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Tronox Holdings Plc (TROX)

Q1 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Hello, everyone, and welcome to Tronox Holdings First Quarter 2022 Earnings Call. My name is Juan and I will be coordinating your call today. At this time, all participants are in listen-only mode. [Operator Instructions]

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

Jennifer Guenther

Vice President-Investor Relations, Tronox Holdings Plc

Thank you and welcome to our first quarter 2022 conference call and webcast. Turning to slide 2 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 the presentation on our website at investor.tronox.com.

Moving to slide 3. A friendly 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

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represents our best judgment based on what we know today. However, actual results may vary based on these 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. Additionally, please note that all financial comparisons made during the call are on a year-over-year basis, unless otherwise noted.

Moving to slide 4. 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. I'll start this morning by setting the stage with a quick overview of Tronox. We're the world's largest vertically integrated TiO2 producer, with nine pigment plants, six mines, and five upgrading facilities across six continents. Our 2021 revenue totaled $3.6 billion, which was fairly evenly distributed across the Americas, Europe, Middle East and Africa, and Asia Pacific. Our 1.1 million tons of pigment capacity supports our well-balanced base of approximately 1,200 global customers.

Our vertically integrated business model supplies approximately 85% of our internal feedstock needs, and this ensures consistent and secure supply for our customers. In addition to TiO2, we also generate significant value as the world's second largest producer of zircon, with approximately 297,000 tons of capacity. We are proud of the organization we've created following the transformative Cristal acquisition three years ago and the value we have and will continue to generate for our stakeholders.

Before turning to the first quarter highlights, I want to address the crisis in the Ukraine. Our financial exposure is minimal, with less than 1% of our total revenue from Russia and Ukraine combined in 2021. But more importantly, our hearts go out to those impacted by the conflict, and we offer our support to those who are affected.

Now, let's turn to slide 5 to review our first quarter results. Tronox delivered solid first quarter results and continued to serve our customers against a backdrop of increasing costs, higher commodity prices, logistics constraints, and extended downtime at our Stallingborough, UK pigment facility, which has since been resolved. It is a testament to the dedication of our employees that we've continued to deliver results in line with our expectations while overcoming these ongoing challenges, so we thank the Tronox team for their commitment.

Despite the challenging operating environment, we delivered adjusted EBITDA of $240 million within our guided range. In the quarter, we invested $103 million in key capital projects. This included newTRON, our project to digitally transform our global portfolio, which is expected to generate savings of $150 to $200 per ton on a run rate basis by the end of 2023. We also invested in our mining extensions in South Africa and the Atlas Campaspe mine in Eastern Australia, and JF will review these investments in more detail later in the call.

We generated $86 million in free cash flow from our strengthened and differentiated business model. And on April 4, we closed the refinancing transaction, enabling the achievement of our previously stated $2.5 billion gross debt target ahead of our 2023 goal, while also reducing cash interest payments, extending maturities and increasing pre payable debt. We repurchased 1.4 million shares of our stock in the quarter totaling $25 million, and we have $275 million remaining under the board-approved share repurchase program through February of 2024.

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Finally, we announced a significant renewable energy project in South Africa, which we will now review on slide 6. In March, we announced that we entered into a long-term power purchase agreement with South African independent power producer SOLA Group to provide 200 megawatts of solar power to our mines and smelters in South Africa. This project is expected to provide approximately 40% of Tronox' South African electricity needs and lower our worldwide Scope 1 and 2 emissions by approximately 13%. We anticipate the project should be fully implemented by the fourth quarter of 2023.

This project is only one example of numerous initiatives and investments we are pursuing to meet our publicly announced goal to align with the global warming scenario below 2 degrees Celsius and achieve net zero greenhouse gas emissions by 2050. More information about our sustainability initiatives will be available in our 2021 Sustainability Report expected to be published by mid-year, which we will expand on further at our Investor Day on June 16.

Turning to slide 7, I will briefly review our first quarter financial highlights in more detail. Revenue of $965 million represented an 8% increase versus the prior year, driven by higher TiO2 and pig iron revenue. Income from operations includes the onetime settlement fee totaling $85 million, representing the break fee and related negotiated interest. Our effective tax rate in the quarter was 53% due to the settlement and tax rate changes in foreign tax jurisdictions. Without these items, our normalized Q1 effective tax rate would have been 25.5%.

Our GAAP diluted earnings per share was $0.10 and our adjusted diluted earnings per share was $0.60, an increase of 40% year-over-year. Adjusted EBITDA of $240 million represented a 7% increase. Our margin decreased 40 basis points to 24.9%, impacted by unfavorable product mix related to zircon, logistics constraints, higher commodity costs and the extended downtime in Stallingborough. Free cash flow of $86 million increased 12%.

Now, moving to slide 8, I will review our commercial performance in more detail. Our first quarter results were in line with our expectation, with our team continuing to manage strong customer demand while navigating a number of macro challenges, including continued input cost inflation and supply chain disruptions. Total revenue increased versus the prior year driven by TiO2 and pig iron sales, partially offset by lower zircon revenue and currency headwinds.

Revenue from TiO2 sales was $773 million, an increase of 11%, driven by a 20% increase in average selling prices on a local currency basis or an 18% increase on a US dollar basis, partially offset by a 6% decrease in volumes. Sequentially, TiO2 volumes increased 9%, at the high end of our previously communicated range, driven by higher volumes across all regions. While average selling prices increased 6% on both the local currency and a US dollar basis.

Although we continue to monitor the macro situation, TiO2 demand remains solid. TiO2 supply-demand balance remains tight due to continued strong demand, while inventories remain low and delivery times continue to be extended by shipping delays and supply chain disruptions.

Zircon revenue decreased 12% to $108 million, driven by a 38% decrease in volumes, partially offset by a 43% increase in average selling prices. Sequentially, zircon volumes declined 20%, while average selling prices increased 14%. The volume decline on both a year-over-year and a sequential basis are due to higher sales volumes from inventory in the previous quarters as we communicated previously. Revenue from other products was $84 million, representing a 17% increase, primarily due to higher pig iron volumes and higher average selling prices.

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Our dedicated team of employees are working to ensure we earn the right to be the supplier of choice for our customers. We have substantially increased the number of long-term volume contracts with our global customer base, securing our volumes well beyond 2022. Our demand outlook for the year remains solid as TiO2 market tightness persists, while inventories remain below seasonally normal levels and similarly positive trends continue in the zircon and pig iron markets.

While we experienced unexpected challenges this quarter, Tronox remains well positioned to continue to overcome these adverse conditions. With our enterprise optimization model, we are able to maximize our global footprint and we are investing to sustain our competitive advantage. We are focused on executing against our strategy to deliver safe, quality, low cost, sustainable tons for our customers.

Our expectation for TiO2 market demand growth in line with GDP in 2022 remains unchanged. This will be supported by the need to replenish inventory throughout our customer supply chain channels. Distribution remains extremely challenged headed into the second quarter. And considering this as well as low inventory levels, we anticipate TiO2 volumes to be in line with the first quarter of 2022 levels. We expect TiO2 pricing to continue to increase, reflecting strong market demand and commodity price increases.

Zircon sales volumes are expected to increase slightly sequentially, benefiting from some orders that rolled over from the first quarter but will remain more in line with production levels for the remainder of the year. Zircon pricing improvement in the second quarter is expected to more than offset the volume headwind on an EBITDA basis, and we expect this trend to continue for the full year.

I will 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, and good morning, everyone. Moving to slide 9, our adjusted EBITDA growth of 7% to $240 million was driven by higher pricing across all products and favorable exchange rate, partially offset by higher cost to serve our customer, including increased commodity costs, lower volume and unfavorable product mix, primarily due to zircon. Freight rate remained elevated, while demurrage expense in South Africa drove most of the incremental costs due to port congestion.

We incurred higher mining costs, including raw material and natural gas, driving higher cost per ton. Favorable exchange rate impacts on cost of goods sold more than offset unfavorable exchange rate impact to revenue, resulting in a net positive impact overall. As a reference, our TiO2 manufacturing Q1 costs per ton has increased nearly 20% compared to the prior year, with the largest increase from natural gas, sulfuric acid, chlorine, coke and electricity. However, we are confident we can continue to improve margins due to the continued solid market demand, favorable feedstock position, and our ability to implement pricing across all product line.

Turning to slide 10, I will review how executing against our strategy will enable us to continue differentiating our business and meet our financial target. We remain committed to executing our strategy to become an advantaged vertically integrated global TiO2 leader. Foundational to our strategy is to produce low cost, high quality pigment for our customer and sustaining our integrated global footprint to ensure security of supply for our customer and optimize our global footprint.

Our mining and upgrading facilities continue to run at high operating rate at a time when feedstock are critical. This, combined with our integrated planning capability, will allow us to increase production and produce up to

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40,000 ton of additional TiO2 this year versus 2021. Our effort and capital expenditure will continue to be dedicated to pursuing our strategic objective through projects like newTRON and our mining projects. Our strategy drive our ability to leverage our unique portfolio to optimize our assets and secure our position as the most adaptable, resilient TiO2 industry leader, allowing us to continue to deliver industry leading financial performance.

Turning to slide 11, I will now review our key capital projects that will unlock future value creation from our asset. If we look at our major strategic capital projects, they can be divided in two categories. The first being grow and cost saving capital; and the second as vertical integration related capital. newTRON fall under the first bucket. newTRON is our strategic multi-year global digital transformation project.

The second bucket relate to sustaining our vertical integration. Our business model is our source of differentiation, and investing in our mine is critical in sustaining that advantage. Atlas Campaspe represents the next phase of our mining plant in Australia, and the Namakwa and Fairbreeze extension represent the next phase in South Africa. Atlas Campaspe, as a reminder, is expected to come online in the second half of 2022 to replace the Snapper/Ginkgo mine as they reach end of life. These tenements are abundant in natural rutile, high value zircon, and high grade ilmenite, suitable for synthetic rutile, slag processing or direct pigment production.

The investment in Atlas Campaspe will also put in place the infrastructure for this new mining area, where we have other important future mining resource in our portfolio. The Namakwa and Fairbreeze extension will ensure sustained production beginning in 2024 and 2025, respectively, and extend the mine life in South Africa beyond 2035. In total, we anticipate investing $150 million to $175 million in 2022 across our mining projects, which will sustain Tronox 85% internalization of feedstock, supporting over $300 per ton saving relative to average high grade feedstock market price.

Turning to slide 12, I would like to review the various elements of newTRON and remind investor of why this project is so transformational for Tronox. newTRON will transform our business, 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, efficient maintenance spend, enhanced automation and throughput, and standardized process.

The new vendor management system put in place allows improved handling of catalog purchase order and invoice, enabling the optimization of our procurement activity globally and result in $20 million in saving in 2021. As an example of enhanced automation, we continue to see significant stabilization in our chlorinator at Hamilton as a result of program being trialed today. This has increased the uptime of the plant and has also led to reduced coke consumption. We are very excited about this initial result and what this mean for Tronox future and for our shareholder.

Efficient maintenance mean our plants' employee have improved capabilities to plan and schedule maintenance before equipment failures to optimize production schedule and downtime. Standardization across our function will lead to improved visibility and a streamlined order to delivery process, enabling better data visibility and decision making. It also facilitate the transfer of best practice from one site to the others. The anticipated $150 to $200 per ton saving by the end of 2023 will come from all four of these area with clearly identified benefit, which we look forward to reviewing in further detail at our Investor Day.

Finally, I'd like to provide a brief update on our slagging operation in Jazan. The first slag was tapped at the end of November. The ramp up is progressing according to plan. We are continuing to utilize the slag produced at Jazan at our Yanbu facility. At a time where tight feedstock condition are impacting the TiO2 industry, a fully operational Jazan would make Tronox more competitive by strengthening our vertical integration strategy. We expect the site

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to continue to ramp up from here forward, ensuring a safe and sustainable operation. We will keep the market update on the progress of the site.

I will now turn the call over to Tim Carlson to cover our balance sheet and outlook. Tim?

Timothy Craig Carlson

Chief Financial Officer & Senior Vice President, Tronox Holdings Plc

Thank you, JF. On slide 13, we provide an overview of our financial position, liquidity and capital resources. We ended the first quarter with net leverage of 2.4 times, within our previously stated targeted range of 2 times to 3 times. While we ended the quarter with $2.6 billion in debt, the refinancing transaction announced in the first quarter and completed early in the second quarter enabled us to obtain our previously communicated $2.5 billion total debt target as announced in early April, and extended maturities while lowering interest costs.

Total available liquidity as of March 31 was $758 million, including $292 million cash and cash equivalents, which is well-distributed across our global operations. Capital expenditures totaled $103 million in the first quarter, with the increase driven by the key projects JF outlined. Depreciation, depletion and amortization expense was $68 million. Our free cash flow totaled $86 million due to our strong cash earnings.

We returned $25 million to shareholders in the first quarter in the form of share buybacks. We repurchased approximately 1.4 million shares. There is $275 million remaining through February 2024 under the share repurchase program authorized by the board in November 2021. We increased our dividend to $0.50 per share beginning with the first quarter dividend, which was paid out at the beginning of the second quarter.

Turning to slide 14 and I'd like to share our outlook. As John mentioned, we anticipate demand trends to remain solid for both TiO2 and zircon amidst the backdrop of continued supply chain disruptions, inflationary pressures, including elevated commodity prices, and ongoing geopolitical instability in the Ukraine. We do not expect inflationary cost pressures to significantly abate. However, the planned increase in production through the end of the year will enable improved fixed cost absorption and help lower our cost per ton.

We expect second quarter adjusted EBITDA to be $265 million to $280 million. These expectations are driven by sequential increases in pricing, zircon volumes and production rates, and partially offset by headwinds from commodity cost inflation and logistic constraints. For the full year 2022, our outlook for adjusted EBITDA and adjusted diluted EPS remains unchanged.

We have updated our cash to use assumptions as follows. We increased working capital expenditures by $25 million to a use of $100 million to $150 million of cash, as well as begin to rebuild inventories to more normalized levels and Jazan continues to produce slag. We lowered net cash interest expense to $110 million to $120 million, reflecting more favorable interest rates from the refinancing transaction. We increased cash taxes to $50 million to $60 million to reflect updated assumptions. And we increased capital expenditures to $400 million to $425 million to reflect higher vertical integration investments, primarily for Atlas Campaspe.

Based upon these updated cash assumptions as well as the onetime settlement costs, we have updated our free cash flow outlook for the year to be a minimum of $265 million. These represent our best estimates based upon our current market outlook. We continue to see significant runway ahead and expect to see earnings expansion, driven by growing the top line, reducing our cost per ton through high return capital projects, remaining focused on disciplined expense management, and leveraging our tax attributes.

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Turning to slide 15, I'll briefly review capital allocation. We expect to continue to prioritize capital expenditures with the projects we have reviewed, driving significant value for Tronox both today and in the near future. With remaining free cash flow, we anticipate to service the dividend, continue to reduce debt levels and opportunistically repurchase shares.

Our forecast to 2022 capital expenditures breakdown as follows. Maintenance and safety capital of $125 million, investments and sustaining our vertical integration of $150 million to $175 million, growth in cost reduction projects of $100 million, and other small strategic projects of $25 million. We estimate our annual returns on total capital expenditures inclusive of maintenance and safety capital to be between 25% and 30%.

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

Jean-François Turgeon

Co-Chief Executive Officer & Director, Tronox Holdings Plc

Thank you, Tim. Turning to slide 16, this page outline our key focus area for 2022, which remain unchanged from our end of year earnings call. As we wrap up today's prepared remark, I want to take a moment to acknowledge the outstanding position Tronox is and due to the commitment by your organization throughout the last several year. This would not be possible without our 6,500 global employees. So, thank you to everyone for your ongoing effort. With our portfolio of assets and market position, we are confident in our ability to capitalize on our momentum, execute against our objective, and deliver on our commitment to our stakeholder.

Turning to slide 17, we are planning to hold our second Investor Day on June 16 and look forward to presenting more detail on our long term strategy, key operational and financial aspect of the business, ESG related practice, and more. We continue to navigate the current macroeconomic challenge while transforming our company, which will ensure our future remain bright.

Conclude our prepared remark. With that, I'd like to turn the call over for question. So, Juan?

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QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] And the first question comes from the line of Josh Spector from UBS. Please, Josh, your line is now open.

Joshua Spector
Analyst, UBS Securities LLC

Q

Yeah, hi. Thanks for taking my question. I guess just first on your TiO2 volume outlook, the flattish quarter-over-quarter, can you comment on what's the biggest limiting factor there? And to your comments about increasing production this year, do you expect to buck normal seasonal trends later this year and increase sales volumes? Or is that a little bit more at risk and more of a 2023 benefit?

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

A

Yeah. Thanks, Josh. We had in the first quarter – we – as we stated on the call, our volumes were at the top end of our range, up about 9%, and the reality is going into the first quarter our inventories were below seasonal norms and our team did a great job of getting our orders out in the first quarter.

When you think about where we are going into Q2, our inventories again below seasonal norms, we referenced the [ph] Stall (00:28:33) outage, which had an impact on our inventory. So, this is just our ability to try to keep up with the demand. If we look at our order pattern, it's well above what our – we believe that flat number would be and to the extent we have some opportunities to actually get more tons out and address some of the logistics issues, that's – it's possible we could be above that. But right now, it looks more flat and it's not related to demand, it's related to our ability to meet that demand in the quarter.

And as far as – when we think about the second half of your question around volumes, we did say we're going to make 40,000 tons of additional volume and I would say that the majority of that volume will start to come in the latter part of this quarter and moving into Q3 and Q4. So, we talked about working capital on the call. We still need to build some inventory to make sure we can meet the demand of our customers. So, we're still confident in our outlook and that volume increase moving into the second half of the year will help us to meet our customer demand and our service levels.

Joshua Spector
Analyst, UBS Securities LLC

Q

Thanks. That's helpful. And just on the co-product side, I mean, a lot of discussion about zircon and obviously that's very important for you guys. But curious if you could comment on pig iron. Prices moved up in the quarter. I'm not really sure what you're seeing. Demand -wise there, there's still kind of a frenzy on that side. And I'm really trying to think about, is that an incremental benefit sequentially about the flow through of higher pricing there or is that not really baked into your outlook at this point?

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

A

So, Josh, it's JF here. Look, pig iron, as you know, is always linked to iron ore and obviously the conflict in Russia and Ukraine at the moment has limit the production of pig iron coming out of those two country, and we have seen price of pig iron move up significantly. Look, we haven't assumed that that would remain the case. Obviously, we

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don't know what will happen with the conflict. So, we've been cautious in our assumption for what will happen with price, but we're not influencing the price of pig iron. I mean, we're selling everything we produce and we benefit from the bigger market in relation to that.

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

A

And we're kind of the tail on that dog. But I mean, suffice it to say the prices have moved. And when we think about the second quarter, most of those contracts are already locked in. So there is – that higher pricing is factored into Q2. But to JF's point, in the back half of the year, that's probably upside if the conflict continues.

Joshua Spector
Analyst, UBS Securities LLC

Q

Got it. Thank you.

Operator: Thank you. Our next question comes from the line of John McNulty from BMO Capital Market (sic) [Markets] (00:31:33). Please, John, your line is now open.

John McNulty
Analyst, BMO Capital Markets Corp.

Q

Yeah. Thanks for taking my questions. So, I guess, first one would just be on Europe. Obviously, the energy outlook has gotten noticeably more difficult. I guess, can you help us to understand, just given you've got a reasonable amount of exposure in Europe, how you balance the energy side versus the pricing and what looks to be still solid demand? Can you get through what you need to in terms of pricing, do you think, just given the kind of fragile economic backdrop there? So, how should we think about the European assets?

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

A

Hey, John. It's Tim. Thanks for the question. As it relates to energy in Europe, our largest exposure is in Stallingborough given natural gas in the Netherlands, where it's part of an industrial park and we've got forward contracts in place for the year [indiscernible] (00:32:29) it's much smaller in France and a very similar approach. We are hedged and have forwards in place for Q2 to about 67% of our exposure, and our forecast is pretty much where the current market prices are today just given the recent uptick over the last week. We're currently forecasting at that level. So, not a lot of exposure.

As it relates to our current forecast for the rest of the year and just given where we are with pricing right now, price more than offset some of the cost increases, not just the pressures from natural gas but also the pressures that we're seeing in sulfur in Europe – I'm sorry, in China in sulfuric acid and Brazil in really coke and anthracite across the board.

John McNulty
Analyst, BMO Capital Markets Corp.

Q

Got it. Okay. No, that's helpful. And then, you'd mentioned earlier around the cost of production is up about 20% or so. When I think about the offsets, you've got price and you've got newTRON, like, do you expect to get more than enough price to offset that 20% cost of production so that all of the savings for newTRON actually fall to the bottom line? Is that the right way to think about that? Or does some of it actually – some of the newTRON savings

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get eaten up over the next year or two just on the higher cost of production overall? How should we think about that?

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

Hey, John. As it relates to 2022, that 20% increase in cost structures, that cost is primarily focused in process chems and energy utilities. Process chems energy and utilities are actually up 60% year-on-year. As I mentioned, we are able to cover those costs from a price perspective and we do anticipate that the newTRON benefits will help us drop to the bottom line, which is one of the reasons that we remain confident in our full year range.

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

And that's why, John, we expect our margin to continue to improve.

John McNulty
Analyst, BMO Capital Markets Corp.
Q

Got it. Okay. No, that's helpful. Maybe if I can squeeze one last one in. I noticed the CapEx number inched a little bit higher. Is that a function of just general inflationary trends or is that where you're pulling a bit of future CapEx forward into this year?

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

Hey, John, it's the former. It's all inflation.

John McNulty
Analyst, BMO Capital Markets Corp.
Q

Got it. Thanks very much for the color.

Operator: Thank you. Our next question comes from the line of Frank Mitsch from Fermium Research. Please, Frank, your line is now open.

Frank J. Mitsch
Analyst, Fermium Research LLC
Q

Thank you. Thank you so much. I was just curious, what did you size the Stallingborough impact in 1Q or was there any spillover into 2Q?

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

Yeah. Frank, thanks for the question. The [ph] Stall (00:35:29) issue, the unplanned extended outage cost is about $10 million in the first quarter, we're backup and running and obviously that will be a benefit quarter-on-quarter.

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

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And then in Q2, Frank, as we mentioned, there's a little bit of flow through due to the lower inventory. The impact on revenues. No impact on cost.

Frank J. Mitsch
Analyst, Fermium Research LLC
Q

Got you, got you. And speaking of costs and you just detailed what process chemistries have been inflating. Just curious, regarding chlorine, you mentioned chlorine is one of the ones that has been inflating for you. Can you talk about the availability and your ability to source chlorine and what your outlook is there? Obviously, there's a lot going on in that business.

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

Yeah, Frank. Our chlorine footprint is a bit different globally depending upon the plant, but we don't have any problem getting chlorine at this particular stage. So, a couple of quarters ago we were having some issues. But at this stage, availability of chlorine is not something that keeps us up at night.

Frank J. Mitsch
Analyst, Fermium Research LLC
Q

Fantastic. Thanks so much.

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

Thank you.

Operator: Thank you. Our next question comes from the line of David Begleiter from Deutsche Bank. Please, David, your line is now open.

David Begleiter
Analyst, Deutsche Bank Securities, Inc.
Q

Thank you. Good morning. Just on TiO2 pricing, what's embedded in your guidance for both Q2 and the full year?

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

We don't provide clear guidance as far as percentage increases, but what we can say is we would expect to see pricing continue to move up in Q2. We've already locked those numbers in. And in the second half of the year considering the environment we're operating in with low inventories and demand where it is, we would expect to continue to see pricing moving up in the second half as well globally.

David Begleiter
Analyst, Deutsche Bank Securities, Inc.
Q

Understood. And just on – very good. And just on Chinese exports of TiO2, what are you seeing right now and what's your expectation for the back half of the year given current lockdowns over there?

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

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Yeah. Look, so exports were up a little bit from Q4. Q4 was a reasonably high number. But when you think about what's happening in China right now, growth had slowed down a bit and then you had the lockdowns. There's clearly a lot of congestion in the Shanghai Port. So there's a – I'd say a bit of a move to try to move material out. We have a plant in China so we've got a lot of visibility into what's going on in that market. We had some congestion in the Shanghai Port. We've now moved a lot of our shipments to the Ningbo Port and [ph] Xiamen Port (00:38:13) so we're able to get material out. And at this particular stage with demand where it is, I would say those exports and the amount that they increased weren't super surprising for us.

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

A

Yeah. And, David, I would add to John's comment that we have seen the raw material to feed the TiO2 plant in China remained very stable at a high level and some of the commodity like sulfur, for example, even in the last three months since we talked to you where we had said that sulfur price was at record high, well, the price of sulfur in China has increased by 33% more. So, it's that level never seen. And just to give you a feel. To make a ton of TiO2 pigment, you need about 1.2 to 1.3 ton of sulfur, which that sulfur is used to make sulfuric acid. And that's why we see no threat from China related to export.

David Begleiter
Analyst, Deutsche Bank Securities, Inc.

Q

Thank you very much.

Operator: Thank you. Our next question comes from the line of Hassan Ahmed from Alembic Global. Please, Hassan, your line is now open.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC

Q

Good morning, John and JF. I wanted to revisit your comment about the cost inflation, cost per ton sort of being up 20% year-on-year. I mean, you guys being as integrated as you are, I'd imagine that inflationary number is far higher for your competitors. So, just wanted to get a sense of what you're seeing in terms of just the global cost curve. I mean, despite all of these price hikes that we are seeing in TiO2, just broadly, is there a sliver in the marketplace which is not making money right now?

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

A

I think – Hassan, thanks for your question. And I would say, yes, there is a sliver even at the prices that we're operating at now of operators that may not be making money. And to your point, all those costs that impacted us by 20% I wouldn't say are maybe significantly different from our competition. But our ability to vertically integrate and use our material internally with a $30 – about a $300 per ton at a minimum advantage over and above our competitors actually helps us continue to be more competitive, as we noted earlier.

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

A

Yeah. And you would remember, Hassan, that we used to see say that our ore advantage was $200 to $300 per ton. Well, what we see now, it's above $300, as John mentioned. And in some case, it goes even up to $400. And, look, with what's happening with the tight ore market, that advantage should continue to increase.

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Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC

Q

Very helpful. And as a follow up on zircon, just wanted to get a sense of what you guys are seeing in terms of supply-demand over there. Obviously, a bunch of moving parts there as well, China construction being one of them. But more importantly, we'd love to hear what you guys are seeing in terms of the white clay side of things because obviously, as I understand it, Ukraine was a big, big producer of white clay and it seems none of that product is in the market anymore.

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

A

Yeah. Thanks, Hassan. I'll touch on the last one first and from a clay perspective, you have to think about – there was a fair amount of inventory that was already in place at a lot of our customers in the tile manufacturing industry. So, I think early on there was some real concern that the clay that was coming out of the Ukraine was going to have an impact. Fortunately, there was inventory of clay and it's become, I think, a lot easier to reposition clay from other regions of the world into the European region. So that's one thing.

With regards to the market in general, the – if you think about – our estimates for 2021 was that the market was about 1.2 million tons of consumption. And in 2022, it's about 1.1 million – call it equivalent, about the same, 1.2 million tons. We talked about sales were much higher in 2021 because we had a lot of the inventory that we had to service that demand. We believe that the industry has about 160,000 tons less inventory to service the same demand that happened because I mentioned it was flat, which is about 13% of that demand.

So, in summary, you've got lower inventory. Supply chain is, I would say, very depleted. I was just in Europe meeting with some of our zircon users, including some tile manufacturers, and the inventories are visibly depleted. So I think the market has changed very quickly, our order books are fluctuating a bit. we talked a little bit about the mix issue in the first quarter with regards to some of the products aren't all the same so we sold [indiscernible] (00:43:37), which is a little bit lower quality, and zircon. As those volumes fluctuate a little quarter-to-quarter, you'll see some variance in our margin from that particular product segment. But we're very confident about the zircon market between now and the end of the year and moving into 2023.

Hassan I. Ahmed
Analyst, Alembic Global Advisors LLC

Q

Very helpful. Thank you so much.

Operator: Thank you. Our next question comes from the line of Michael Leithead from Barclays. Please, Mike, your line is now open.

Michael Leithead
Analyst, Barclays Capital, Inc.

Q

Great. Thanks. Good morning, guys. First, I just wanted to ask on Jazan. I think last quarter you said you expected the site to achieve sustainable ops in the second half of this year, but I'm not sure I heard that phrasing this quarter. So, is that still the plan or has that moved at all?

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

A

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Mike, it's JF. It's still the plan and Jazan has been performing according to plan. So, we had a very successful start of the year with Jazan. So, it's still expected for the second half of 2022.

Michael Leithead
Analyst, Barclays Capital, Inc.

Q

That's great to hear. And then maybe just second, a little bit broader. You're trading your stock at a quite cheap valuation on absolute or relative terms. And obviously, I think you believe you have a pretty strong medium term outlook with the growth projects and the like. But for whatever reason, it seems like the market isn't really giving you credit for that right now. So, just curious how you guys are thinking about improving that valuation or maybe unlocking more value for shareholders here.

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

A

So maybe, Mike, I could start and let my colleague add. But look, we're planning an Investor Day in June. It's going to be June 16. And obviously, all our investor and people who wants to know more about Tronox are welcome. We'll go in more detail into our strategy, our plan.

I mean, we're investing a lot in our business at the moment to make it better, to lower our costs, to increase our supply to our customer, to be a strong supplier, and I believe that this is what is in our control. And if we continue to act and do that, people will realize that we create value and we're a solid place to invest. So, I think that's our plan and strategy.

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

A

And if you think about where we are today – to answer that question about why we're undervalued, I still think there's a lot of people out there that fear things are going to move back to where they were historically, maybe two, three cycles ago. We spent a lot of time working on our margin stability initiatives. This is the 20th quarter that we've been north of 20% EBITDA margins. I don't think that is something that I would refer to as extremely volatile business profile. Moving to JF's point, higher on margins in fact into the second half of this year. So, I think we have to continue to communicate how we've changed and transformed the business, and we're confident that we can do that.

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

A

And the last item that we'll touch on a bit at Investor Day is really the strength of our vertically integrated business model and the flexibility that we have from our global operations as it relates to a downside scenario. There are just a number of different levers that we can pull to preserve cash and generate even reasonable EBITDA in a downturn.

Michael Leithead
Analyst, Barclays Capital, Inc.

Q

Right. Thanks so much.

Operator: Thank you. Our next question comes from the line of Matthew DeYoe from Bank of America. Please, Matthew, your line is now open.

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Matthew DeYoe
Analyst, BofA Securities, Inc.

Q

Good Morning, everyone. If we think about the shift in FX that we've seen, particularly with the dollar strength, I mean, how do you – how should we think about this as a change to your guidance given some of the EBITDA sensitivities we've talked about in the past?

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

A

Hey, Matt, it'll definitely be a bit of a tailwind for our guidance. We haven't changed our full year guidance, the range. The rand has fluctuated and the Aussie dollar has fluctuated quite a bit over the last couple of months. Word is currently is actually incremental upside to where we think we might come out. But what happens with FX could change tomorrow. So, we're in a very positive place right now as it relates to our business model, and FX could be a headwind or a tailwind depending on what happens in the marketplace.

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

A

That would be one of the elements when we think about the range. That could have a positive impact on the range depending upon where that lands.

Matthew DeYoe
Analyst, BofA Securities, Inc.

Q

All right. Thank you. And then the Namakwa and Fairbreeze expansion sounds like they're going to come on the back of Atlas Campaspe. So, should we expect CapEx to be elevated for some time? I mean, 2022 spending levels, is that consistent with 2023, 2024 or should they move lower because [indiscernible] (00:48:38)? How does this – how do you think this plays out over the next years?

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

A

Look, Matthew, we have flexibility with our capital. We have started those projects now specifically to make sure that we can adjust the capital depending on what we will see in the market. Look, obviously for this year, Atlas Campaspe we're just finishing the construction. So it's a big year and that mine will be in operation. So, no more CapEx in 2023 for Atlas.

We have start Namakwa and Fairbreeze early because we want to spread that CapEx over the year and because we see the market for zircon and for rutile being so strong that those project have huge return on capital invest. So, they're good project to accelerate. But because those mine are already in production and it's not like in the case of Ginkgo and Snapper, we had to move the operation into a different area. We had to move the mine like 100 kilometers away from where we used to mine. In the case of Fairbreeze and Namakwa, those extension are adding capacity to existing mine and you could always pause those and reaccelerate depending on the market condition. So, that's why we said really our base capital as a company is the $100 million to $125 million, which is what I call the maintenance capital. All the excess that we're spending this year is really creating value for our shareholder.

Matthew DeYoe
Analyst, BofA Securities, Inc.

Q

All right. Thank you.

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Operator: Thank you. Our next question comes from the line of Vincent Andrews from Morgan Stanley. Please, Vincent, your line is now open.

Will Tang
Analyst, Morgan Stanley

Q

Hi, guys. This is Will Tang on for Vincent. Thanks for taking my question. I guess just a follow-up on a previous question related to 2022 CapEx. I mean, which cost buckets like labor, equipment, etcetera, are you guys seeing kind of the greatest cost inflation at Atlas? And then to what extent the cost kind of lock in for the rest of the year? And then, I guess, just can you guys also kind of touch on what's driving that $25 million in heightened working capital needs for the year? Is it mainly related to kind of higher inventories from that 40,000 kind of increase in production? Thanks.

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

A

Hey, Will. Thanks for the question. As it related to capital, the inflationary pressures, they're primarily third-party contract costs related to wrapping up our Atlas Campaspe project. That project comes online early in the third quarter, so we don't anticipate significantly more inflationary costs above that.

And as it relates to working capital, we've taken a hard look at our inventory balances globally to make sure we've got sturdy supply for our customers. So there's a bit of a tick up on inventory. As well as just given increased revenues from improved pricing and volumes, it's causing receivables to go up. So, that's a little bit of an increase and as we mentioned earlier, the Jazan facility continues to produce slag so we'll have a bit of slag inventory as well in that balance. But at the higher end of the range, we'll be at the higher end of the working capital range and f things don't work out as we think, we'll manage working capital to the lower end of that range.

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

A

And with regards to the 40,000 tons of TiO2 that we talked about producing, there will be an element of building some inventory. We repeatedly talk about we're well below seasonal norms, but I would not suggest all of that's going to go inventory because we have orders that we need to meet.

Will Tang
Analyst, Morgan Stanley

Q

Got it. And then I guess just if I could ask one more question. I'm wondering how the cost profile of electricity from that renewable energy project in South Africa compares to what you guys are realizing currently. Is that like – like should we expect a material difference or is the motivation behind [indiscernible] (00:53:00) driven by intentions to reduce your emissions profile? Thanks.

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

A

Yeah. So that – most of that benefit's going to come in 2024 because that project will be online by the end of 2023 in full force. I would say there is some advantage attached to that but not a significant amount of advantage from a cost perspective at this particular stage, but we'll continue to monitor that.

Will Tang
Analyst, Morgan Stanley

Q

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Got it. Thank you.

Operator: Thank you. Our next...

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

A

The only other item I'd add to that – the only other item I was going to add to that, Will, as you know, one of the issues we've had in South Africa is just the increasing cost structures related to Eskom and electricity. With this project that we have with solar, it'd be a relatively fixed cost structure going forward. So we won't see those significant increases going forward like we do currently. Sorry about that, Juan.

Operator: And the next question comes from the line of Ed Brucker from Barclays. Please, Ed, your line is now open.

Edward Brucker
Analyst, Barclays Capital, Inc.

Q

Hey, thanks for taking the question. So my first one just on guidance for the full year and I guess inflation expectations, are you baking in that inflation is going to be flat to where it is right now for the rest of the year? Or is there going to be some upside or downside leeway in there?

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

A

Ed, it's Tim. As it relates to inflationary cost structures, we're expecting continued inflation through the rest of the year, both from a logistics standpoint and also from a process chems and energy standpoint. In fact, there's probably another $100 million of inflation that we've got in our guidance for the rest of the year. And – but we're relatively confident and very comfortable that we'll continue to offset that with the pricing that we have.

Edward Brucker
Analyst, Barclays Capital, Inc.

Q

Got it. My next one, you surpassed the debt reduction goal pretty quickly and I was pretty impressed as well. But you noted that you still plan on paying down more debt. So, I just wanted to see if you'd be able to quantify how much more you want to pay down, and then the thought process around that to continue to reduce that especially relative to maybe increasing share repurchases or even M&A to further vertically integrate.

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

A

Yeah. So Ed, from a cash standpoint, we're very comfortable operating around the $200 million of cash on our balance sheet just given the strength of our vertical integration and our portfolio. So excess cash that we have in any given quarter over and above the high returning capital that we've talked about, we're going to use targeting 50% continued debt reduction and continually to opportunistically buyback shares under the program that we have authorization from the board.

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

A

And that $2.5 billion of gross debt was an interim target. So, as we maybe get a little bit closer to Investor Day, we'll talk about announcing what that next target would be for debt reduction.

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Operator: Thank you. [Operator Instructions] We currently have no further questions. I will hand over back to John Romano for any final remarks.

John D. Romano

Co-Chief Executive Officer & Director, Tronox Holdings Plc

Thank you. We'd like to thank you all for joining the call today. In summary, we remain focused on the levers within our control executing against our strategy, operational excellence, and delivering on our key capital projects, as JF mentioned earlier, to enhance our vertically integrated portfolio. Market demand remains solid and Tronox remains well positioned to continue to deliver on our commitments to all of our stakeholders, and we'll continue to generate the value for our customers and our shareholders. Thank you very much and have a great day. That concludes our call.

Operator: This concludes today's conference call. Thank you so much for joining. You may now disconnect your lines.

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