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- Q1 2014 Momentive Specialty Chemicals Earnings Conference Call

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PRESENTATION

Operator

Good days ladies and gentlemen, and welcome to the 2014 Momentive Specialty Chemicals conference call. My name is Katina and I will be your coordinator for today.

(Operator Instructions).

As a reminder this conference is being recorded for replay purposes. I would now like to turn the presentation over to your host for today's call, Mr. John Kompa, Investor Relations, Momentive Specialty Chemicals. Please proceed.

John Kompa - Momentive Specialty Chemicals - Chairman of IR

Thank you Katina. Good morning and welcome to Momentive Specialty Chemicals' First Quarter 2014 earnings conference call. On today's call will be Craig Morrison, Chairman, President and CEO. Bill Carter, Executive Vice President and Chief Financial Officer. And George Knight, Senior Vice President and Finance and Treasurer.

As a reminder this call is also being webcast and the slides referenced in today's conference call are available through the Momentive.com website under the investor relation section of Momentive Specialty Chemicals. A replay of this call will be available for one week. And the replay dial in information is contained in our latest earnings release.

Before we start, I'd like to review information about forward-looking statements and the use of non-GAAP information as part of this call. As you know some of our comments today may include statements about our expectations for the future. Those expectations are subject to known and unknown risk, uncertainties and other factors that may cause the Company's actual results and performance to be materially different from any future results or performance suggested by these expectations.



The slide you now see gives you more information on the assumptions and factors we consider in making those forward looking statements. We can't guarantee the accuracy of [core counts] or estimated, and we undertake no obligation to update any forward-looking statements during the quarter. Except as otherwise required by law. For more information on our risk factors, please our earnings press release and our SEC filings.

In addition, some of our comments may reference non-GAAP financial measures. A reconciliation of the most directly comparable GAAP financial measure and other associated disclosures are contained in our earnings release and on our website. Our earnings release and our recent SEC filings are also available on the internet at momentive.com.

With that, I'll now turn the call over to Craig Morrison to discuss our quarterly results.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Thanks, John.

Turning to page four, our first quarter revenues were approximately \$1.3 billion, an 8% increase, while segment EBITDA increased by \$12 million or 11%. Total segment EBITDA reflected higher overall volumes and productivity gains driving stronger results in both of our operating divisions.

In our global forest products business, EBITDA grew 9% due to continued improvement in North American housing, emerging market growth and our productivity initiatives. Our epoxy, phenolics and coatings division posted EBITDA gains of 12% from strength in our oilfield, specialty epoxy and Versatic acid businesses, offset by continued softness in our base epoxy resins.

In our first quarter, we also successfully completed the strategic acquisition of a profits facility in Shreveport, Louisiana. The Shreveport site provides immediate capacity to meet the growing demand for our oilfield products. The site's central location in the Haynesville Shale region enhances our existing integrated asset network. We anticipate that this acquisition will continue to support our specialty portfolio growth going forward.

Turning to slide five in our combined raw material index, you can see that raw material input cost increased sequentially in the first quarter of 2014 versus the fourth quarter of 2013. Compared to the prior year period, raw materials were mixed. We saw decreases of 2% in phenol and 5% in urea, while experiencing a 26% increase in methanol. Going forward, we continue to remain vigilant on the pricing front to effectively manage raw material volatility.

Turning to slide six, we've highlighted our integrated manufacturing network in North and Latin America, which are our key growth markets for our forest products business. As a forest products technology leader, we're focused on developing new products that optimize our customers' process capability and product performance.

Additionally, we continue to look to expand our extension manufacturing network. Our last expansion in 2010, which was our Montenegro site, further strengthening long-time presence in Latin America. This world-class site is the most automated site in our global network and has been essential in driving our growth in that region.

We've recently announced that we're in the final stages of the site selection process for another new plant in Brazil while also expanding through a new forest product site in Louisiana. Both expansions should contribute to our earnings in 2016.

Let me now turn the call over to Bill Carter, our CFO, to further discuss our results. Bill?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Thank you, Craig.



Turning to our epoxy, phenolic and coating resin segment, first quarter 2014 revenue totaled \$817 million, a 7% increase on volume gains of 8% and a currency translation benefit of 1%, offset by price mix declines of 2%. Our quarterly segment EBITDA increased by 8 million compared to the prior year as strong gains in oilfield, specialty epoxy and Versatics were offset primarily by cyclical and base epoxy resins. Both the US and EU markets continue to show improvement within EPCD.

Turning to the next slide, in our forest products resin segment, sales totaled \$476 million, an 11% increase with price mix improvement of 9% and volume gains of 7% offset by negative currency translation of 5%. Segment EBITDA gains reflected our operating leverage from higher volumes and our lean cost structure.

We benefited from the continued recovery in North American housing and formaldehyde demand. In Latin America, we saw strong demand from housing, general construction and furniture. We also posted improvement European results due to our past restructuring actions and operating leverage.

Regarding our balance sheet, we continue to benefit from a significant liquidity position with cash plus borrowing availability under our credit facilities of \$624 million as of March 31st. Our capital expenditure investments totaled \$34 million in the first quarter of 2014. We continue to expect to invest approximately \$185 million to \$210 million in CapEx in 2014.

Our networking capital totaled \$608 million at the end of the first quarter, which remained a modest 12% of sales. As anticipated, networking capital increased versus year-end 2014, due to higher volumes from improving demand and seasonality, as well as inflation.

Let me now turn the call back to Craig to wrap up.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Thanks, Bill.

Turning to slide 13, our forest products business posted strong quarterly results due to the continued recovery in the North American housing market and strength in our Latin American business. Our epoxy, phenolic and coatings resin segment reflected strong oilfield, Versatic acids derivatives and specialty epoxy performance partially offset by cyclical and base epoxies.

We continue to make strategic investments in our specialty portfolio as we successfully integrated the Shreveport oilfield acquisition into our portfolio. We've also recently announced construction of a new formaldehyde plant in North America and a new forest products plant in Brazil.

We remain focused on optimizing our cost structure through our productivity initiatives and have achieved \$61 million in cumulative savings from the shared services agreement. Finally, we continue to carefully manage our balance sheet and have a substantial liquidity with \$624 million of cash and available borrowings.

Thanks for your continued interest in the Company. And I'll now return the call to John Kompa.

John Kompa - *Momentive Specialty Chemicals - Chairman of IR*

Thanks, Craig.

Operator, if you could please open the line for questions and remind callers of those instructions.



QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions).

Your first question comes from the line of [Terric Homed], representing J.P. Morgan. Please proceed.

Terric Homed - J.P. Morgan - Analyst

When you look at the epoxy volume growth number of 8% during the quarter, can you sort of, you know, discuss kind of US versus Europe? You know, is the US higher than that 8% and Europe lower or vice versa? Kind of any color you can give us on that?

Craig Morrison - Momentive Specialty Chemicals - Chairman, President, CEO

Yes, generally in those two regions, we've seen roughly similar amount of growth. Both have shown improvement. Asia has generally been weaker, especially on the base side. But, you know, on the specialty side for epoxies, Asia has also showed a nice recovery.

Terric Homed - J.P. Morgan - Analyst

And if you look at the oilfield resins business there, as well, is that also kind of running at a similar number of 8%? Or is that materially higher at this point?

Craig Morrison - Momentive Specialty Chemicals - Chairman, President, CEO

When you look at -- no, that is significantly higher on share gains, as well as there has been some market rebound there, obviously, with natural gas pricing showing some improvement over where it was 12, 18 months ago. So, no, that's significantly higher when you look on a volume year-over-year basis.

Terric Homed - J.P. Morgan - Analyst

Okay, thank you. Then you talked a little bit about the winter weather impact. You guys appear to have done a great job of dodging the bullet. But do you have a number in mind for kind of what the impact was, in dollar terms, during the quarter?

Bill Carter - Momentive Specialty Chemicals - EVP, CFO

Yes, it was not substantial. So, I think it would be in the kind of low single digits, from an EBITDA perspective.

Terric Homed - J.P. Morgan - Analyst

All right. And then just last one for me, on working capital, it's a bit of a high quality problem, just given the volume growth. But any expectations on recapturing some of that growth inventory receivables towards the end of the year, or should we think about it as potentially somewhat sticky, given just the strength of the volumes you guys are seeing?



Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

No, you should think that we will see the trends that we have traditionally seen on working capital. So, to your point, Terric, we will expect it to go up from a perspective of seeing volume go up. But we would expect a significant working capital benefit in the fourth quarter.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Because the other factor is we tend to build at certain times of the year for plant shutdowns, maintenance, et cetera, which is frequently a first, second quarter type issue.

Terric Homed - *J.P. Morgan - Analyst*

Right. And then just one last one for me [before I wrap up], on CapEx, you have your number out there for 2014. Any sort of preliminary thoughts we should build into our models for 2015? Or is that process a little too early?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

I would say that you should consider that we will have elevated CapEx in 2015, as well. So, as clearly as you've looked from 2013 to 2014, you can see it's up. And it's around what Craig discussed, being the additional investments we're making in our forest products business.

Terric Homed - *J.P. Morgan - Analyst*

Got it. Thank you very much.

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Thank you.

Operator

Your next question comes from the line of Adam Goodwin, representing Goldman Sachs. Please proceed.

Adam Goodwin - *Goldman Sachs - Analyst*

Hello, thank you for taking my questions. My first question -- were there any manufacturing related issues during the quarter, similar to what you had experienced in the fourth quarter?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

I don't think -- I think, to kind of the earlier question, we had more issues, I would say, around weather disrupting manufacturing versus any significant outage.

Adam Goodwin - *Goldman Sachs - Analyst*

Okay.



Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

So, it was more weather-related.

Adam Goodwin - *Goldman Sachs - Analyst*

Okay. And then the \$50 million intercompany loan to Super Holdco Finance that was disclosed in your 10-K. Was that already repaid during the first quarter? And then just a broader question, there, as well, would you expect any impact or costs associated with the Momentive performance bankruptcy filing for Hexion, or is that not likely to be the case?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Yes, for your first question, we expect that loan will be repaid probably either end of second quarter or the third quarter. But it will definitely be repaid, we believe, in 2014.

I think on your second question, we don't have any cost that we believe will accrue to Momentive Specialty Chemicals related to the bankruptcy.

Adam Goodwin - *Goldman Sachs - Analyst*

Okay. And where does the intercompany loan show up on the cash flow statement?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Well, actually, for accounting reasons, we -- you'll see that we have re consolidated or consolidated that entity. So, although we're [risk] disclosing we made a loan, the \$50 million continues to show up as an asset on Momentive Specialty Chemicals books. And so, you don't actually see it as a dispersion.

Adam Goodwin - *Goldman Sachs - Analyst*

Got it. And then my last question, in the base epoxies business, is there anything about the way that your plants are configured at Pernis or Deer Park that would prevent you from rationalizing some of that upstream capacity and just seeking to focus more so on the specialty side of the business?

I mean, my own impression of base epoxies is that that business doesn't look like it's going to get much better at any point in the near future. And if you look at the success that competitors like Huntsman have had at restructuring their own businesses -- I just wonder why you guys have been a bit slower to pull the trigger there.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Well, we did announce a plant last year that we had rationalized, which was Wesseling, which is probably similar in size to the Huntsman plant. We continue to look at opportunities to optimize that business. Obviously, we won't discuss anything specifically until we have something -- if we have something formal to announce.

But an ongoing focus of optimizing -- we, I think, have a history of making adjustments where appropriate. Sometimes those things take a little longer than others for various reasons. But when we have something to announce, we'll discuss it. But clearly we always have an ongoing focus on assessing assets and how to optimize.

Adam Goodwin - *Goldman Sachs - Analyst*

Okay, great. Thanks a lot, guys.

Operator

Your next question comes from the line of Roger Spitz, representing Merrill Lynch. Please proceed.

Roger Spitz - *Merrill Lynch - Analyst*

Thanks. Good morning.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Good morning.

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Good morning, Roger.

Roger Spitz - *Merrill Lynch - Analyst*

Drilling down on the base epoxy resins [BPA], can you talk about what your volume change as a percent was in that combined base business versus Q1 2013?

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Volumes on the BPA side and the precursors in general were up in line with the kind of volume increase we saw for the overall business.

Roger Spitz - *Merrill Lynch - Analyst*

You mean BPA was up on the 8% level?

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

No, I apologize. I was misspeaking. I was looking at the wrong page.

It was actually down on a year-over-year basis -- I apologize -- for the precursors in general.

Roger Spitz - *Merrill Lynch - Analyst*

Which is...



Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

BPA, ECH.

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Yes, it was up sequentially from the prior quarter, but down versus the prior year.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Yes, I was looking at the wrong column.

Roger Spitz - *Merrill Lynch - Analyst*

Right. When you say volumes on ECH, I thought you were barely in the merchant market. Are you referring to what you're using internally? Or (multiple speakers) --

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

I'm just saying [we are] -- for the pages we have, we consolidate our precursor volumes. So, it would largely be driven by the BPA numbers. But the ECH numbers are in there, as well.

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Right. We're working in and out of the ECH market --

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Yes.

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

As we have excess. But you're right, it's [the bulk] --

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

It's largely going to BPA. So, you can take it as a largely BPA-based number. Down year-on-year, up quarter-over-quarter.

Roger Spitz - *Merrill Lynch - Analyst*

And how about LER volumes year-over-year?

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Down slightly, call it low single digits on a year-over-year basis.



Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

And up sequentially.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Yes.

Roger Spitz - *Merrill Lynch - Analyst*

Okay. And can you comment in terms of looking at those three together or breaking it apart however you want -- again, not hard numbers on EBITDA, which I know you don't want to provide -- but looking year-over-year on EBITDA, are we sort of flat versus Q1 or is it falling off still?

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

On a combined [Barry] basis, which is our base epoxies, which combines all of that, it's actually on a prior quarter basis. And part of this is seasonality. It's improved. So, we kind of consider ourselves at the low point in the trough. So, on a prior quarter basis, it's improved.

Roger Spitz - *Merrill Lynch - Analyst*

Okay. Last question on the [pond fuses], do you think the issue has been in the industry overall more on oversupply in LER, BPA or [EPI]? I know there's a lot to go around, but where is more of the problem, in your view?

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Well, I think when you look at right now, the oversupply in the LER is a very significant problem. And obviously, Asia's the driver there; and the ability to export into Europe and North America -- I'd say that's the biggest genesis of the problem right now.

Roger Spitz - *Merrill Lynch - Analyst*

Great. Thank you very much.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Thank you.

Operator

Your next question comes from the line of Brian Chavarria representing Credit Suisse. Please proceed.

Brian Chavarria - *Credit Suisse - Analyst*

Good morning, gentlemen.



Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Hello, Brian.

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Hello.

Brian Chavarria - *Credit Suisse - Analyst*

Just looking quickly at the cash flow statement, was the Shreveport the only facility that was purchased during the quarter? Because that \$52 million -- is that all just basically the cost of that Shreveport facility?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Yes.

Brian Chavarria - *Credit Suisse - Analyst*

Okay, got you. And it also looked like you guys are increasing in your adjusted EBITDA number -- the amount attributed to that facility. Is that just as you get a better handle on that, or can you give some more color? I would have thought that as you already had some impact in 1Q, that that --

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Yes, that's really just continuing to fine tune the number.

Brian Chavarria - *Credit Suisse - Analyst*

Okay.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

I think, yes, as we look at it, we're actually finding synergies, more opportunities than we had originally thought on reformulation; greater efficiency of process capability, et cetera. So, we continue to refine the number.

Brian Chavarria - *Credit Suisse - Analyst*

Got you. So, that looks like a very good acquisition, then for you guys.

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Yes.



Brian Chavarria - *Credit Suisse - Analyst*

Once that gets up and running fully. And then I guess turning over to -- I don't know if you want to comment on this at all, but second quarter, how that's looking, at this point. We're kind of halfway through. Are you continuing to see these positive trends on the specialty kind of epoxy side, and how is kind of forest products looking with the housing?

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Yes, I'd say in general, we feel there's more of a positive balance as we move into the second quarter. Europe is continuing to show, I think, some rebound. The US is -- obviously housing was a little weak in the first quarter, given the weather and some interest rate expectations, et cetera. But in general, we see the quarter as a more favorable trend, so that would be directionally how we'd look at it.

Brian Chavarria - *Credit Suisse - Analyst*

Got you. And then just touching back on Terric's point from earlier, regarding kind of working capital and just trying to think through that as well as kind of the CapEx ramp-up through the year, when do you kind of -- I guess order of [magnitude], do you have any sense of what second quarter working capital outflow could look like? And when do you see yourself kind of hitting the low point, in terms of your liquidity for the year? You guys certainly [sell] a lot, but just trying to --

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Yes, I think second quarter, we would expect it to be a usage of working capital, but a much smaller magnitude. So, something, I would say, kind of a quarter of what we used in the first quarter, or slightly less. We expect small usage in third quarter and then a significant recapture in the fourth quarter. And that is, again, to my comment, similar to kind of prior year seasonality, because typically, we're a large generator in the fourth quarter.

Brian Chavarria - *Credit Suisse - Analyst*

Okay, that's helpful. Thank you very much.

Operator

Your next question comes from the line of [Richard Cass], representing Jefferies. Please proceed.

Richard Cass - *Jefferies - Analyst*

Hello, guys. Good morning.

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Morning, Richard.

Richard Cass - *Jefferies - Analyst*

Just quickly, on the price side in the forest products business, you guys showed nice year-over-year gains there. Can you break that down a little bit into your various markets and kind of give a little bit more color on where that's coming from?



Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Yes. I mean, we had a nice step up in line with the overall step up in the North American market. In that particular case, it was largely driven by our formaldehyde business because resins was a little bit weaker, based on the fact that housing [starts] were down and the weather really did affect customer plans, largely from a distribution standpoint, and getting shipping and trucking around.

We also, when you look at Latin America, had very, very nice growth that was significantly higher than the overall business' growth, as well as we also had very high growth, although it's on a lower EBITDA percent basis, in Europe.

So, in general, all of our markets were performing quite well and contributed to the year-over-year improvement.

Richard Cass - *Jefferies - Analyst*

Okay. And it doesn't sound like there's any expectation for that to change in the near term here.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

No, we continue to see not just on a quarterly basis, but as you look out and you look at housing starts and where they're at right now in North America, compared to the historical norm, [we've got] \$1.5 million right now; we're about a million. So, we consider the next few years to be looking quite positive.

Latin America continues to be overall very positive market and we don't see a change there as we see our customers continuing to build. And we're building just to try and stay up with them. So, overall, we consider it a positive environment.

Richard Cass - *Jefferies - Analyst*

Okay, very good. And just lastly for me, can you quantify the contribution from the acquired Shreveport facility in the quarter?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Yes, I think we, from a perspective of on a run-rate basis, this year, we'll get a partial contribution, obviously, in terms of ramp-up. But we would expect it to be somewhere north of \$20 million, in terms of EBITDA, eventually moving up from there over the next couple of years.

Richard Cass - *Jefferies - Analyst*

Okay. And it's safe to say you're kind of below that run-rate contribution-wise in 1Q?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Correct.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Yes, in Q1, it was pretty much flat.

Richard Cass - *Jefferies - Analyst*

Perfect. Thank you.

Operator

Your next question comes from the line of James Finnerty, representing Citi. Please proceed.

Unidentified Participant - *Citi - Analyst*

Hello, this is actually [Jesse] on for James. Just had a quick question on your thoughts on methanol prices, given supply additions. Do you guys have an outlook for 2015?

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Yes, again, we're reflecting really what we're seeing -- the prognosticators. And generally, it obviously has gone through a fair period of spiking and we consider it to be a favorable trend through the remainder of this year heading into next year.

This year will be projected significant declines in virtually all regions of the world. And the next year, they're projecting flat. But in all candor, I think what you find is that tends to be that further out, people just project flat in generally because it becomes a little more difficult -- the volatility in the world [contains] that pretty quickly. But we consider that a fairly favorable raw material market right now on methanol.

Unidentified Participant - *Citi - Analyst*

Got it. Thank you.

Operator

Your next question comes from the line of David Troyer, representing Seaport. Please proceed.

David Troyer - *Seaport - Analyst*

Good morning. Most of my questions are follow-up.

Bill, I heard your explanation on the restricted purpose loan -- how because of consolidation, it doesn't run to the cash flow statement. But I guess I'm not sure that I follow. I'm trying to reconcile the decline in cash -- or maybe more accurately, kind of the increase in net debt, which includes cash, between year-end and quarter-end; and working capital is a big component of that, the acquisition's a big component of that. But would \$50 million of the loan be in that bridge or not be in that bridge?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

So, it would not be in the bridge, although the money -- when we made the loan, the cash was moved to the subsidiary of our holding company. We did consolidate that subsidiary; it was the variable interest entity rules. So, we re consolidated that cash.



David Troyer - *Seaport - Analyst*

Okay.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Yes, David, if you think about reconciliation, too, from the cash flow statement, working capital was a use of \$126 million. We had the acquisition of \$52 million and then we had cap expenditures of about \$34 million. So, that's really [about a] decrease in cash of about \$180 million.

David Troyer - *Seaport - Analyst*

Okay. And then I suppose that the consolidation also explains why, when looking on the asset side of your balance sheet, I don't see this loan either?

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

That's correct.

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Right. Because when we consolidated it, we eliminate the intercompany loan.

David Troyer - *Seaport - Analyst*

Okay. And then that entity that is consolidated, it's merely an asset to loan and a liability to loan? There are no other assets and liabilities?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

No, that's correct. It was a special purpose entity set up only for that transaction.

David Troyer - *Seaport - Analyst*

Okay. Okay, thank you. Then a follow-up question on the Shreveport acquisition. You know, \$22 million or call it kind of low 20s of EBITDA potential for \$52 million -- I, too, want to congratulate you on a tremendous acquisition. Or to achieve synergies -- to achieve full utilization -- is there some level of spending that's material that needs to happen to realize [those]?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

No, I wouldn't say there's anything material. To Craig's point, I think he mentioned it in terms of there was certainly some minor amounts of capital, in terms of configuration of the facility. But there was no major material CapEx related to the acquisition.

David Troyer - *Seaport - Analyst*

Okay. That's all I had. Thank you.



Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Thank you.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Thank you.

Operator

Your next question comes from the line of Frank Longobardi representing Alcentra. Please proceed.

Frank Longobardi - *Alcentra - Analyst*

Hello, good morning. I just wanted to follow-up on two questions -- one from Roger about the base epoxy business. If I heard you correctly, you said volumes kind of overall for base epoxies were down year-over-year but the EBITDA was generally slightly up year-over-year? So, I just wanted to know what's kind of driving that; is it just cost savings or structuring, or maybe some reconciliation? That would be helpful.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Yes, just a point of clarification, the base epoxy improved on a quarter-over-quarter basis and was slightly worse on a year-over-year basis. So, I think we're throwing out two different numbers there.

Frank Longobardi - *Alcentra - Analyst*

Right, but then I think you said that the base epoxy EBITDA was improved year-over-year on volumes that were down year-over-year.

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

No, I think the same trend is EBITDA improved sequentially from prior quarter to current quarter, but was down this year versus last year.

Frank Longobardi - *Alcentra - Analyst*

Okay, that makes more sense.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

[Both cases], we saw sequential improvement, but declined versus prior year.

Frank Longobardi - *Alcentra - Analyst*

Okay, just wanted to clarify that. Thank you.

And then following up with Brian's question about kind of the second quarter outlook -- can you comment specifically about base epoxies, in terms of the trends there? Will you continue to see a sequential improvement?



Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

When you look at the markets in general, we're seeing North American demand pick up and a little bit more pricing power there. In terms of Europe, we're seeing volumes pick up but we're also seeing imports still very problematic. And when you look at Asia, we're not seeing any real improvement, as it's still awash in excess capacity.

So, we're not seeing a significant improvement yet overall in the base epoxy profitability. There might be a small marginal improvement, but we're not seeing that significant shift that we'd like to see and have seen in the past.

Frank Longobardi - *Alcentra - Analyst*

So, I mean, sequentially, could we see kind of maybe just flatten -- expect it to be kind of flat-ish from prior quarters?

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

I think if you assumed flat, it would not be far off.

Frank Longobardi - *Alcentra - Analyst*

Great. Thank you.

Operator

Your next question comes from the line [Maryann Kirschner] representing [Numara] Asset Management. Please proceed.

Maryann Kirschner - *Numara Asset Management - Analyst*

Hello -- a few more on epoxies. There were a number of announcements of the intentions to rationalize capacity. I think those discussions started kind of mid-last year. And I'm just curious if anything was actually done.

And also, what are the operating rates currently, versus last year? And in terms of the new capacity additions, which I understand are still ongoing, what is happening there, if you could clarify that?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

In terms of announcements on the past year rationalization, you may -- Craig earlier had mentioned we had closed a plant in Europe last year, and I'm not sure if that's what you're referring to. We have not announced any other rationalizations of the [past year].

Maryann Kirschner - *Numara Asset Management - Analyst*

I'm talking about industry overall.

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Oh, overall?



Maryann Kirschner - *Numara Asset Management - Analyst*

Right.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Yes, I mean, other than there's a couple of smaller facilities that have been discussed, I can't really speak for competitors and what their current status is on those facilities. Obviously, there was the Huntsman announcement, et cetera. But the general status -- we don't see a significant step function change in demand capacity right now, in terms of the capacity component. And again, Asia continues to be problematic.

Maryann Kirschner - *Numara Asset Management - Analyst*

Okay. All right. Another question, then, different from the epoxy question, is what are the expected cash restructuring spending this year? And generally, at which point do we kind of run the business without any additional restructuring spending?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Yes, I think in terms of restructuring spending, we have in the footnote to our Q, which you will see, the impacts of, certainly in the first quarter, around business realignments and description of what those are. I think in terms of when we won't have any more of that, I think it is, to a certain extent, an ongoing part of our business that we, as Craig said, whether it's the epoxy business or other businesses, we continually look at our plant footprint in our portfolio and we continually look for opportunities for productivity and cost takeout.

So, I think that we would expect, over time, to continue to operate more efficiently. And that will undoubtedly result in some business realignment and/or costs associated with rationalizing our manufacturing network.

I think interestingly, as we look, that was one of the hallmarks of our forest products business where we took down a number of plants in the midst of the housing downturn -- took restructuring charges for those plants, but have ended up with a much more efficient plant network and much higher leverage, as we've seen volumes come back significantly. And that has been a big component of the success of that division -- is operating in a very efficient environment which, at the time, caused us some restructuring money, but is certainly paying off today.

Maryann Kirschner - *Numara Asset Management - Analyst*

Okay, thank you.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Thank you.

Operator

Your next question comes from the line of Jordan Hollander, representing Deutsche Bank. Please proceed.



Jordan Hollander - *Deutsche Bank - Analyst*

Hello, guys. I just had a question on the kind of long-term kind out outlook for the margin at the epoxy, phenolic and coating resin segment. Margins were up slightly year-over-year; looks like specialty is growing. Do we expect that trend, I mean, as specialty becomes a bigger piece of the pie, do we expect margin expansion there? And just how do you kind of think of that overall for the next year plus?

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Yes, I think our projections would indicate margin expansion. If you look at some peak periods in the past where there were some more favorable cyclical trends around [Barry] and some of the specialty markets, which I think are returning now -- Barry's not, but the specialty markets are. That business operated 7%, 8% EBITDA points higher than is currently operating. I'm not saying it would go back exactly to that number, but directionally, I think it would indicate that we continue to project a more favorable environment on margin.

Jordan Hollander - *Deutsche Bank - Analyst*

Okay. And just secondly, just a follow-up on kind of your comments on the housing market, I know you said first quarter there was some weather impacts, some interest rate impacts; are we seeing any slowing of the growth going forward from some of the interest rate factors, or just still that steady kind of uptick over the next medium term here?

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Yes, I think as has been in the press and places, there was some slowdown in the first quarter attributing to that, as well as the weather. How much each one contributed is a little more difficult to know.

But we see, in general, a positive environment going forward. And obviously external events can always happen -- interest rate changes, things that you don't know about for sure. But we think the general environment remains positive for that market overall.

Jordan Hollander - *Deutsche Bank - Analyst*

Okay, great. And then the last one for me, just tied to the intercompany loan, will there be any cash impact [to you guys] when that gets paid off, or to the operating company?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Well, the loan will be repaid, so the cash will come back to Momentive Specialty Chemical upon the repayment of the loan. Does that --

Jordan Hollander - *Deutsche Bank - Analyst*

Yes.

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Is that what you mean? Yes. I mean, so that cash went out; it will come back.



Jordan Hollander - Deutsche Bank - Analyst

Okay, great. Thank you.

Operator

(Operator Instructions).

Your next question comes as a follow-up from the line of Roger Spitz representing Merrill Lynch. Please proceed.

Roger Spitz - Merrill Lynch - Analyst

Thanks. Regarding your merchant formaldehyde business, does this business track your overall segment geographic sales, or are you mostly in just a North American formaldehyde merchant market?

Craig Morrison - Momentive Specialty Chemicals - Chairman, President, CEO

By far, our largest market is North America. It's very much a North American-based business. And obviously, the environment with shale gas, et cetera and the [builds] that have been going on related to that, methanol, et cetera, are very, very favorable for us. So, we continue to have a very positive outlook on the formaldehyde business.

We are continuing to expand that business into Latin America, as well. It's a very attractive business from an EBITDA standpoint and a margin standpoint.

Bill Carter - Momentive Specialty Chemicals - EVP, CFO

And we do have a merchant position in Europe, as well. To Craig's point, North America is much larger.

Roger Spitz - Merrill Lynch - Analyst

Okay. So, the merchant position in Latin America is small or nonexistent. However, with the new facility, you'd want to grow the merchant formaldehyde business position. Is that the way for us to understand that?

Craig Morrison - Momentive Specialty Chemicals - Chairman, President, CEO

Yes, we're seeing demand growing. And there's a lack of capacity to fill that demand. So, we're looking to enter that void and expand our position there, as it is a very attractive market to be in.

Roger Spitz - Merrill Lynch - Analyst

Great. And this is a covenant question, if you want to answer it. Regarding the 6.25% first lien bonds, what kind of first lien capacity might you have if you want to refinance your subordinated debt at that level?

Bill Carter - Momentive Specialty Chemicals - EVP, CFO

George, do you want to take that? I know we have --



George Knight - *Momentive Specialty Chemicals - Senior VP and Treasurer*

Yes, I mean, we have some capacity, Roger. But I don't think we're in a position to comment on that right now.

Roger Spitz - *Merrill Lynch - Analyst*

Okay. Thank you very much.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

Thank you.

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Thank you.

Operator

Your next question comes as a follow-up from the line of Frank Longobardi, representing Alcentra. Please proceed.

Frank Longobardi - *Alcentra - Analyst*

Hello. Just in line with that last question, are you able to comment and tell us what your current restricted payment capacity is at the moment?

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

No, I don't think we will comment on that.

Frank Longobardi - *Alcentra - Analyst*

Okay. Thank you.

Operator

There's no further questions at this time. I would now like to turn the call back to Mr. Craig Morrison for closing remarks.

Craig Morrison - *Momentive Specialty Chemicals - Chairman, President, CEO*

I'd like to thank everybody for participating in today's call and we look forward to updating you at the end of the second quarter. Have a good day.

Bill Carter - *Momentive Specialty Chemicals - EVP, CFO*

Thank you.



Operator

Thank you. Ladies and gentlemen, thank you for your participation in today's conference. This concludes the presentation. You may now disconnect. Good day.

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