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Celanese Corp. (CE)

Q2 2019 Earnings Call

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Scott Richardson
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Analyst, JPMorgan Securities LLC

Robert Koort
Analyst, Goldman Sachs & Co. LLC

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MANAGEMENT DISCUSSION SECTION

Operator: Greetings and welcome to Celanese Corporation second quarter 2019 earnings conference call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference is being recorded.

It is now my pleasure to turn the conference over to your host, Chuck Kyrish. Thank you. You may begin.

Chuck Kyrish

Vice President, Treasurer & Investor Relations, Celanese Corp.

Thank you, Rob. Welcome to the Celanese Corporation second quarter 2019 earnings conference call. My name is Chuck Kyrish, Vice President, Investor Relations and Treasurer. With me today are Lori Ryerkerk, Chief Executive Officer; Scott Richardson, Chief Financial Officer; and Todd Elliott, Senior Vice President, Acetyl Chain.

Celanese Corporation distributed its second quarter earnings release via Business Wire and posted prepared remarks about the quarter on our Investor Relations website yesterday after market close.

As a reminder, we'll discuss non-GAAP financial measures today. You can find definitions of these measures as well as reconciliations to the comparable GAAP measures on our website. Today's presentation will include forward-looking statements. Please review the cautionary language regarding forward-looking statements, which can be found at the end of the press release as well as the prepared comments document. Form 8-K reports containing all these materials have also been submitted to the SEC.

Since we published our prepared comments yesterday, we'll now open the line directly for your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. At this time, we'll be conducting a question-and-answer session. [Operator Instructions] Our first question comes from David Begleiter with Deutsche Bank. Please proceed with your question.

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

Q

Lori, just on your implied Q4 guidance, what's driving the expected improvement in Engineered Materials? And how much of an improvement do you expect in that segment in Q4?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

Thanks, David. If we look towards second half through third quarter into fourth quarter, we do see indications that kind of the acute destocking that we've seen in first and second quarter is unlikely to continue. In Acetyls, although inventories are high, it really represents only a few weeks and we see some indications that there's some movement there.

On Engineered Materials, again talking to some of our key customers, some of the folks in Tier 2s and Tier 3s and the supply chain, especially into automotives and things, we see indications that what's top levels have pulled down quite significantly in the first half, and we don't expect that to continue. So we're not forecasting restocking, but we are expecting to see demand going back to more normal levels and we're suggesting that would have not as much seasonality than in fourth quarter because we've already seen the destocking occur this year. Just by way of evidence on that if we look at our order book for July, it's already about 10% higher than it was in April at this time. So that's really the basis for our outlook for the rest of the year.

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

Q

That's very helpful. And just an update maybe on the M&A pipeline and the transformational transaction that was discussed at the last earnings call. Thank you.

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

So we continue to look at all levels of M&A, David, both kind of small bolt-on acquisition as well as the more transformational activity that Mark is busy looking at. On the bolt-ons, while we have still many prospects we're looking at, we haven't found any that are delivering at the value we would like yet to complete this year, but that activity will come through. And as I said, Mark continues to work on the transformational M&A. But as we told you all before that that will come when it comes and a little bit uncertain on that timing.

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

Q

Thank you very much.

Operator: Our next question comes from Jeff Zekauskas with JPMorgan. Please proceed with your question.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Thanks very much. In your Engineered Materials business, your equity income was down in the second quarter year-over-year and you have some strong comparisons coming up. What's the trajectory of equity income? I know that there were timing issues having to do with oil prices.

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

So if we look at equity income year-over-year, we saw about a $27 million decline there. Actually, almost two-thirds of that, $16 million of it was really due to affiliates and of the affiliates $10 million was due to turnaround timing at Ibn Sina. So clearly, we expect that to reverse itself. We had some weakness in other affiliates in the second quarter and in the first half, as I think we described last quarter, specifically around our China affiliates that are a little more exposed to auto. We've seen some strengthening of that in the second quarter.

So I think going forward, again, we'll see the reversing of that turnaround time in Ibn Sina. We are seeing some strengthening in our affiliate performance. And then the remainder of that, the additional $10 million year on year is just general market conditions, which, as I described to David's question, we do start to see some signs of starting to recover some of the demand as we go into the second half.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Is acetic acid pricing in China getting better sequentially, and might it make a difference to your returns in the third quarter?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

Certainly if it gets better, it won't make a difference to our returns in the third quarter. I think indications we've had in the last few weeks is we are starting to see some firming up pricing in acetic acid. Things move around those. So whether that's sustained or not, I think is a question.

Todd, do you have any comments you want to make around acetic acid pricing going forward?

Todd Elliott
Senior Vice President, Acetyls, Celanese Corp.

A

Jeff, the demand situation in China is probably the most important thing to watch. We saw demand come off by at least 10%, probably more than that for acetic acid, up sequentially Q1 to Q2. That's an industry comment, not a Celanese comment. But that's weighed on demand conditions, of course, and then therefore pricing conditions and pulled down utilization rates in the second quarter.

We're watching that very closely. We've pivoted our business to derivatives, mainly vinyl acetate and emulsions and have grown that space by 9% sequentially on volumes and that slipped to the overall acetyl business by about 2% sequentially. But to your point, we're watching China price. We're heavily involved, of course, in that part of the world and demand is a key thing to watch at this stage.

Jeffrey J. Zekauskas
Analyst, JPMorgan Securities LLC

Q

Great. Thank you so much.

Operator: Our next question comes from Bob Koort with Goldman Sachs. Please proceed with your question.

Robert Koort
Analyst, Goldman Sachs & Co. LLC

Q

I was wondering if you could give us some breakdown of your CapEx. You talked about $0.5 billion in 2021. Can you give us those buckets in terms of maintenance or cost reduction activity and then gross spending in maybe some of the highlight projects that are in there?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

Sure. Thanks, Bob. So if we look at where we are and let me just start with 2019. So in 2019, we're approaching $400 million in CapEx. If you look at where that's being spent, about 50% of it is in EHS and what I call maintain margin project. So turnaround, reliability related projects, maintaining the equipment to basically maintain where we are, about 25% of it's in cost reduction projects. And I think what's significant about that is that's about three times more than we've had in previous years and that really reflects our continued focus on helping ourselves, if you will, through productivity while doing relatively minor investments, so they yield large future cost saving. And then about 25% is in revenue generation.

Now as you go forward and you see that number getting closer to $500 million, all of that growth is really in revenue generation and/or productivity. So it is projects like methanol expansion, it's project like the VAM expansions we've done. We have some additional compounding lines starting up as we go forward as well as some debottlenecking activity in various polymers in the U.S. and in Europe and in Asia actually, in all three regions. So the real growth is all in revenue-generating activities, either volume and/or productivity. And in almost all cases, we can trade off productivity for volume.

Robert Koort
Analyst, Goldman Sachs & Co. LLC

Q

Got it.

Scott Richardson
Chief Financial Officer & Senior Vice President, Celanese Corp.

A

Bob, I think on a go-forward basis, I think what I would bake in there on that is about $150 million of MOB type CapEx, and the rest is exactly what Lori talked about from a cost reduction and rev-gen standpoint. But we look at the entire bucket of CapEx, and the returns we generate on that entire bucket, inclusive of MOB, perhaps 20% – greater than 20% return. So that's what I would bake in on a go-forward basis.

Robert Koort
Analyst, Goldman Sachs & Co. LLC

Q

Can I ask on the EM side? You guys had some pretty explosive growth there four, six, eight quarters ago. It started to slow, and then you're also battling maybe some raw material pressures and being more selective on your pricing. This quarter it looked like both volume and price got dinged. I guess I can see the volume side, but can you talk a little more about what's going on in price and maybe how you're pricing in EM correlated to what's happening in the raw materials?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

So if we look at Engineered Materials, as we've talked about, we've seen the decline in auto demand, we've seen the decline in electronics demand. Clearly in some areas, especially nylon, for example, and elastomers, which have been heavily challenged by those declines, we have seen a lot of competitors in the market driving price down, and we've seen a lot of pricing being done to compete for volume. Now we haven't followed that all the way down, and obviously that's why our volumes are somewhat off in those areas. But we have seen some pricing pressure, especially in those areas and especially as it applies to automotive.

What I would say there is nylon and elastomers are heavily impacted by the M&A we had over the last two or three years. So that's also year on year and quarter on quarter. We haven't had any significant M&A in the last year. So that is a change from, say, the past several years. And what we see with our affiliates is while we're happy overall with our financial performance, a lot of the volumes that came in with – sorry, not with our affiliates, but with our acquisitions – a lot of the volume that came in with our acquisitions were not as differentiated as our base portfolio, not generated using the same project model, and therefore not as sticky as some of our base portfolio.

So as we've gotten into this more challenging economic backdrop, we've seen some of those volumes not be as resilient as our base portfolio. Over time, we expect that to change as we are developing those volumes consistent with our business model, but we have seen those influences come together in this quarter.

Robert Koort
Analyst, Goldman Sachs & Co. LLC

Q

That's helpful. Thank you.

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

Thanks.

Operator: Our next question comes from Vincent Andrews with Morgan Stanley. Please proceed with your question.

Vincent Stephen Andrews
Analyst, Morgan Stanley & Co. LLC

Q

Thank you and good morning. Just a question around your capacity in acetyls in Asia, there were some reports during the quarter that you were taking your own utilization rates down. So could you discuss that a little bit and then help us understand where rates are now in the third quarter and where you expect them to be?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

So maybe I'll start and ask Todd to weigh in more specifically. Generally in acetic acid in China, we are seeing a demand decline of more than 10% in the second quarter, and that put China capacity utilizations around 70%. And that's versus if you go back, say a year ago, you know that was well into the mid-80s or even a little bit higher. So for certain, utilization is significantly down in China in general.

Our own capacity, I'll let Todd come on, on that, but I will say we did see some other producers in China take units down entirely and take capacity back in response to that as that combined with a historically low level of pricing made it unaffordable for folks to run. Maybe, Todd, you have a few comments on our operations.

Todd Elliott
Senior Vice President, Acetyls, Celanese Corp.

A

Yes, sure. Thanks, Vincent. Thanks, Lori. Vincent, we flex our acetyls network on a daily basis. This is what we do every day and every week and every month, try to get the maximum value we can in each of the products. And we did a great deal of that in Q2.

Our activations were up 30% sequentially, and this is our measurement of really actions and decisions that we take to flex our network in the best way. So remember we had a couple of turnarounds in the system in Q2. We had a vinyl acetate turnaround in Bay City as well as in Nanjing. So that kept VAM rates lower in those two units. Acetic acid wise, if you look out a little bit, we do have turnarounds. The first part of the turnaround in Singapore towards the end of this quarter, Q3, and then mainly into Q4.

So without giving specific rates by unit, I think the key takeaway is our flexibility, our ability to pivot whether acetic acid or derivatives is really the differentiation that we would point to. So we intentionally moved plus-5% of our acetic acid tonnage downstream to our derivatives. So we shifted to VAM, shifted to emulsions 5% sequentially. That allowed us to grow VAM and emulsions by 9% volumetrically from Q1 to Q2, and then therefore lifting the overall chain by 2% sequentially.

So those choices, those options and choices are what we would point to, and really the end result is profitability of $189 million, which if you take out the turnaround that I mentioned before, which were about $50 million of headwind in the quarter puts us about that $200 million run rate for the business on a quarterly basis while keeping EBIT margins above 20%.

Vincent Stephen Andrews
Analyst, Morgan Stanley & Co. LLC

Q

Okay, that's helpful. If I could just ask in EM on the volume side of the equation, you called out a couple of things that a little more color on would be helpful. One, it sounded like in the first quarter there was an inventory build from some of the healthcare customers. If can you just help us understand how that volume does swing around from quarter to quarter. It seemed like in the first quarter, volume was strong if I go back and look at the comments from then. So how does that work that their volume shifts around? And then secondly, I think there was a comment that volume was also hurt by a mix effect. If you could just help us understand what that is. Thank you.

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

Thanks, Vincent. And actually those are really the same thing. So medical continuous to be a very strong sector for us, but it is a very relatively small volume sector with very high margin. And so, actually small swings in volumes can have a very big impact on our earnings. And what we saw in the first quarter is we did see customers, particularly in the UK building volume in anticipation of a Brexit move, clearly, it didn't happen, worrying about tariffs and availability and everything else relative to Brexit. And again, it's not a huge volume, but it swings a good bit of the margin.

If you look at our EM quarter to quarter, first quarter to second quarter, of what we say is the volumetric impact – of that volumetric impact, so 7% total volumetric impact, 4% of that was actual EM volume. 3% was just the mix with most of that being medical. So just the fact that medical volumes got moved into the first quarter from second quarter. We see this from time to time. It was particularly big first and second quarter, but medical tends to be a bit lumpy. We get a big order once we had FDA approval and people will stock up as they prepare for run, and then – so go down. So it tends to be a bit lumpy or maybe there's some of our other business, but we did see the first to second quarter primarily because of the Brexit impact.

Vincent Stephen Andrews
Analyst, Morgan Stanley & Co. LLC

Q

Okay, thank you very much.

Operator: Our next question comes from Mike Sison with KeyBanc. Please proceed with your question.

Michael J. Sison
Analyst, KeyBanc Capital Markets, Inc.

Q

Hey, nice quarter there. In terms of the Acetyl Chain, I'm just curious. You guys, as you've talked about, do a good job pivoting in upstream, downstream geographically. And so, if you think about the second half of the year, where do you think you're going to need to pivot to make your earnings outlook for the year and maybe it's hard to say, but just any current – are you going to stay downstream, that type of thought?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

Thanks, Mike. So on the Acetyl Chain, quite frankly we're quite pleased with where we are, continuing to turn in seven consecutive quarters above 20%. And I think the second quarter is really just a good example of the strength of the model in acetyls and the ability to have optimization to continuously do activations, as Todd just described, to really deliver the most value at wherever it exists beyond the chain.

I think an interesting point and maybe a bit to your question, if you look at the very low pricing we're seeing in acetyls in China, less than $400 a ton. The last time we saw this level of pricing was back in first quarter of 2017. And if you look at the earnings, the first quarter 2017 for Acetyl, it was $109 million. You compare that to the second quarter now at $189 million. We've had an $80 million uplift in the value of the Acetyl Chain and basically the same economic condition based on the strength of the model and the folks deploying it and the focus on productivity and all of the other steps.

Put another way, margin on acetyls went from 14% in the first quarter 2017 to now 22% in second quarter 2019. So I think that really speaks to the strength of the Acetyl Chain. Really to achieve that $10.50 view for the year, it's really just continuing to activate that model and continuing to deliver on that $200 million level quarter on quarter. And obviously if we were to get for whatever reason a good run up in the price of acetic acid in China in particular, that would just be more on top of that.

Michael J. Sison
Analyst, KeyBanc Capital Markets, Inc.

Q

Got it. And then there's a quick follow up. In terms of EPS, you did about – well, you did $5 in the first half and adjusted EBIT about close to $800 million. So if you look at the second half, you need a little bit more obviously in EPS, $5.50. Does your adjusted EBIT have to go up a lot in the second half to do better, or is it – maybe just a thought on how the second half adjusted EBIT looks relative to the first half?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.
A

Again, we are assuming some improvement in market conditions based on my earlier comments. So obviously, EBIT will go with that. But clearly, also on an EPS basis, we're held by the share buybacks that we've had in the first half of this year as well as last year. But let me turn it over to Scott to maybe give a more complete answer.

Scott Richardson
Chief Financial Officer & Senior Vice President, Celanese Corp.
A

I think that that's really the point. I think we do need a slight improvement in the adjusted EBIT. And I think Lori talked earlier about how we expect that, given the destocking we saw in the first half that we believe the second half can be better. Order book starting out in July are a little better than what we saw, particularly in the second quarter. And then just what we saw in the first half of this year, we're currently not baking in the same level of Q4 seasonality. So when you kind of take all those things into consideration, you should have slightly a better adjusted EBIT in the second half plus the benefit of the buybacks we did in the first half and what we expect to do in the second half.

Michael J. Sison
Analyst, KeyBanc Capital Markets, Inc.
Q

Got it, thank you.

Operator: Our next question comes from John Roberts with UBS. Please proceed with your question.

John Roberts
Analyst, UBS Securities LLC
Q

Thank you. Methanex is going forward with its third unit in Geismar. Todd, could you give us an update on the Clear Lake methanol expansions that you're doing with Mitsui?

Todd Elliott
Senior Vice President, Acetyls, Celanese Corp.
A

Thanks, John. As we announced last quarter, our plan is to take that unit up to 1.7 million tons. That would be operational some time in 2022. We're pleased with the output of that unit that continues to contribute value as it's running above the original design capacity. But we're on track again to raise that up by about 150,000 tons. That would be shared with our partner and, again, on track towards 1.7 million tons by 2022, and we'll update that specific timing as we work through the progress. We did receive the requisite permit from Texas to proceed down the path there.

John Roberts
Analyst, UBS Securities LLC
Q

Okay. And then, Lori or Scott, in the Engineered Materials business, could you share with us how much the automotive business was actually down during the second quarter? Was it down double-digit percent?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.
A

So if you look at actual automotive builds, quarter to quarter we actually saw about a 3% drop, most of that coming entirely out of Asia. The U.S. was actually up a little bit on the strength of trucks, but EU was down. Of course, builds is interesting, but what really matters to us is what the demand for product is. And there in our discussion with the Tier 2 and Tier 3 suppliers to auto, in all regions we were hearing from some of our key customers and distributors declines of 20% to 30% on volumes. So clearly, an indication to us that destocking was continuing into the second quarter.

John Roberts
Analyst, UBS Securities LLC

Q

Were you down in line with those Tier 2 discussions that you had?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

No. our EM volume, actual volume was down about 4% in total for EM.

John Roberts
Analyst, UBS Securities LLC

Q

Okay.

Todd Elliott
Senior Vice President, Acetyls, Celanese Corp.

A

And, John, the auto piece of that was just maybe about 1 percentage point higher than that.

John Roberts
Analyst, UBS Securities LLC

Q

Okay, good. Thank you.

Todd Elliott
Senior Vice President, Acetyls, Celanese Corp.

A

Good.

Operator: Our next question comes from P.J. Juvekar with Citi. Please proceed with your question.

P.J. Juvekar
Analyst, Citigroup Global Markets, Inc.

Q

Yes. Hi, good morning. Lori, as the center of gravity for acetyls shifts from the U.S. and at the same time for EM the focus of growth seems to be China, does that mean that there would be less integration between the two businesses going forward?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

It's an interesting question, P.J. I don't think there's less integration going forward. We have raw materials available in China. There's plenty of acetic acid producers. It just may mean that less of our own material was going into the EM in China, but we continue to have a growing EM business in the U.S. So I don't see it having a significant change in terms of the amount of integration between the two businesses.

P.J. Juvekar
Analyst, Citigroup Global Markets, Inc.

Q

Okay, thank you. And as acetic acid prices dropped, you nicely pivoted to VAM and emulsions. And so, that's a great tactical move from your team. But when do competitors catch up with that move or are they not that flexible, because I would imagine that these are big large companies that are global and they should be able to do the same thing?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

So the interesting thing is I think there aren't any competitors who can do the same thing. That's the beauty of our integrated model. There are a lot of competitors who make acetic acid, there are competitors who make VAM and there are competitors who make emulsions. There's not many who make all three from the start of the value chain, that's CO and methanol all the way through emulsion. And that's really where our model is, I think, differentiated from others and is strong and allows us to give less volatile results and this level of earnings is because we are fully integrated through the chain and fully integrated geographically, which not all of our competitors are. So we have the ability, as we did this quarter, to reduce our exposure to Asia and increase ourselves into the Western Hemisphere, where available margins were higher for VAM and emulsion.

P.J. Juvekar
Analyst, Citigroup Global Markets, Inc.

Q

Thank you.

Operator: Our next question comes from Duffy Fisher with Barclays Bank. Please proceed with your question.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Yes, good morning. A question around Lori's comment that you're $80 million a quarter better now in this kind of a tough acetic or acetyls market than you were in Q1 of 2017. It would strike me that that's got to be one of three factors, either better realized price versus the posted price, better cost, or you're selling more volume into the market. Can you break it down into those three buckets, that $80 million? Where does the majority of it come from? And how much do you think is structural versus maybe just some transitory fortunate business?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

Duffy, I think – look, we worked very hard for these results. So what I would tell you is I don't have the exact breakdown in front of me. It's a little bit of all of it, but it really is the ability to flex our model and make choices about where we take value out of the chain. So it's certainly price and the price we're realizing for VAM and emulsions, if you will, versus acetic acid. But I think the point is it is the strength of the value chain, the strength of the geographic model, and the talent of our folks, if you will, to be able to constantly flex and make decisions every day about where to extract value in that chain, which makes us confident that we can continue to deliver these results even in periods of low margin environment like we've seen in the second quarter.

Todd Elliott
Senior Vice President, Acetyls, Celanese Corp.

A

And, Duffy, I could add. Remember, we've added integration with methanol. We've added integration more recently with carbon monoxide. We expanded our vinyl acetate unit in Clear Lake by 150,000 tons. We've achieved more options, frankly, with this global network that Lori just outlined. So it's really the combination of that and the real-time use of data, which provides us insights to make these all – these to affect these decisions that contribute to the result. We believe it's repeatable and we're going to look to add additional value steps going forward. John asked the question about the methanol expansion. There are other value addition steps that we're pursuing and look to layer those on top as we look out.

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

Thanks, Todd. And I think we shouldn't ignore productivity, for Celanese we are delivering about $100 million a year in productivity steps. So again, roughly kind of 50-50, that's certainly doing that year-on-year-on-year is making us more competitive as well lowering our overall cost base.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Great. And then does the market believe that the coal gasification explosion at Yima is going to be a big deal for the acetic acid and the acetyls market in China?

Todd Elliott
Senior Vice President, Acetyls, Celanese Corp.

A

Duffy, I think, it's too early to get into that and it's a terrible thing. Many lives lost and multiple injuries in there. In Henan province, there's something like 11% of domestic Chinese capacity in that province. So from a country perspective, that province is a big producer. This particular unit was only a couple hundred thousand tons. So call it 2% or so of the domestic capacity. So we're watching that. It will remain to be seen what the province does across the other units there in Henan and whether steps will be taken to curtail operations there. We're focused on what we can do with our customers to keep our efforts and business connected and ultimately work the Q3.

Duffy Fischer
Analyst, Barclays Capital, Inc.

Q

Terrific. Thank you, guys.

Operator: Our next question comes from Laurence Alexander with Jefferies. Please proceed with your question.

Laurence Alexander
Analyst, Jefferies LLC

Q

Good morning. I have two quick ones. First, on the uptick in the order book that you've seen recently, can you give a sense for how broad-based is it or if there are any particular regions that are stronger than others in terms of the pace of improvement?

And secondly, on productivity and turnarounds, is there any lumpiness that we should be thinking about for 2020 and 2021 in terms of the timing of outages going forward?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

So on the order book, we're seeing it fairly broadly, I would say, because of the declines we saw in second quarter. It's probably more noticeable in some of those grades nylon, elastomers that I talked about, seeing good recovery in POM, good recovery in LDPE and to electronics. So I'd say it's pretty broad across the different grades that we make in the order book, and then also pretty spread between the regions at this point.

Scott Richardson
Chief Financial Officer & Senior Vice President, Celanese Corp.

A

On turnarounds, Laurence, we're doing that work right now on flanging that up across the corporation as we do turnaround planning, and we'll more provide more insight into that probably in October.

Laurence Alexander
Analyst, Jefferies LLC

Q

Thank you.

Operator: Our next question comes from Ghansham Panjabi with Robert W. Baird. Please proceed with your question.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.

Q

Thank you. Good morning. And, Lori, congrats again on your new role.

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

Thank you.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.

Q

I guess going back to your EPS guidance reiteration for 2019 and sort of the embedded expectation for improved demand fundamentals as per your comments in the press release. Are you basically assuming that the inventory destocking that pressured the first half is now behind you or are you assuming any sort of acceleration in end market volumes including in the EM segment?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

So that assumption is, we are assuming that destocking has pretty much behind us. Now we're not assuming any restocking, if you will, we're really assuming a return to normal demand in the third and fourth quarter and some assumption around not seeing the amount of seasonality in fourth quarter we usually see for destocking because we believe the destocking has already occurred.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.

Q

Okay, that's helpful. And then just in terms of some of the supply chains for markets such as electronics perhaps moving away from China into other parts of the world including Southeast Asia at least directionally, how are you sort of balancing your focus on expanding your EM footprint in China, which you called out in your prepared comments versus some of the other regions across Southeast Asia more broadly? Thank you.

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

Yeah. So we are very focused on expanding our EM operations in China in not just our sales. I mean, I think if you go back historically most of – our EM business in China really started with following big auto, if you will, into China and people that we supplied in other regions of the world whether it be Europe or the U.S. basically supplying the same materials into China. And so it's very much on an exporting material from the U.S., exporting from Europe into China. So if you look at it the large percentage of our EM materials in fact quite the majority are not just produced but also compounded outside of Asia, and then imported into Asia and into China.

That worked when we were doing a lot of auto and things that had long lead times and things that had pretty long life. But if you look at our business now and especially as you go into consumer and electronics and things that maybe even change every six months to a year, it's just not a supply chain that can meet our customer demands to get products more quickly, development more quickly. So we are already – have a couple of projects going in this year to add compounding lines in China, and our future capital program over the next few years is focusing on adding poly as well as additional compounding in China, really to shorten the supply chain to meet the needs of our current customers in China and the rest of Asia.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.

Q

Thank you.

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

Thank you.

Operator: Our next question comes from John McNulty with BMO Capital Markets. Please proceed with your question.

John P. McNulty
Analyst, BMO Capital Markets (United States)

Q

Yeah. Good morning. Thanks for taking my question. Lori, in your prepared remarks, you had highlighted the ability to accelerate some of the actions around cost cutting. Can you quantify or give us the magnitude as to what you can pull forward to 2019 this year?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

Yeah. So we pulled forward about $60 million, let's call it, of capital projects, capital spend. So, give you an example, these are things like retrofitting and refurbishing natural gas boilers to get better energy efficiency at plants. I mean these are things that we won't necessarily see the payout this year, but we'll see the payout next year and the years that follow. But to give you an idea on productivity, the combination of capital projects and other productivity, where we had been doing a run rate of about $100 million a year on productivity, that number for this year will be between $150 million to $200 million. So we've been able to pull in, call it, $50 million to $100 million on a full-year basis now. Obviously, not all was implemented January 1, so we won't get all of it this year, but call it $50 million to $100 million.

John P. McNulty
Analyst, BMO Capital Markets (United States)

Q

Got it. That's helpful. And then with regard to EM, I guess, how much or what percent roughly of your products can be kind of swapped out quickly if there is competition around pricing because it does sound like that may have been a little bit of an issue? And then how much of it's really kind of specked in and is really tough to displace around random price cuts or lapses in discipline?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

I'm not sure I know the exact numbers, I'll ask Scott to back me up here, but right now I would say it's probably a third of it's really very sticky, I mean, very, very hard, a third of it is specked in, but probably others could be are either already specked in or could be and then a third of it is more of what I'd call, me-too kind of products which is easier for people to come in and out of based on price.

Scott Richardson
Chief Financial Officer & Senior Vice President, Celanese Corp.

A

I think that's exactly right, John. We're – I mean about a third of the business is a little bit more transactional, it's still an engineered solution. So it's not something that changes, I mean, from one day to the next, but it can be switched out. The reality of it too is we can also switch out between polymer families, so that's an opportunity for us as well depending on where various raw materials are and given the breadth of our portfolio now and the fact that we have over 20 different polymer families that we can go into, it just gives us a lot more flexibility in this market depending where raw materials are in the more transactional spaces. But it continues to be important for us as we build our project pipeline and really start to try to put more focus on that specked in sticky business that Lori talked about.

John P. McNulty
Analyst, BMO Capital Markets (United States)

Q

Great, thanks very much for the color.

Operator: Our next question comes from Kevin McCarthy with Vertical Research Partners. Please proceed with your question.

Kevin W. McCarthy
Analyst, Vertical Research Partners LLC

Q

Good morning. A question on the acetyls industry. As we look at some of the trends, it seems to us that there's a relatively large number of outages across the industry in recent months, recent quarters. My question is do you agree with that? And if so, do you have a sense for how much or how many of these outages are maintenance related among your competitors versus caused by economic reasons with market prices thinking do you see competitors throttling back simply because they go cash negative for example?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

Yeah. Thanks, Kevin. It's always a little bit hard to say, but now let me ask Todd to follow up my comment. We know in China that some capacity has been intentionally shut down due to the combination of demand and pricing. Second quarter is traditionally a fairly heavy turnaround quarter as well. So certainly in the U.S. and in Asia, we see some taken out for maintenance. Now having run operations for 35 years, I can tell you people make a lot of decisions around extending maintenance outages and doing them at a slower pace and things when economics are like they are now. So it's always a little bit unclear about how much is economic versus how much is maintenance. But certainly we've seen both.

Todd, you may have more specifics you can provide.

Todd Elliott
Senior Vice President, Acetyls, Celanese Corp.

A

Kevin, it's a good question. And to Lori's point, it's hard to know the exact figure. But if we were to try and track utilization rates with that demand drop sequentially by over 10% in acetic acid Q1 to Q2, we believe that would have pulled utilization rates down on a global basis to just under 80%, so call it around 79% with China actually dipping under 70% utilization rate.

So on the heels of that to your question, to your point, we do believe kind of intentional curtailment occurred late in Q2. We would call a run rate typically around 300,000 tons of sort of normal outages. We think that that might have doubled if you kind of ramp it up and factor all that in. It's again hard to be absolutely precise here. But there had to have been some intentional actions. We certainly do our part with our own network and that's what we do to take care of our customers and also to maximize value for our shareholders all the time.

So there were some curtailments indeed. And as we go into Q3, that's important to track and watch and really set the tone for improvement as we go into second half of the year. But demand is critically important. We've got to focus on demand conditions and starting to see that that industrial space, particularly in China, is starting to recover and that will help really a lot of all of our businesses.

Kevin W. McCarthy
Analyst, Vertical Research Partners LLC

Q

That's very helpful. And then as a follow-up, again sticking with Acetyls, what are your latest thoughts on rationalization of Celanese's capacity in Asia? Did you need to get through IMO 2020 and really see how the fuel markets react in Singapore?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

That's exactly right. I mean, we've announced our intentions to do an acetic acid reconfiguration. We are still progressing with that project. But ultimately the decision, it is based on productivity by the way. It is based about utilizing lower raw material costs in the U.S. Gulf Coast and taking capacity out of Asia. But that decision of where to take capacity out of Asia will depend on exactly what you said, where do we end up with bunker fuel pricing, what does that mean for Singapore capacity, where does coal pricing go, what does that mean for Nanjing margins, and we'll make that decision at that time based upon where we are on both of those.

Kevin W. McCarthy
Analyst, Vertical Research Partners LLC

Q

Thank you very much.

Operator: Our next question comes from Arun Viswanathan from RBC Capital Markets. Please proceed with your question.

Arun Viswanathan
Analyst, RBC Capital Markets LLC

Q

Great. Thanks. Good morning. I just wanted to go back to the guidance for both Q3 and Q4. I guess looking at Q3, it's just between Q1 and Q2, I would put it, maybe at $250 million. And then your statement, there seems to be a path to the $10.50, so that would imply maybe around $3. I just wanted to understand that path a little bit more. I guess the mechanics would be both Acetyls and EM going up in margins and price and volume. Where do you see the greatest confidence in that path? Is it in EM or Acetyls, and where do you see the risk factors as well? Thanks.

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

So as I think we said, we really feel confident in our ability to continue to do deliver Acetyls in the $200 million range. Clearly, if we see firming in acetic acid pricing, as we've had some indications if that's sustained, that could be further upside for Acetyls. And for all the reasons we discussed earlier around destocking, et cetera, we expect to see recovery in Engineered Materials as we go forward through the end of the year. And then of course, since we're talking earnings per share, we also have the impact of the share buyback and seeing the full-year impact of that on the numbers.

Arun Viswanathan
Analyst, RBC Capital Markets LLC

Q

Okay, thanks. And do you also expect to update your longer-term targets that you provided last year for 2018 through 2020 at some point? Thanks.

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

So we're working now through a strategy refresh. We'll be working through that through the end of the year. Clearly, part of that will be to look at 2020 again and relook at our view for 2020. So hopefully in the October timeframe, we'll have that certainly as we work through the strategy. And to the end of the year we'll have a view on 2020.

Arun Viswanathan
Analyst, RBC Capital Markets LLC

Q

Okay, thanks.

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

As well as the out years beyond that, yeah.

Operator: Our next question comes from Aleksey Yefremov with Nomura. Please proceed with your question.

Aleksey Yefremov
Analyst, Nomura Instinet

Q

Thank you, good morning. In Engineered Materials, how should we think about your margin sustainability? Was the level of margin for wholly owned business in the first half representative of what you could see in the second half?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.
A

Look, I think for all the reasons we described, I think we expect second half to be stronger for Engineered Materials than it was for first half. I think certainly for our acquired businesses, we expect further strengthening in those business models and the delivery against the model for those going forward, as well as the general improvement with the market conditions with not anticipating further destocking. So I think for our own in-control businesses as well for our affiliates, but especially for our owned businesses, we expect a stronger second first than first half.

Scott Richardson
Chief Financial Officer & Senior Vice President, Celanese Corp.
A

And, Aleksey, just typically volumes are strongest in Asia in Q4. Margins are a little bit lower there versus the Western Hemisphere, just with Chinese New Year in Q1 moving into that timeframe. So typically, our Q4 margins are a little bit lower. So that would be something just to keep in mind as well.

Aleksey Yefremov
Analyst, Nomura Instinet
Q

Great, thank you. As a follow-up, you guided third quarter somewhere between first and second quarter. Should we think about that guidance as sort of the midpoint, or are you closer to the first quarter level or is second quarter level in your thinking about 3Q?

Scott Richardson
Chief Financial Officer & Senior Vice President, Celanese Corp.
A

Aleksey, I think we're still fairly early as we start the quarter, and so I think it's going to really be how demand materializes. I think there have been some pretty public announcements from some of the, for example automakers taking summer shutdowns. But we do expect to more or less see destocking coming to an end, as we talked about. So it's in that range. And as we work our way through the quarter, we'll have a better idea on where we finish, but it's somewhere in that range.

Aleksey Yefremov
Analyst, Nomura Instinet
Q

Thanks a lot.

Operator: Our next question comes from Jim Sheehan with SunTrust Robinson. Please proceed with your question.

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.
Q

Share buybacks were pretty robust in the quarter. Are you still targeting around a 7% share count reduction for the year? It does seem like you're on track to do even more possibly.

Scott Richardson
Chief Financial Officer & Senior Vice President, Celanese Corp.
A

Jim, we've been very open about the fact we're going to be opportunistic with share buybacks. We expect this year to be in the range of where we were in 2018. We did $800 million in 2018, and we expect to be in that general range. We're finishing the first half at $500 million. In the last 12 months, we've bought back about 9% of the outstanding shares.

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Thank you. And on the full-year outlook, $10.50, you're assuming an acceleration of sorts in the fourth quarter. If you don't see that uptick, what kind of downside do you see for full year 2019?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

So if we were to see market conditions continue similar to the first half, then we would expect our earnings per share to be down 3% to 5%.

James Sheehan
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Thank you.

Chuck Kyrish
Vice President, Treasurer & Investor Relations, Celanese Corp.

A

Rob, we'll make the next question our final question.

Operator: Our last question comes from Matthew Blair with Tudor, Pickering, Holt. Please proceed with your question.

Matthew Blair
Analyst, Tudor, Pickering, Holt & Co. Securities, Inc.

Q

Hey, good morning. Thanks for taking my questions. Could you talk about how the month of June performed relative to the entire second quarter for both Acetyl Chain and Engineered Materials? It sounds like maybe June was the strongest month of the quarter in EM, but potentially one of the weakest months in Acetyl Chain. Is that the right way to think about it?

Lori J. Ryerkerk
President, Chief Executive Officer & Director, Celanese Corp.

A

So let me talk about EM. So typically, the last month of the quarter is the strongest quarter for EM. That's just typical, so just the way people run their businesses. So definitely, I think June was actually probably not our strongest month in the second quarter, but it was a good quarter for us in June.

Interestingly enough, we actually saw increase in auto and China in June, the first increase in terms of auto sales that's occurred since May of last year in China. We don't necessarily think that's sustainable because it was based on some very heavy discounting going on in China to move vehicles that won't meet the new air emission standards that are going into place. So June was a bit of an interesting month. So some areas of strength, some areas of weakness.

I'd say for EM, not a good month, but not atypical for the end of the quarter. I think in Acetyls, I don't know that it was significantly different. I can ask Todd to comment. I don't actually think it was particularly strong or weak as comparison to the rest of the quarter. Scott, do you have any?

Todd Elliott
Senior Vice President, Acetyls, Celanese Corp.

A

No, that's good. I think that's fair, Lori. I mean, the middle of the month was probably the lowest of the three, but not to your point; pretty balanced overall.

Matthew Blair
Analyst, Tudor, Pickering, Holt & Co. Securities, Inc.

Q

Great, thanks. And then, Todd, could you talk about the Chinese VAM market? So far in Q3, it looks like pricing might have come off quite a bit already this quarter. There have been some reports of economic run cuts from some of the major producers, including Celanese. Do you have any more color there?

Todd Elliott
Senior Vice President, Acetyls, Celanese Corp.

A

Again, similar to the comments from before with respect to our operational activities, so we will flex our units as we see the match with customer needs, customer demand, cost, profitability. So we'll do that in all units around the world, so that flexibility is important for us. So I would not characterize VAM China as declining at this point. I think it's been fairly healthy as we go Q2 to Q3, more to come and certainly we got to watch the development over the course of the quarter. But no, I think that was a little too severe of a characterization in terms of the Q-to-Q drops. So we're working hard to lever the quarter in Q3 as we outlined before.

The one thing we do have to navigate through, we do have a turnaround in Q3 in Frankford on VAM. So we've got probably a $10 million headwind there that we've got to work around. But that's probably the one thing from an operational perspective we've got to through.

Matthew Blair
Analyst, Tudor, Pickering, Holt & Co. Securities, Inc.

Q

Thank you very much.

Todd Elliott
Senior Vice President, Acetyls, Celanese Corp.

A

Thank you.

Operator: Ladies and gentlemen, we've reached the end of the question-and-answer session. At this time I'd like to turn the call back to Chuck Kyrish for closing comments.

Chuck Kyrish
Vice President, Treasurer & Investor Relations, Celanese Corp.

Thanks, Rob. Certainly we'd like to thank everyone for listening in today and the good questions at work. As usual we're around after the call to address other questions that you have and Rob, with that you can close this out.

Operator: Thank you. This concludes today's conference. You may disconnect your lines at this time. And we thank you for your participation.