sell to the manufacturing sector of the economy. People that make things and – versus the headlines in the media and we think people are playing a cautious and adjusting their inventory levels.

Kevin W. McCarthy
Analyst, Vertical Research Partners LLC

Q

Okay. And last one in the housekeeping category, on slide number 15 in the second footnote that appears there, I think you indicated about 92 million Nexeo shares. I was under the impression that that we'll be tracking closer to 90 million. And so, I'm wondering if you could refresh us on what happens with the warrants and how those are being treated in this year, [ph] Carl (00:41:15) if there's any change there or otherwise that would cause a little bit of upward tension in that number.

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

A

Yeah. Okay. The 92 million versus 90 million, Kevin, let me get back to you on that. I think it's 92 million. The warrants – we've reserved 7.6 million Univar shares to account for or be prepared for the potential exercise of those warrants. They – those warrants, to remind you, have a limited term that expire in June of 2011 and – 2021 I'm sorry, 2021. So that two and a half years out and [ph] on an (00:42:02) equivalent Univar strike price are around $27.80, that's the strike price.

Kevin W. McCarthy
Analyst, Vertical Research Partners LLC

Q

Okay. I'll circle back. Thank you so much.

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

A

Okay. Thanks.

Operator: Your next question comes from the line of Jim Sheeshan (sic) [Jim Sheehan] (00:42:19) with SunTrust. Your line is open. Jim, your line is open.

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Thank you. Sorry about that. In talking about your outlook for flattish industrial production, could you just talk about what you're seeing currently and what you've seen over the past couple of years in terms of an outsourcing tailwind for your business?

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

A

Sure. I think that this is one of the questions that we address fairly frequently. I think across the course of my career in the chemical industry the outsourcing trend has been [indiscernible] (00:43:05). One of the things that is really inhibited to outsourcing is the ability to execute consistently well across a range of geographies, and secondly the visibility of the business once business passes across to distribution. One of the things that we have seen is because we are now more able to execute more consistently across a range of reasons and geographies, we're becoming more attractive to suppliers and that's driving the supplier authorizations.

And secondly with the digitization that we're about to bring and able to bring, we are able to bring a transparency along with supply chain which is something which suppliers really value because they can see exactly what's happening to their business, it doesn't just disappear into a black hole. So we think that's going to be a source of competitive advantage for us as we continue to grow and develop, and will help us win more than our fair share of the outsourcing trend.

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Thank you. And...

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

A

Jim in terms of the impact on our guidance, we are pursuing new authorizations, some of those are outsourcing, taking business that was previously sold by the supplier directly into the market and some is winning business from other distributors. But we have dialed into our guidance a modest increase in earnings from new authorizations including that factor of additional outsourcing.

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Thanks, Carl. And also on your free cash flow guidance does that include debt amortization?

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

A

That does not include debt amortization. We have about $6 million of debt amortization to pay under the new debt structure in 2019.

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Thanks, Carl.

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

A

[indiscernible] (00:45:10) it's about $6 million for this calendar year.

Operator: Your next question comes from the line of Steve Byrne with Bank of Montreal (sic) [Bank of America Merrill Lynch] (00:45:21). Your line is open.

Steve Byrne
Analyst, Bank of America Merrill Lynch

Q

David, hello. A question for you on your comment around a quarter of the distribution facilities were candidates for closure. Did I hear that correctly? Is that – is it just based on the overlap of the footprint of the [indiscernible] (00:45:45) distribution facility? And maybe what would you see as an optimal number of closures to a high throughput and utilization at the existing facilities?

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

A

So what we've done is look to – what we are doing is looking at each facility and the capabilities of each facility, the technical capabilities of each facility, the capacity of each facility, the customer density around those facilities, the permitting around those facilities. And so if it makes sense to combine facilities and not disrupt service, in fact if we can enhance service then that's what we'll do. And so the 25% of the sites that we're considering, I mean we're looking at all the sites that we have and then deciding which ones are going to be key anchor sites for us to drive growth for the future. And those are just some of the things that we're looking around, some of them will require some capital expenditure if we want to do that. But some sites will have some unique capability which we want to retain if the business through there is profitable.

I think going forward, I don't know what the ultimate number is. I think that as we – what we look to do is to provide a differentially high level of service to customers. So our on time and full rates are roughly in the high 90s. We want to keep them there. That service requirement, that reliability that easy to buy from is core parts of our value offering for customers. So, I don't have a number that's an optimum in mind, but we'll continue to invest in those key sites now, and we'll be able to afford to invest in really making them technically more competent and digitally more capable which will allow us to capture a lot more growth at a higher service level.

Steve Byrne
Analyst, Bank of America Merrill Lynch

Q

And can you comment on how much cost synergy you could achieve from some fraction of those closures? And I assume none of that is in your $100-million guidance.

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

A

Well, I think it is. So, in the $100-million synergy guidance, there is a proportion around asset closures, I think it's a little under a third. The $100 million is around asset closures, so that's what we've disclosed.

[indiscernible] (00:48:13)

Steve Byrne
Analyst, Bank of America Merrill Lynch

Q

I'm sorry, Carl.

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

A

It's one of our top three areas of synergy capture, cost capture, yes.

Steve Byrne
Analyst, Bank of America Merrill Lynch

Q

How much of that is in that quarter of the facilities, can you comment on how many facilities that is?

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

A

Well, we've said that we have round numbers about 100 facilities in United States, and then Nexeo has about 40 ex-Plastics. When we're done, we should have about 100 facilities, and I think that it's important to recognize that we also – we've got great density, we don't need to add any territory, and we also operate generally one shift a day, though we have plenty of capacity to increase volume in this business plan and we intend to do so.

Steve Byrne
Analyst, Bank of America Merrill Lynch

Q

Okay, and just one last one. Are you considering the merits of staying in that Canadian ag business given the potential for disintermediation by some of the e-commerce platforms that are in development in ag?

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

A

Well I know this is one that you've been keen on for a while. Look, I mean, I think that we are really laser focused on being the most valued chemical ingredient distributor on the planet, that's our focus. The Univar Solutions' mission is to really find distribution and be the most valuable chemical ingredient distributor on the planet. And so that's what we're going to be laser focused on. And to the degree that any of our businesses [ph] adds or be traction (00:49:45) that then we'll look at what the future of those businesses are based on their profitability, their growth and their return on capital.

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

A

Yeah, and I would add to it. I know that – your reference there. I wouldn't attribute it to disintermediation. It's a great business that we have in ag. It earns a wonderful return on capital and provides a great service to the consumers of agro chemicals in Canada, and so we continue to focus on that and we will continuously evaluate our portfolio of all businesses including ag.

Steve Byrne
Analyst, Bank of America Merrill Lynch

Q

Thank you.

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

Thanks, Steve.

Operator: [Operator Instructions] Your next question comes from Duffy Fischer with Barclays. Your line is open.

Duffy Fischer
Analyst, Barclays Capital, Inc.
Q

Yeah. Good morning. First question is just around free cash flow and the change in guidance from regional, your EBITDA went up $110 million at the midpoint but the cash flow only went up $50 million at the midpoint. Why is the conversion so poor on that incremental new EBITDA because you're excluding the cash cost for restructuring?

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

Yeah, that's right Duffy. We're adding about $50 million, we don't have a good feel or sense yet for the working capital ups and downs of that added chemical business from Nexeo. Once – as of Friday, these two businesses are merged and there is no longer historical Nexeo and historical Univar, so we'll get a better hand on the working of their receivables and payables and steady cash flow. Your observation is correct. It's a bit lower than what we would expect from our chemicals business but we'll work through that in the coming month.

Duffy Fischer
Analyst, Barclays Capital, Inc.
Q

Okay. And then could you bucket for me if you go back to the original $208 million of LTM EBITDA that you got with Nexeo, how much of that goes in the sale, how much of that is kind of in the pro forma, and then how much of that gets eaten up by say stranded costs when you made the Plastics sale?

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

Okay. Roundly, Duffy, on that one-third, two-third is the split of that LTN between Plastics and chemicals. As far as [ph] trading to Costco (00:52:16), we've got a – with the buyers of Plastics, we've got a transitional services agreement in place that will provide what's needed to the buyer. And our management of those services and the cost to deliver them will be very focused on eliminating or avoiding stranded costs.

Maybe the most difficult area will be IT, the IT area where it's hard to really disengage from the fixed costs associated with IT. But for the other services provided, they are much more people related and we've got dedicated resources in place to provide those services and we'll adjust as that TFA agreement expires.

Duffy Fischer
Analyst, Barclays Capital, Inc.
Q

So, okay, just to clarify. So if you use your two-thirds of the original, that would be about $135 million of EBITDA that's pro forma still with you, but if you back into the guide like we did a little bit earlier in the call, you're kind of running at $110-million rate this year, is that $25 million delta that's come down is that the stranded cost, is that the way we should think about it and that will go away over time?

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

A

No, no, no, Duffy, that's just two months. You're dealing with 12 month numbers and we bought it last Friday. So, we're just including in our guidance 10 months' worth of Nexeo chemicals.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Oh! No, but the two months are the two smallest months of the year and you're getting $10 million of synergy. So I'd argue that those roughly offset that the run rate for Nexeo in your numbers is your looks like $110 million to $115 million.

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

A

I think, you're a little high, but it's – we're really just prorating 10 months of the year into our guidance.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Okay. Thank you.

Operator: There are no further questions at this time I will now turn the call back to the presenters.

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 follow up questions please reach out to the Investor Relations team. Have a great day.

Operator: This concludes today's conference call. You may now disconnect.