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Tronox Holdings Plc (TROX)

Q2 2021 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning and welcome to the Tronox Holdings Plc Second Quarter 2021 Earnings Call. All participants will be in listen-only mode. [Operator Instructions] After today's presentation, there will be an opportunity to ask questions. [Operator Instructions] Please note this event is being recorded.

I would now like to turn the conference over to Jennifer Guenther, Vice President, Investor Relations. Please go ahead.

Jennifer Guenther

Vice President-Investor Relations, Tronox Holdings Plc

Thank you, and welcome to our second quarter 2021 conference call and webcast. On our call today are John Romano and Jean-François Turgeon, Co-Chief Executive Officers; and Tim Carlson, Chief Financial Officer. We will be using slides as we move through today's call. Those of you listening by Internet broadcast through our website should already have them. For those listening by telephone, if you haven't already done so, you can access them on our website at investor.tronox.com.

Moving to slide 2. A reminder that comments made on this call and the information provided in our presentation and on our website include certain statements that are forward-looking and subject to various risks and uncertainties, including, but not limited to, the specific factors summarized in our SEC filings. This information represents our best judgment based on today's information. However, actual results may vary based on these

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risks and uncertainties. The company undertakes no obligation to update or revise any forward-looking statements.

During the conference call, we will refer to certain non-US GAAP financial terms that we use in the management of our business and believe are useful to investors in evaluating the company's performance. Reconciliations to their nearest US GAAP terms are provided in our earnings release and in the Appendix of the accompanying presentation.

Moving to slide 3, it's now my pleasure to turn the call over to John Romano. John?

John D. Romano

Co-Chief Executive Officer & Director, Tronox Holdings Plc

Thanks, Jennifer, and good morning, everyone, and thank you for joining us today. We'd like to start today's call by thanking all of our employees around the world for all the continued hard work and support, which allowed us to deliver these great results. Our second quarter results were very strong despite multiple supplier and logistics headwinds. This was another record for – record quarter for Tronox on TiO2 sales volumes, revenue, earnings per share, adjusted EBITDA and free cash flow, all enabled by the continuation of the market recovery, the strength of our differentiated vertically integrated business model, and the support of our customers.

Revenue in the second quarter increased 4% sequentially to $927 million, primarily driven by higher TiO2 and zircon average selling prices. This represented a 60% increase year-over-year. Net income for the quarter was $77 million and diluted earnings per share was $0.46, while adjusted earnings per share was $0.61. The difference between diluted EPS and adjusted EPS is due to debt redemption costs associated with our Q1 refinancing.

Our adjusted EBITDA was $237 million, setting yet another record for Tronox. This figure came in at the top end of our guided range due to improved commercial performance as expected, offset by higher inflationary pressures and operational disruptions. JF will review this in more details in a few minutes. Adjusted EBITDA margins improved to 26% for the quarter. We generated $150 million in free cash flow after investing $60 million in capital expenditures. We repaid $135 million in debt in the second quarter and an additional $70 million in July for a total of $205 million.

Our total debt balance as of today is $2.8 billion and our trailing 12-month net leverage ratio is 3.2 times. We are $300 million away from our total debt target of $2.5 billion and 0.7 times from the midpoint of our targeted net leverage ratio, representing significant progress in light of the strength of the cycle, our positioning and cash flow-generating capabilities.

Moving to slide 4, I'll now discuss our commercial performance in more detail. As I previously highlighted, the second quarter was a very strong quarter from a commercial perspective. TiO2 revenue was $740 million, an increase of 6% quarter-over-quarter and 59% year-over-year, driven by continued strength in customer demand. Sales volumes grew 1% quarter-over-quarter on the low end of our guided range, mainly due to supply chain challenges that limited vessel and container availability at a time when inventories were already below seasonal norms. This sequential growth was led by North America and Europe. TiO2 volumes increased 45% versus the second quarter of 2020, which was the quarter most greatly impacted by COVID-19.

Volume growth in Europe and Asia Pacific led the year-over-year recovery, though all regions saw a double-digit growth. TiO2 price increase initiatives continued throughout the quarter, resulting in a 5% sequential increase. This equates to a 9% increase year-over-year on a US dollar basis, or 6% on a local currency basis.

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Revenue from zircon sales declined slightly due to lower zircon volumes in the quarter as expected, partially offset by improved pricing. Demand continues to be very strong for zircon and we've been able to serve this growth in demand with inventory, which will continue to benefit us throughout the end of the year. Due to the tightness in the market, coupled with the increase in demand, pricing increased 5% from Q1 levels, or 1% over Q2 2020.

Despite the higher pig iron selling prices, feedstock and other product revenue declined 8% sequentially, as some pig iron volumes rolled into the third quarter due to timing impacted by logistics issues. On a year-over-year basis, revenues increased 50% due to significantly improved pig iron volumes and pricing, driven by strong end market recovery. There were no external CP slag sales in Q2 of 2020, so the year-over-year comparison this quarter is on a like-for-like basis.

Our global supply chain and logistics and order delivery employees navigated yet another quarter of disruptions to meet our commitments and serve our customers to the best of our ability. So, I'd like to thank all of those employees again around the world for a job well done. We believe we are still in the early stages of the cycle. Regional price initiatives are continuing across both TiO2 and zircon. Demand remains very strong throughout the supply chain, driven by the recovery across all of our end markets and we believe inventory levels throughout the supply chain continue to be well below seasonal norms.

As we look ahead to the third quarter, we are balancing strong customer demand against our ability to deliver based on continued supplier and logistics constraints. Taking these factors into consideration, we expect TiO2 volumes to decline 5% to 10% sequentially, which would still represent the strongest third quarter volume on record.

Zircon sales volumes are expected to remain elevated above 2019 and 2020 quarterly volumes, benefiting from sales from inventory, though volumes will be lower than the second quarter levels. Zircon pricing improvement in the third quarter is expected to more than offset the volume headwind. TiO2 and zircon prices are expected to continue to increase as we make progress with our regional price initiatives.

I'll now turn the call over to JF for a review of our operating performance and profitability in the quarter. JF?

Jean-François Turgeon

Co-Chief Executive Officer & Director, Tronox Holdings Plc

Thank you, John. Moving to slide 5. As John mentioned, adjusted EBITDA of $237 million was another record for Tronox. The increased volume and pricing, John outlined, support significant increase in EBITDA, which were offset by headwinds from unfavorable foreign exchange rate, inflationary pressure, and operational disruption. These operational disruption include the EBITDA headwinds we discussed on our first quarter earnings call, which were the $10 million impact from the planned five-year maintenance shutdown of our synthetic rutile production facility and the $4 million impact from the longer than anticipated downtime at our Botlek pigment plant due to an unexpected supplier shutdown. Additionally, we had a $5 million EBITDA impact from unexpected downtime at our Stallingborough pigment plant due to mechanical issue. All of these operational disruptions will roll of in the third quarter.

Digging a bit further into the comparison, adjusted EBITDA increased 67% year-over-year, driven by improved volume and selling price across all product as well as improve production costs, including synergy, partially offset by unfavorable FX rate and the operational disruption. Production costs were favorable year-over-year due to the improved operating rate at the mining site due to the COVID impact and smelter relying cost in South Africa in

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2020. Sequentially, adjusted EBITDA improved 5% due to the improved pricing and production costs, partially offset by operational disruption, unfavorable FX rate, and lower co-product volume.

Production costs were favorable partially due to improvement at our Yanbu pigment facility, which continued to deliver above expectation. Inflationary pressure, including both external ore purchase and raw material such as energy and sulfur price as well as increased logistic costs continue to impact our earnings. Additionally, you would have seen the news about the riot that occurred in South Africa. We want to assure you that our operations were not directly impacted. However, there were disruption to KZN port, which at this point haven't materially affect us. However, there is some risk that some of our shipment could be delayed as the port continue to work through the backlog.

While the operational disruptions for the second quarter are not recurring, pressure on the cost side of the business coupled with chlorine availability issue are expected to partially offset continued price increase in the third quarter As a result, we anticipate third quarter adjusted EBITDA of $245 million to $260 million.

Turning to slide 6. This is a critical time for Tronox. While overcoming these various challenge, we remain focused on progressing project newTRON or enterprise-wide cost reduction initiative that will transform our business and more than offset raw material and fixed costs inflation, enabling us to remain among the lowest cost TiO2 producer and enhance service to our customer. We will achieve this through an optimized global supply chain, reduced maintenance spend, enhanced operation, improved throughput, and standardized process. This project is especially important given the increasing costs we are facing. We expect newTRON to unlock cost reduction of $150 to $200 per ton by the end of 2023. We look forward to updating you on our progress.

Our vertically integrated business model continues to differentiate us from our competitor providing security of supply, a global footprint that we can leverage to our customer advantage, and co-product that contribute significant value to our portfolio. We are on a journey of transformation and continue to deliver on our commitment to our stakeholder. We demand a lot of our organization, and our people continue to respond. We are grateful for the ongoing effort of our colleague around the world to deliver safe, quality, low-cost, sustainable ton for our customer. Thank you.

Turning to slide 7. On this last point, producing safe, quality, low-cost, sustainable ton is a key part of our strategy and how we strive to differentiate ourselves. Though sustainability has long been a part of everything we do at Tronox, we are improving how we disclose our progress and effort related to our ESG performance as it become an increasingly critical focus area for our stakeholder. This week, we published our 2020 Sustainability Report that highlights our commitment to improvement for the future. It provide detail on how we will align ourselves with a global warming scenario below 2 degree Celsius and achieve an aspirational goal of net zero greenhouse gas emission and zero waste to external dedicated landfills by 2050. The report also reinforce our Journey to Zero to achieve zero injury, zero incident, and zero harm. We invite all stakeholder to review this report on our website to learn about our accomplishment to-date and the aggressive goals we have set for the future.

I will now turn the call over to Tim Carlson. Tim?

Timothy Craig Carlson

Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

Thank you, JF. On slide 8, on the left hand side, we have outlined our liquidity and capital resources at the end of the quarter. We have $767 million in total available liquidity, including $303 million of cash and cash equivalents, which is appropriately distributed across our global operations. Our current liquidity is more than sufficient to operate the business.

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Moving to the right hand side of the page, capital expenditures in the second quarter were $60 million. CapEx is expected to increase in Q3 and Q4, reflecting the pacing of expenditures related to newTRON and Atlas Campaspe capital projects in the year, as well as other maintenance spend, though we are bringing our outlook down to $300 million to $325 million given our mid-year reassessment of where we are in terms of capital deployment.

Depreciation, depletion and amortization expense was $71 million in the quarter and we expect DD&A to be approximately $300 million to $320 million for the year. Our free cash flow for the quarter was $150 million due to our strong cash earnings. We also returned $28 million to shareowners in the form of dividends year-to-date. Given the continued strength in our cash generation capabilities, our confidence in our business model and our view on the cycle, we are increasing our quarterly dividend by $0.02 per share to $0.10, bringing our annualized dividend to $0.40 per share. We expect to continue to generate significant cash flow and believe that we'll be able to soon achieve our debt target and we'll continue to evaluate our capital return to shareowner policies moving forward.

Turning to slide 9, I'd like to share our outlook. As John mentioned, both TiO2 and zircon prices are expected to increase, as we make progress with our regional pricing initiatives. TiO2 market demand remains very strong, though we're balancing our market outlook with the supplier and logistics constraints including chlorine availability issues. We expect third quarter TiO2 volumes to decline 5% to 10% from record second quarter levels.

Zircon sales volumes are expected to remain elevated above 2019 and 2020 quarterly volume levels, though lower than Q2 levels. We expect our Q3 2021 adjusted EBITDA to be in the range of $245 million to $260 million due to lower volumes, inflation, raw material price increases, and chlorine availability issues, partially offsetting expected price improvements and the second quarter operational disruptions rolling off.

FX rates have come off through their recent lows, [ph] though we continue (00:18:39) to be a headwind year-over-year, recall that a one move in the ZAR is equivalent to approximately $7 million to $8 million on a quarterly basis, a AUD 0.01 move in the Australian dollar is equivalent to approximately $1 million to $2 million on a quarterly basis, taking into account our current hedge position which will benefit us through the second quarter of 2022. Beginning in the third quarter of 2022, it will increase to $2 million to $3 million per quarter, excluding the hedge.

Moving on to our expectations for full year 2021, we anticipate the following uses of cash. Net cash interest expense of $140 million to $150 million. $40 million to $50 million of cash taxes, an increase of $10 million, given our increased earnings expectations for the year. Capital expenditures of $300 million to $325 million, which includes expenditures related to newTRON and Atlas Campaspe. And pension contributions of less than $5 million. We continue to actively manage working capital to be a source for the year. Net-net, we expect strong free cash flow generation despite cost pressures on the business that will be used to continue to delever over the remainder of the year. These represent our estimates based upon our current market outlook.

I'll now turn the call back over to John for closing remarks before opening the call up for questions.

John D. Romano

Co-Chief Executive Officer & Director, Tronox Holdings Plc

Thanks, Tim. JF, Tim and I are very proud of the organization's accomplishments in the first half of this year. This is a critical time for Tronox. We remain confident that our portfolio of assets and market position, we are prepared to continue to capitalize on the momentum and delivering on the commitments to our stakeholders. We have

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continued to operate with our future in mind and are diligently progressing on the previously identified key capital projects to reduce costs and ensure we sustain our advantaged position.

That concludes our prepared comments. And with that, I'd like to turn the call over for questions. Operator?

QUESTION AND ANSWER SECTION

Operator: We will now begin the question-and-answer session. [Operator Instructions] The first question is from John McNulty of BMO Capital Markets. Please go ahead.

John P. McNulty
Analyst, BMO Capital Markets Corp.

Q

Yeah. Good morning. Thanks for taking my question. Maybe we can dig into the supply and freight issues a little bit more. Can you give us whatever clarity you might have as to the timing of when we might be able to start to see some of these issues get resolved? I know there are certainly kind of moving targets right now, but any color that you might be able to give us would be great?

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

So, John, I'll start with that and I'm sure John can add. Look, we see the issue that will last until the end of the year. Look, I know that at the beginning of the year, we thought that for the second half of 2021, that would improve. But really the reality is, everything is still very, very tight. And the visibility that we have at the moment bring us to the end of 2021 and it's still a challenge to get vessel, to get container, to put the material in and to move things around.

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Yeah. John, I guess from the standpoint of – and it's kind of two things. Also, it's the logistics switch. Again to JF's point, we would hope by the end of the year that we'd start to see and get some relief from that, but it's really hard to say at this stage, it hasn't gotten any better. And then from our ability to continue to work with our suppliers, we've had other issues. Clearly, there was some disruption in the first quarter that had to do with the storm Uri, that has been exacerbated by other issues that we've talked about regarding chlorine, not only in the US, but also in our plant in Stallingborough.

John P. McNulty
Analyst, BMO Capital Markets Corp.

Q

Got it. And then assuming that these issues aren't just specific to Tronox, I guess can you speak to what all of this means for the ability for the industry to start catching up in terms of building inventory, kind of getting back on track, as it does seem like things are pretty thin and I would imagine this makes it thinner, but I guess I'd love some color from you guys on that?

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Yeah. Look, from the standpoint of the – we think the entire supply chain with regards to inventory is below what we refer to a seasonal norms. And our ability to build inventory between now and the end of the year and meet

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customer demand with all the challenges that are going on is going to be difficult. This has absolutely nothing to do with demand. So I would suspect maybe to directly answer what I expect your hedging for and that is that demand will continue to be pent up and will likely elongate this cycle. And we have a lot of requests from customers for additional volume. I don't think Tronox is on an island with the transportation issues that are going on in the industry right now.

John P. McNulty
Analyst, BMO Capital Markets Corp.

Q

Got it. And then maybe just one last question. There was a lot of a noise around ore supply throughout the quarter and a lot of kind of data points picking up. Can you speak to your thoughts on global ore supplies and what it could mean for TiO2 pricing as well as the ability for the industry to either add capacity, debottleneck, et cetera? Thoughts would be great.

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Yeah. John, look, you're referring to Iluka announcing that they will shut down their mine that produce natural rutile in Sierra Leone, and Rio Tinto issue in KwaZulu-Natal shutting down their mine that feed their big smelter there. So, look, I think this play into the strength of Tronox, we're vertically integrated. So we have our own mine and our own concentrator and upgrading facility. We're 85% vertically integrated and the 15% that we buy [ph] on through (00:24:50) the market, I mean, we have had long-term contract in place and we're well equipped to deal with that type market.

You also know that we're going to start Jazan toward the end of the year. So I think we're in a very good position for facing that reality, which I think will play to our strength, because we will see our competitors seeing their feedstock costs moving up at a time where we're working hard on lowering the costs of producing out of our own operation.

John P. McNulty
Analyst, BMO Capital Markets Corp.

Q

Great. Thanks very much for the color.

Operator: The next question is from Josh Spector of UBS. Please go ahead.

Joshua Spector
Analyst, UBS Securities LLC

Q

Yeah. Hey, guys. Thanks for taking my question. Just when you talked about TiO2 volume sequentially in the quarter, you talked about improvements in North America and EMEA. Can you give us some color of what you're seeing in Asia Pacific and if any of the demand patterns changed or customer order patterns changed through the quarter?

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Yeah. Josh, so from the standpoint, we saw growth in every region. We made reference that we saw more growth in Europe and in North America in the second quarter. But we have not seen demand weakened at all. The growth has moderated a bit in China and I think that's where maybe there's some concern around what's happening. We don't see China weakening. We see that demand continuing to be significant. There's clearly

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some obstacles. We have an operation in China. Freight rates out of China and other regions of the world are very expensive right now. And it's not only the expense of the containers and the logistics, it's the port congestion. So all of what's happening I think in China right now from the standpoint of demand is still positive. There's some comments coming out with regards to what if – what's happening could be deemed as weakness and we don't see that at this stage.

Joshua Spector
Analyst, UBS Securities LLC

Q

Okay. Thanks. Appreciate that. And just in line with some of the comments around the volume constraints last quarter into three – third quarter, is there any region which you would say is seeing a bigger impact of some of those supply constraints and perhaps getting less material, and is that playing into your ability to get pricing in that region?

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

I think, I'll add and then, JF, if you want to make another comment, please feel free to. It depends on the timing. We mentioned the UK having a problem. The chlorine issue there was basically a power outage that created a problem for the chlorine provider in the UK. So that was an issue. There's been a lot of discussion about chlorine availability in North America. The logistics issue plays into our ability to export out of Australia quite frankly and that's a very congested market for us. We ship a lot of material out of Australia into other regions of the world. So I'd say that there's not really any one region that's more significantly impacted over the first half. I'd say in the second quarter, we may have saw a bit more in Europe and North America, although we still had very strong numbers in North America.

Joshua Spector
Analyst, UBS Securities LLC

Q

Okay. Thank you.

Operator: The next question is from Frank Mitsch of Fermium Research. Please go ahead.

Frank J. Mitsch
Analyst, Fermium Research LLC

Q

Hey. Good morning and nice results. I want to follow up on the feedstock supply issue and the ore supply issue. Certainly, there's going to be some inflation there. I'm just curious what your crystal ball is forecasting in terms of ore pricing over the next 6 to 12 months. What sort of order of magnitude would you anticipate ore prices moving up, given the supply difficulties that we're seeing there?

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

So, Frank, well, you know that we don't speculate on what price will do going forward. So I think that your guess is as good as ours. Look, we certainly see a tight market. But we feel that as Tronox, we're in a good position with our own production. And because we don't sell any feedstock onto the market, I mean we're not trying to speculate what will happen with price.

Frank J. Mitsch
Analyst, Fermium Research LLC

Q

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JF, with all due respect, your guess is way better than mine on the outlook there. But understood. And I believe you mentioned that Yanbu – sorry, I wanted to ask about Jazan start of year end, what's your confidence level there, what's the progress there, can you give us a more granular update?

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Yeah. Sure. Look, we're very confident that we're going to start. Look, mechanical completion is almost done. We're looking at the end of August to have Metso Outotec complete all of the change that we wanted to the facility. And look we have, in parallel, start co-commissioning of the new equipment that were installed and the change that were put in place. And we're looking at [indiscernible] (00:30:20) commissioning starting in October. And look, this is in line with what I mentioned at the last earnings call. There was a bit of delay because of COVID-19 and getting some of the material to finalize the modification on site. But all of that material is now on site almost. Well, we're at 96% completion of the installation of that. And look, we should see our first slag in the last quarter of the year. So that's basically the update. Not a lot of change since last quarter, but still continue to progress.

Frank J. Mitsch
Analyst, Fermium Research LLC

Q

Got you. Understood. And then, lastly, on Yanbu operating above expectations, can you provide a little more color there?

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Yeah. Sure. Look, we broke a record of production at Yanbu in May, so we were very pleased with that. That's a record of all time for the plant. So that's in line with us telling you that we would be able to deliver synergy by transferring the knowhow of our Hamilton plan to this Yanbu plant in KSA and I guess it looks good for 2022, as we continue to see a strong demand that we'll be able to grow for production to meet our customer needs.

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

And Frank, just to add to that, that capability has also allowed us to transfer some of the legacy Tronox grades over to Yanbu, which is also helping us in these times where we need more production at a variety of different plants.

Frank J. Mitsch
Analyst, Fermium Research LLC

Q

Got you. Understood. Thanks so much.

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Thank you.

Operator: The next question is from Matthew DeYoe of Bank of America. Please go ahead.

Matthew DeYoe
Analyst, BofA Securities, Inc.

Q

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Thank you. So KZN Sands is fairly close to RBM and throughout the province, there is clearly an uptick in violence and unrest. And I know you had mentioned outside of the port, your operations were kind of somewhat unimpacted. I'm just wondering how that's the case and how you've been able to stay open, given the backdrop and what we've seen in operations just a couple miles down the road?

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Yeah. So Matthew, I'll try to give you some color. Well, our plant is in Empangeni, which is inland from Richards Bay. And look, it's true that there was riot. Look, it's all related to Mr. Zuma. I think that that was the drop that makes the thing start. But – and, look, what happened is you have people with extreme poverty in that part of the country and lots of unemployment and people vandalize the shopping center and grocery and fuel station and all that. You saw that on the news. But our people, we put a lot of effort in creating a special environment within Tronox with our value, with our outward mindset, and our people are our ambassador. And they knew that something was to happen in the community and we stopped trucking material in between the mine and the smelter and we put our truck back at our site ahead of those events happening, because our people knew that that would happen. So then things kind of blowed, went out of proportion, but nothing happened at our site. We had our people taking care of our asset.

And look, when government took back the control and police and the army came, well, we were able to restart right away with no damage and basically minimum impact to our operation and production. And that shows to the importance of working with your people, your employees. And I'd say that South Africa is probably better today than it was before that event, because, I mean, the good people took control of what happened. I mean, the era of Mr. Zuma, I mean, I'm not to judge, but, I mean, that was a bad time for South Africa and I think that things are improving there so.

Matthew DeYoe
Analyst, BofA Securities, Inc.

Q

Okay. And – thank you for that, JF. It seems like if I read your statements correctly or your commentary that there's some zircon inventory liquidation going on right now at Tronox, which is kind of boosting your numbers. If I were to think about next year and the type of volumetric headwind that could represent business, what should we think about beside that?

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

A

Yeah. So in 2022, our zircon revenues will migrate back to really 2019, 2018 levels, pre-pandemic levels. The inventory that we built in 2020 as a result of the pandemic were actually beneficial for us, because we were able to meet all of the market needs over the last couple of quarters. But with that being said, given how tight the market is, we have been able to offset some of that volume with price. In fact, more than offset that in the quarter. And we expect that to continue in Q3 and Q4. So while we will have a volume headwind year-over-year, in Q3 and Q4, price will more than offset that.

Matthew DeYoe
Analyst, BofA Securities, Inc.

Q

Okay. [ph] Tim, (00:36:20) but you've mentioned that revenues will be kind of consistent with 2019, 2018. Was that a volume comment, or is this kind of consistent with what you'd expect price to do between now and then as well?

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John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc
A

No, that was a volume comment.

Matthew DeYoe
Analyst, BofA Securities, Inc.
Q

Okay.

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc
A

Again, I think at this point, and I think we've said in the prepared comments, even in Q3, although we're expecting lower volumes, price would more than offset the downturn, actually helping our revenue.

Matthew DeYoe
Analyst, BofA Securities, Inc.
Q

Yes. [indiscernible] (00:36:50)

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc
A

And to be very clear, the demand is very strong at this particular stage and that's why we think that moving into the – into next year with less volume, Atlas Campaspe becomes more and more important as we replace some of the mining assets that we have. So now the money that we're spending to reinvest in the business throughout the cycle is going to help us. But it's going to take some time to get some of that capacity up and running.

Matthew DeYoe
Analyst, BofA Securities, Inc.
Q

Understood. Thank you.

Operator: The next question is from Hassan Ahmed of Alembic Global. Please go ahead.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC
Q

Good meaning, guys. I wanted to revisit a question around ore supply or supply demand fundamentals over there. And, again, understood on the near-term side effects. We've seen issues in Sierra Leone. We've seen some issues in South Africa as well. But if I take a look at [indiscernible] (00:37:48), obviously, it's been an industry, which has been undersupplied, underinvested for a while, right. And now here we are with the issue in Sierra Leone, the issue in South Africa. How are you guys thinking about supply demand fundamentals, call it, near to medium term in ore? And on a relative basis, in terms of availability, how are you guys thinking about the availability and supply demand fundamentals of low-grade versus high-grade ore?

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc
A

So, Hassan, I'll try to give you a little bit more color on this. Look, we feel that we're doing our part in the sense that we announced our Atlas Campaspe mine almost a year ago and we're going to start that operation next year. And that would allow us to maintain our 85% vertically integrated position, even if we're increasing our pigment

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production to grow with our customers. So that's [ph] all part (00:38:58), if you want. And look, we have other project in our pipeline that we're looking at to continue to maintain that position and even increase our vertical position, if we need to. We kind of like to be slightly short, because that allow us to be on the market and buy from the supplier, have a good understanding of what happened, and that's what we have done to make sure that we would have the material that we need.

That being said, you're right, when you said that the industry probably underinvest in recent year, because the price didn't justify to open new mine and to invest in a complex upgrading facility. And look, even if you talk about a mine for chloride or a mine for sulfate, the costs are the same. The difference is really just the type of ore that you have in the ground. But I mean, it's not cheaper to open a sulfate ilmenite mine than to open a chloride ilmenite mine. It just depends on the resource. And I guess the chloride resource out of the ground are more scarce or they are rare, and that's why you need upgrading facility like a smelter, like what we have in South Africa or [ph] an SR plants (00:40:37) like we have in Australia, or our future Jazan operation.

So, because those assets allow you to take an ore that is not really compatible to the chloride process and make it compatible as the feed at an economical value for the chloride process. So, that's what we're doing. So, I hope that that gives some color, but we see that as positive for the industry, because in the coming year, I think that with limit pigment production is not building new pigment plant, it's going to be opening new mine to feed those pigment plant. And I think that's where when people panic about China overfloating the market. China cannot do that, because they don't have the mine to feed their chloride expansion. So that's where the vertical integration of Tronox will really play in our favor.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC

Q

Understood. Understood. Very clear. And just sticking to the theme of raw materials, again and again on the call, you guys talked about chlorine supply kind of being an issue in the second quarter and maybe into the third quarter as well. But it seems that, as I sort of hear some of the commentary coming out of one of the biggest sort of chlorine producers in North America, in particular, that that's going to be an issue that's going to be here for a while, right. How are you guys going to react or deal with this sort of reduced availability, call it, of chlorine particularly in the North American market? And how do you think the industry deals with that?

And I guess where I'm going with this question is, everyone's talking about us being in the sort of early innings of an upcycle within the TiO2 sort of cycle. Cash flows are improving and the like. Do – I mean, is it fair to assume that maybe you guys or the industry start thinking about building some of your chlorine capacity? I mean, is that something that you guys are thinking about?

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Yeah. So, Hassan, this is John Romano. We do have – outside of North America, we have a lot of purpose-built chlorine plants. So clearly, that's something we continue to evaluate. It's not just chlorine, although that's been kind of the focal point here recently. There's been other issues with nitrogen and oxygen and other plants. I mean, there are a lot of issues in the industry right now.

With regards to chlorine, coupled with looking at opportunities where we might actually evaluate building our own chlorine facility, we're also looking at our ability to continue to work with other suppliers. Our supply chain team has a good plan in place as we move into 2022 that will continue to support our growth not only in the US, but globally.

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Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc
A

Yeah. And Hassan, just to link it with the feedstock, Tronox having nine pigment plant and full control of its feedstock. We're, obviously, sending [ph] lower ore (00:43:54) to place in the world where we have extra chlorine and we try to keep the high grade feedstock for our Hamilton plant in the US, because, I mean, we're facing that reality of the chlorine, I mean, so – but we have kind of rearranged our feedstock to deal with that.

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc
A

And if you think just – we've referenced again 5% to 10% decrease in Q3 prior to Q2, a lot of that has to do with – what JF just said. We have been able to manage the chlorine issue by moving higher grade feedstock to other facilities to have a higher head grade, therefore, needing less chlorine. Some of the issues that happened recently are now being a bit exacerbated by transportation issues in getting that ore there quickly. So it's not a long-term issue for us. It's more of a short term one. Nonetheless, it's an issue that we're dealing with.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC
Q

Very helpful, guys. Thank you so much.

Operator: The next question is from Duffy Fischer of Barclays. Please go ahead.

Duffy Fischer
Analyst, Barclays Capital, Inc.
Q

Yeah. Good morning, fellas. Question just around the theoretical volume increase for next year. So if we assume that demand stays very strong and we assume that a lot of these logistical issues go away and your operations run as you would plan, how much more TiO2 would you be able to produce and sell next year versus what the plan looks like midpoint for this year?

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc
A

Well, I mean, we assume, Duffy, that the TiO2 will grow like GDP and we are aligning ourselves with customers that are growing slightly faster than the market. But, I mean, we don't expect the type of growth that we've experienced from Q1 to Q2 and going forward to last. So, I mean, we don't have plants of growth of double-digit, but we have plant of grow of mid-single-digit growth for next year.

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc
A

So, clearly, Yanbu is a big part of that, how we're going to support that growth with production, and we've talked about the synergies there, those are going to continue into 2022. We continue to work with our operational excellence programs and, again, our vertical integration will allow us to continue to support their growth at our plants. We're not looking at any specific expansions, but continuing to debottleneck our plants. And we believe that we'll be able to continue to do that and capture the growth, at least, at our percentage share and probably more.

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Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Okay. Maybe I missed it, so I wasn't talking about kind of structural increases or like the long-term 10-year average growth. Most of it I was talking about is just physical operations where it seems like, obviously, you had – Stallingborough had an issue this year, right. I mean, theoretically, that doesn't happen next year. So just on a like-on-like basis, 2021 into 2022, if we assume some of the supply issues, physically, how much more, I mean – or maybe a different way to ask it, the midpoint of your base case this year through the end of the year, what production level is that relative to what you would call your theoretical nameplate this year? I mean, I'm just trying to understand, is it a 75,000 kt bump, is it a 125,000 kt, roughly how much more would we have to sell next year than this year?

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Well, one color that I want to give, Duffy, is, we are increasing our production. So from 2021 to 2022, we'll improve significantly the amount of ton that we'll produce. But you have to realize that we started 2021 with inventory and at the moment, we have absolutely no inventory, well, we're below seasonal norm, as John said. So we need to rebuild that inventory.

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

And so – and when we think – so, I guess, generically, though, we try to run at the 95% utilization rate. You can't get to 100% on a regular basis. We have got nine plants. There's going to be issues. All that being said, we'd hoped that we could probably get another maybe 40,000 tons to 50,000 tons out next year. But to JF's point, there has to be an element of that, that goes back to rebuilding inventory, because we're not at the sustainable level at this stage.

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

And we don't see that negatively, because, obviously, we're not the only one facing that reality. So it would just keep the markets from going to building huge inventory and then create another cycle. Instead, it will stabilize the situation and that's positive we found.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Very fair. And then, with things being so tight and with you guys kind of having the broadest plant footprint globally, have you pushed more people or more people asked this year to move into kind of longer term arrangements where maybe there's more sustainability or less volatility in that business over a longer period of time?

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Yeah. Duffy, I would say the answer to that question is yes, but I differentiate that from longer-term agreements. Yes, we haven't – clearly, there's been a lot of interest in margin stability as the market starts to recover. And we don't typically provide details on contract splits. But what we can say is that we have a very good balance of agreements that will allow us to continue to capture price as we move into the second half and longer term agreement commitments, I think, from some of the issues that have happened, because, quite frankly, China has

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clearly added some capacity, but they're, I would say, a bit erratic sometimes. So in some of those areas, we have picked up longer-term agreements moving into the balance of this year and into next.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Great. Thank you, guys.

Operator: The next question is from Vincent Andrews of Morgan Stanley. Please go ahead.

Vincent Stephen Andrews
Analyst, Morgan Stanley & Co. LLC

Q

Thank you, and good morning. A question on pricing and your contracts. Maybe not be the case for you, but I believe it's the case for one of your competitors that also does the value stabilization contracts that there's a linkage on price to PPI. And, obviously, we're seeing a lot of PPI inflation out there. And so my question is, should we assume that your contracts will see a positive price movement in line with something close to where PPI is going?

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Yeah. So just to be clear, our contracts, where you're referring to as value stability agreements, are not anything like that. We don't have anything that's tied to PPI. They're individual agreements that have capability of price to move up. Our price moved up 5% in the quarter. As we noted, we expect to get price strength moving into the third quarter. And we have the ability to adjust those contracts as we do non-margin stability agreements. Again, not providing the split, we still feel we've got a good balance between margin stability and regular long-term agreements, which will allow us to continue to capture price.

Vincent Stephen Andrews
Analyst, Morgan Stanley & Co. LLC

Q

Okay. And then as a follow-up on the volume and shipping situation, you're going to be down 5% to 10% sequentially. We've heard from some of your – presumably some of your customers during this reporting season already and in paint and plastics that they've had issues getting other raw materials, which has caused them to produce less themselves. So, are those folks still taking all the TiO2 they want, because they know later on they're going to make up their production, or are they folks that won't – that will be part of that 5% to 10% reduction in shipments on a go-forward basis? I'm just trying to figure out who's not getting your product, particularly those that are having their own production problems?

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Yeah. So the 5% to 10% reduction is going to be spread evenly around where we're having the issues. So depending upon where we're having a shortage, we have to look at contracts based on agreements and allocate accordingly. So I would say that those decreases would be split. It's not our opinion at this stage that there's any development of fee – raw materials being built up in the chain. We think that not only are inventories low, but our customers inventories of TiO2 are low as well.

Vincent Stephen Andrews
Analyst, Morgan Stanley & Co. LLC

Q

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Okay. Thanks very much.

Operator: [Operator Instructions] The next question is from Jeff Zekauskas of JPMorgan. Please go ahead.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Thanks very much. I think that the currency translation hit to your EBITDA was $83 million in the first half. If currencies don't change, what would be the currency penalty to EBITDA for 2021? And when you're hedges – if currency stayed the same and your hedges come off next year, what's the currency penalty to EBITDA in 2022 in rough terms?

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

A

Hey. Jeff, it's Tim. The hedge change year-on-year is worth about $30 million to $35 million decline next year, of a headwind next year.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

And what's the penalty for this year, as if currencies stay where they are roughly?

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

A

If currencies stay where they are roughly for the rest of the year, there is no penalty on our hedges, because our hedges were locked in at $0.59 back in 2020.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

What I meant to say was, what's the negative currency translation effect in the second half if volumes are more or less the same, prices are more or less the same? Is there a change in the third and fourth quarter?

Timothy Craig Carlson
Senior Vice President & Chief Financial Officer, Tronox Holdings Plc

A

It will still be a headwind, just given the Q3 to Q4 changes. And let me see if I can grab that quickly. I think it's around $50 million, if I remember correctly, in the back half.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Okay. All right. Thanks for that. Your prices went up 5% sequentially. If you think about the US and you think about Europe, I take it they were smaller in the US and larger in Europe to get to that 5%, is that correct?

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Jeff, this is John Romano. I would say that our price increases in the quarter were evenly split across the regions.

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Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Meaning that they were the same percentage change, both in the United States and in Europe?

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

In the same ballpark, yes.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Okay. Have you fully committed to buying the Jazan Slagger, and can you remind us what the net cost of buying that is?

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

So, Jeff, the – so the smelter was out of the original deal, but at the time, we said if the Slagger can demonstrate that it operate and meet the level of production that was guaranteed by the supplier, Metso Outotec, we would acquire it. So basically, the arrangement is done that – look, we at Tronox had some doubt about the technology and we wanted to make sure that if we get the asset, it would be value accretive for the business.

So that's why we say we have the advantage that if successful, we'll get a successful smelter to add to the Tronox portfolio. But if it doesn't work, we're not – we don't have the problem of what to do next with the smelter. So that's how the arrangement is done basically. Look, obviously, while the smelter is being [ph] cashed (00:56:24) and produce material, we will handle that material. So we will buy the slag and buy the pig iron from Tasnee and we will use it in our plant. But it needs to reach a certain level of operation and success for us to acquire the asset.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Right. But how much are you – would you pay for the asset? I think you might have loaned them some money in the past. How do you net it out as to what the cash, the net cash outflow inclusive of debt would be, what if you purchased it, what would that price be?

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

If the Slagger achieves sustainable operations, we assume $322 million of debt in the $125 million that we've already committed. So, $447 million.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

$447 million. And all things being equal, that would happen this year?

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

No, that happens sustainable operations, which is probably a year out from startup, so next – Q4 next year.

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Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Okay. Great. Thank you so much.

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Thanks, Jeff.

Operator: The next question is from Roger Spitz of Bank of America. Please go ahead.

Roger Spitz
Analyst, BofA Securities, Inc.

Q

Thank you very much. I'm not sure I heard correctly earlier. Did you say that you could consider building a core [ph] alkali (00:57:49) plant to address supply issues should traditional chlorine suppliers let not to supply you? And did you say that you're actually currently producing chlorine somewhere outside the US?

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Yes. So what we said was that we're always evaluating that. Building chloride or chlorine facilities for any of our sites is something that we've evaluated over time. We have purpose-built chlorine facilities at some of our locations and we buy merchant chlorine at others. So it's always something that we're looking at and have been evaluating on a year-by-year basis.

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

But, Roger, Yanbu, for example, which is a copycat of Hamilton, has its own chlorine facility. We own that facility and we produce our own chlorine in KSA. And look, as John said, there was never a plant in the US, but depending on what happen with the market, we're going to look at it. If it's a good business case for us, we can do it. It's not something that is rocket science.

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

And it's something we have in our facility in Kwinana as well, another purpose-built plant. So it's just something that we continue to evaluate based on where we are in the cycle.

Roger Spitz
Analyst, BofA Securities, Inc.

Q

Got it. Are you selling caustic soda into the market?

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

We do.

Roger Spitz
Analyst, BofA Securities, Inc.

Q

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Okay. Great. All right. And I guess just last one, we will get [ph] it at the Q – 10-Q (00:59:19), but what was the $135 million of debt repayment in Q2 2021 and the $70 million of debt that was repaid in July 2021? I mean, which item? I'm assuming it was a term loan, maybe it was a Standard Bank [ph] part (00:59:34)?

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc
A

Yeah, Roger, primarily, the term loan. There's a little bit in the Standard Bank in South Africa, but primarily term loan in the US.

Roger Spitz
Analyst, BofA Securities, Inc.
Q

Right. Thank you very much.

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc
A

Thank you, Roger.

Operator: The next question is from Travis Edwards of Goldman Sachs. Please go ahead.

Travis Edwards
Analyst, Goldman Sachs & Co. LLC
Q

Hi. Good morning. Going a little bit different direction, I just had a question on the sustainability side. Just as you've highlighted various targets for emission, waste reduction, have you outlined that the cost is due to achieving those targets? Are those investments material enough that we should expect them to show up in cash flow items in the coming years and if so, how much and where?

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc
A

So, very good question, Travis. And yes, look, as part of our five-year plan, we always predict how much capital we will need to invest and where and it's linked into that number that we made public. So, we talked about $300 to $325 for this year. And, obviously, there is sustainable investment and waste reduction as part of that capital investment for next year. We had talked about $350 million of capital as part of that capital investment. There is an ESG component that is always built year-on-year on that capital deployment.

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc
A

Getting to our 2030 to ultimately 2050 goals, clearly, there is more work to be done on determining what that capital spend is going to be. Right now we're working on a five-year plan, which we've just finalized, but getting out into 2030 and beyond, there's still some work to do there. But clear projects identified to actually reach those targets, at least, at 2030.

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc
A

And I'd add to that, Travis, that some of those projects are value creation. I mean, they're reducing our greenhouse gas, but they also are our good business project.

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John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

They'll help reduce costs.

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Yeah.

Travis Edwards
Analyst, Goldman Sachs & Co. LLC

Q

Got it. Thanks for the time. Best of luck this quarter.

John D. Romano
Co-Chief Executive Officer & Director, Tronox Holdings Plc

A

Thank you.

Operator: This concludes our question-and-answer session. I would like to turn the conference back over to Mr. Turgeon for closing remarks.

Jean-François Turgeon
Co-Chief Executive Officer & Director, Tronox Holdings Plc

Thank you, everyone. And, look, this complete what we had prepared for you. I just want to reinforce a big thank you to all of our employees and all the people who make those results possible. So thank you, everyone, and thank you for your support and interest in Tronox.

Operator: The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.

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