Hexion Inc. (Q1 2018 Earnings)

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Corporate Speakers:

- John Kompa; Hexion Inc.; VP of IR & Public Affairs
- Craig Rogerson; Hexion Inc.; Chairman, President, & CEO
- George Knight; Hexion Inc.; EVP, CFO & Director
- Joseph Bevilaqua; Hexion Inc.; EVP & COO

Participants:

- Nathan Schubert; JP Morgan Chase & Co.; Analyst
- Roger Spitz; Bank of America Merrill Lynch; Analyst
- James Finnerty; Citigroup Inc.; Analyst
- Karl Blunden; Goldman Sachs Group Inc.; Analyst
- Brian Lalli; Barclays Bank PLC; Analyst
- Richard Kus; Jefferies LLC; Analyst
- Juliano Torii; Descartes; Analyst
- Svetoslav Nikov; Cyrus Capital; Analyst
- Tim Raeke; Alcentra; Analyst
- David Troyer; The Seaport Group LLC; Analyst
- Unidentified Participant

PRESENTATION

Operator: Welcome to the Hexion First Quarter 2018 Earnings conference call.

(Operator Instructions)

As a reminder, this conference call is being recoded.

I would now like to turn the conference over to your host, Mr. John Kompa, Investor Relations for Hexion.

John Kompa: Thank you, good morning, and welcome to the Hexion Inc. First Quarter 2018 Conference Call. Leading today's call will be Craig Rogerson, Chairman, President and CEO; George Knight, Executive Vice President and Chief Financial Officer; Joseph Bevilaqua, Chief Operating Officer; and Mark Bidstrup, Senior Vice President and Treasurer.

As a reminder, this call is also being webcast, and the slides referenced in today's conference call are available through the hexion.com website under the Investors Relations section. A replay of this call will be available for 1 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 any forecasts or estimates, 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 see 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 in our website. Our earnings release and our recent SEC filings are available on the Internet at hexion.com.

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

Craig Rogerson: Thanks, John. Good morning, everyone, and thank you for joining our call today. I'm pleased to report a strong quarter with a positive inflection point in our segment EBITDA growth, reflecting our diversified portfolio, leading technologies and lean cost structure.

In the first quarter of 2018, we drove strong top line and segment EBITDA gains of 9% in 24%, respectively. Segment EBITDA reflected continued strong demand and year-over-year gains in our basic epoxy resins, phenolic specialty resins and broadly throughout our Forest Products Resins and global formaldehyde businesses. Adjusted for the sale of our Additives Technology Group business in January 2018, our segment EBITDA increased year-over-year by 26%.

As previously announced, we continue to reduce costs throughout the organization and identified $40 million of new structural cost savings in Q4 of last year. In the first quarter, we realized $13 million of savings and $39 million of in-process savings at quarter-end. At this point, we've completed nearly all of the actions necessary to realize this benefit, and the full run rate impact will essentially all be realized by year-end 2018.

After a strong start to the year, our outlook remains positive, and we continue to expect that our cost savings, along with continued growth across most product lines, will continue to drive improved segment EBITDA in 2018.

Now turning to Slide 5 in our combined raw material index.

Our total raw material cost increased 9% on a sequential basis in the fourth quarter. We've seen inflation for two of our major raw materials as the average price for methanol and urea increased on a year-over-year basis in the first 3 months of 2018 compared to the first 3 months of 2017 by 10% and 3%, respectively.

The average price for phenol decreased by approximately 3% in the quarter compared to the prior year period. We'll continue to closely monitor raw material trends and implement any strategic pricing actions as needed throughout the year.

Turning to Slide 6. We've highlighted a few drivers of our strong first quarter growth.

The industry is expected to remain balanced as no significant planned capacity is expected to come online. Over the next few years, we see epichlorohydrin and BPA tightening, which is driving expansion in liquid epoxy resin pricing.

In our LER business, we continue to see favorable industry dynamics, which are expected to remain so for the foreseeable future, supporting continued profitability.

In addition, global capacity is expected to remain tight as environmental regulation curtails Chinese production.

Finally, we believe our backward integration and global base epoxy manufacturing network is a key differentiator for us as it supports our downstream specialty epoxy business.

Our specialty epoxy resins business remains well positioned due to our differentiated technology and favorable secular trends in renewable energy and eco-friendly products.

Turning to Slide 7. I've highlighted the continued growth in our waterborne coatings business and provided an update on our oilfield business.

Our specialty epoxy resins business remains well positioned due to our differentiated technology, and our next-generation waterborne coating system also supports long-term growth in this business. The majority of the recent growth has been driven by Chinese regulations requiring the use of waterborne coatings for shipping containers.

We anticipate that additional regulations will drive new coating applications in other end markets. To continue to meet customer demand in our waterborne coatings business, we brought on additional capacity in January and expect to add more capacity midyear.

We're also pleased by the market reaction to our new Voyager mobile resin coating service. Initially located in the Permian Basin, the innovative Voyager service is the first mobile manufacturing solution that provides in-basin resin-coated proppant manufacturing for application in the oil and gas industry. For our customers, this new approach provides quicker delivery and more cost-effective delivery of resin-coated proppants.

While -- with transportation being a major cost associated with the use of proppants, freight costs are significantly reduced by the ability to locate coating capacity in close proximity to areas of high drilling and completion activity. The new Voyager unit has been well received by our customers and drove significantly improved U.S. volumes in Q1 '18.

Turning to Slide 8.

We continue to drive our structural cost reduction initiatives. As previously announced, we identified $40 million in savings in late 2017, with about 90% of them related to headcount reductions. By the end of the first quarter, we've taken nearly all the actions required, and the full year run rate will essentially be realized in 2018. We remain focused on achieving our remaining in-process structural cost savings, which we expect to further support our improving segment EBITDA margins.

I'll now turn the call over to George Knight to further discuss our financial results.

George Knight: Thank you, Craig. In our Forest Products Resins segment, first quarter 2018 revenue totaled $406 million, a 7% increase from the prior year, reflecting positive price/mix of 7% and favorable currency translation of 2%, partially offset by slightly lower volumes due to weather-related customer shutdowns and the impact of dispositions. Revenue increased in all regions where we operate.

Segment EBITDA increased by 10% and was higher year-over-year in all regions, supported by higher volumes in our Latin America and European businesses as well as cost efficiencies from the new North American formaldehyde facilities. Adjusted for divestitures, segment EBITDA rose 12%.

Turning to the next slide, in our Epoxy, Phenolic and Coating Resins segment, first quarter 2018 revenue totaled $540 million or a 10% increase from the prior year, reflecting positive price/mix of 7% and favorable currency translation of 8%, partially offset by volume declines of 5%.

Segment EBITDA increased by 35% compared to the prior year, reflecting significant increases in our base epoxy resins and our phenolic specialty resins businesses as well as strong volumes from waterborne coatings.

Regarding our balance sheet. Our cash plus borrowing availability under our credit facilities was $282 million as of March 31, 2018. In terms of optimizing our portfolio, we successfully completed the sale of our ATG business in January for 12x segment EBITDA, which generated $49 million in proceeds.

We also previously announced that we were pursuing the sale of a portion of our Epoxy, Phenolic and Coatings Resins segment, and that process is continuing although we are not commenting further at this time. We invested $25 million in capital expenditures in the quarter and continue to expect to invest between $80 million and $90 million in 2018.

We continue to focus on appropriately managing our working capital. We expect working capital to increase only modestly in 2018 compared to the prior year, with an increase in the first half of the year and a decrease in the second half, consistent with historical trends.

I'll now turn the call back to Craig.

Craig Rogerson: Thanks George. In summary, our outlook remains positive for the majority of the key end markets we serve. We continue to expect improved segment EBITDA in 2018 compared to prior year due to the anticipated growth across most product lines, a lean cost structure, our diversified product portfolio and global manufacturing footprint.

Operator, that concludes our prepared remarks. We'd like now to open the lines for questions.

QUESTIONS AND ANSWERS

Operator: (Operator Instructions)

Our first question is from the line of Nathan Schubert with JPMorgan.

Nathan Schubert: Firstly, just on base epoxies. Both as an organization and as an industry, can you talk about where operating rates were during 1Q as well as today and how that compares with last year? And then just a clarification for me.

Are you fully backward-integrated in the epi in The Netherlands? And if not, how much are you buying? And then just finally, can you comp kind of 2018's start so far versus 2011 in which you had a pretty strong year in base?

Craig Rogerson: Jody, you want to handle that one?

Joseph Bevilaqua: Sure, no problem. There are a number of questions in there. Let me just start with depending upon where you are in the value chain for epoxy, they're running at different loadings or utilization rates. So you just think about liquid epoxy resin, that number is probably still in the 70s, 70% utilization.

There's ample availability to bring on more capacity. The tightness really is around ECH and slightly less so in BPA. The other part of the question on 2011, I didn't quite understand, though.

Nathan Schubert: Yes. I mean, I guess just in terms of where you're at in terms of earnings power 2018, thus far, how does that compare, favorably or unfavorably, to 2011?

Joseph Bevilaqua: It will be another very good year. Different dynamics in each group each year, but I'd say we're on a favorable trend to match that.

Nathan Schubert: Great. And then just secondly. Can you talk about where you're at in terms of wind, specialty and proppants on a year-over-year basis? Were those segments stronger, flat or down? And then what kind of drove the lower volumes in the [EPCR] segment?

Craig Rogerson: Go ahead, Jody.

Joseph Bevilaqua: Another series of questions in there.

Craig Rogerson: Wind.

Joseph Bevilaqua: Yes, the wind piece continues to be really driven by China; the lower numbers or slightly lower numbers in Europe as well. The U.S. is doing pretty well. We continue to believe that wind is the low-cost option for green. It's slightly lower than installed cost for solar but still very positive.

We've talked to you before about grid connections in China and how that does bump along a little bit once it had too much inventory and tried to reconnect to the grid. We think those numbers are going to continue to be favorable and grow and particularly as battery technology develops and the story this year becomes less and less of an issue relative to the return on investment. The proppant question, I think we were stuck in there, please.

Nathan Schubert: I just was trying to calibrate where the other moving parts in EPCR were this year so far.

Craig Rogerson: Okay.

George Knight: Yes. From a volume standpoint, I think your question was, Nathan, the volume was down year-on-year on specialty epoxy on the wind side. As Jody talked about, we're up in waterborne coatings, but wind was down. And then in some of our other businesses there, with some of the raw material price increases we saw at the end of last year and some of the pricing actions we took, we were trading off some volume for pricing in Q1 in some of our other specialty businesses there.

Operator: Our next question comes from the line of Roger Spitz with Bank of America.

Roger Spitz: First, maybe just a reset on this in terms of contracts. When I think about base epoxies, what percent of volumes do you sell are made pursuant to contract? And of those, what are the prices contractually indexed? And how often do those change with the index?

Craig Rogerson: Yes, less than 50% of our liquid epoxy resin volume is contracted, and we use various markers to gauge prices, both contract and noncontract. But all of the large contractors -- all contracts would have some market-based calculation.

Roger Spitz: All right. In terms of BPA, are you just -- you're no longer, and haven't been for a long time, I take it, selling BPA. And I don't think you sell any material amounts of epi. If that is true, how much of that now do you buy versus make internally for your LER for both BPA and epi?

Craig Rogerson: We're still a merchant supplier in BPA markets, so we do have volume. It depends on turnaround schedules and such month to month. But we are still a merchant player in BPA in North America. And you're correct, we don't have any epi business anymore once we closed the Norco facility that we spoke about a bit more than a year ago. And roughly, you can think that we self-serve probably in the range of 70% of our total epi requirements.

Roger Spitz: And how much BPA do you sell on average?

Craig Rogerson: It really goes up and down a bit. And I wouldn't want to put a rated basis to it.

Roger Spitz: And lastly, on this one. On LER, how much do you sell of LER versus use internally downstream?

Craig Rogerson: The bulk of what we produce in LER is sold.

Roger Spitz: Over 50% is sold, okay. Or bulk, okay.

Craig Rogerson: The bulk of it.

Roger Spitz: The bulk of it. And also, on specialty epoxy resins, Versatic Acids, oil has been going up, base epoxy has been going up. Can I assume that spreads in specialty epoxies and Versatics have gotten squeezed on that? Or have they been able to move up pricing, though perhaps not as fast as raws have gone up?

Craig Rogerson: Yes, the--

George Knight: Yes, that's the case, Roger, we've been aggressively pricing in both, but we haven't fully covered the increase in raws in Versatics and some of the specialties.

Operator: Our next question comes from the line of James Finnerty with Citi.

James Finnerty: On formaldehydes, I'm sorry, but this is a -- what's the progress in terms of getting towards the $30 million to $35 million of EBITDA you were targeting there?

George Knight: Yes, in our North America plants, we've exceeded our targets there. As we talked about in Latin America, while the plant is running from an efficiency standpoint, we still have some additional capacity, so we haven't realized the majority of those savings yet in Latin America.

James Finnerty: So as of '17, you had about $17 million of EBITDA. So on an LTM basis, has that improved upon that?

George Knight: Yes, it's probably approximately $20 million on an LTM basis.

James Finnerty: And the expectation is still $30 million to $35 million? Or could it be more given that you're exceeding on the North American side?

George Knight: No, that's still our expectation. We still have to realize the piece down in Latin America. I'll add--

Craig Rogerson: I was just down there. We're optimistic that that's coming in the midterm at some of the rationale for why that plant was built, and some of our customers down there were impacted by the slowdown in the Brazilian economy are now much more bullish. So I'm optimistic as we go into second of this year and then more so into '19 that we'll get closer to the full realization of those project numbers.

James Finnerty: Great. And then just on -- back to base epoxy and intermediates. If -- given various numbers at times, $107 million in 2011, $7 million of EBITDA in 2016, and, in the fourth quarter call, you said you were kind of more than halfway there towards that 2011 number, can you just give us an update in terms of where you stand versus 2011?

Craig Rogerson: I think Jody kind of alluded we're closing in. So put it that way. It's continued to improve dramatically as we go into 2018, and we've got expectations that's going to continue in '18 and at least into the midterm.

James Finnerty: Okay, great. And then just one last one. On proppants, was that business breakeven this quarter or slightly negative? Just any color there would be helpful.

George Knight: Yes, it was slightly negative. But we did close our Brady plant during the first quarter, so we expect to see some improvements throughout the rest of the year from a cost standpoint related to that.

James Finnerty: Oh. And just one other one. Was there any impact from the [furnace] outage in the first half?

George Knight: Nothing material.

Operator: Our next question comes from the line of Karl Blunden with Goldman Sachs.

Karl Blunden: Just a question on the epoxy market and how it's responding to some volume coming back into the market from Owen after a 1Q outage. I don't know if you can comment on that and particularly with regard to overlapping grades. Does it feel fairly balanced? Or what can you tell us?

Craig Rogerson: Jody, you want to do that one?

Joseph Bevilaqua: Yes. I think we're some fairly in balance. There were clearly some short-term tightness driven by the outage. It was a rather long. But we don't see that that's going to have a major impact on a global basis, a restart will have a major impact.

Karl Blunden: Okay. Did you have a sense that they were kind of continuing to sell during that downtime? It's probably the impression that you get from looking at their numbers. But presumably, it suggests that there's not a step-change in how much product is coming to market right now with the outage done.

Joseph Bevilaqua: Yes, you may have more data than I have. There wouldn't be anything that we saw them act any differently in the second -- in the 1st -- start of the year. I mean they've been active.

Karl Blunden: Got you. That's helpful. Just on proppants. What can you tell us there about volume trends? Are those higher year-over-year or significantly higher? Anything just to frame that for us?

Joseph Bevilaqua: Oh, I think uncoated sands continue to grow significantly. I'm sure you see that easily in the marketplace. The resin coated side continues to be a limited number of well completion design using resin coat.

And we think that the total volume is going to continue to increase for sand, and the bulk of that will be in uncoated. And we're not seeing any significant rebound in the use of coated proppants as a percent of the total in the foreseeable future.

Karl Blunden: Got you. And just finally on the wind energy piece, just interested in the momentum there. It sounded like backlogs are being reported up by some of the turbine producers. Is that consistent with your observations? And what do you think the time lag might be before you start feeling some positive uptick there?

Craig Rogerson: Well, it would be consistent with our lower volumes here these last few months, so I'd say that's directionally correct. And I'm not sure that we could give you any really insight relative to the connection and where the connections are currently in place or how many, if you will, blades are on the ground in China at this point. We're not sure.

Operator: Our next question is from Brian Lalli with Barclays.

Brian Lalli: Just a couple for me. Maybe on the epoxy business. Could you help us, I guess, calibrate how much of a quarter-over-quarter benefit was driven by your cost saving actions? Just trying to make sure we understand where those additional savings in the future will flow through.

George Knight: Yes. Quarter-over-quarter, costs were probably $3 million to $5 million. The majority of the benefit really related for the improved margins. Yes.

Brian Lalli: So $3 million to $5 million benefit on a quarter-over-quarter basis?

George Knight: Yes.

Brian Lalli: Got it, cool. And then speaking of any [BCRs]. Is there any way to frame, I guess, how much raw materials were a headwind in 1Q relative to the success you had on price and mix? Just again, frame up how much of your index is kind of flowing into 1Q versus what you might get back going forward.

Craig Rogerson: So you're asking basically what the lag is if there is one?

Brian Lalli: Yes, that's -- yes, correct. Yes, that's right.

George Knight: Yes, I think we recovered the majority of the price increases that we saw in Q4 there. So there's really not any remaining lag that's going to see a benefit for going forward there. So we've been pretty proactive on the pricing side, and we've -- most of that has come into our numbers.

Brian Lalli: Got it. I didn't know if anything that has happened in 1Q in terms of higher raws was still impacting you and you would have to get it back on going into 2 and 3Q, some of them.

Craig Rogerson: There was a lot. The majority was Q4 that we got in Q1.

Brian Lalli: Okay, got it. And then my last one. Just, and I know it's a small item, but just on SG&A. It looks like it's up just a little bit quarter-over-quarter. Obviously, you've had of cost saving commentary. Can you just help us think about maybe what that is on a run rate? I know you have about $7 million in your cost saving target.

George Knight: Yes. Right. So on the SG&A side, it was a couple of things. $1 million of it or $2 million of it was related to the new pension pronouncement there, where all the components of pension expense goes down to nonoperating now. So we lost the return on investment portion of the pensions.

So that was $2 million. Also, with the exchange rates up, just our foreign expenses just translated into higher numbers as well as the impact of just the normal merit and inflation increases there.

Operator: Our next question is from Richard Kus with Jefferies.

Richard Kus: Just a couple of quick ones. So on that $13 million of year-over-year cost saves that you guys got, how does that break down by segment and then general corporate?

George Knight: Yes, I don't have that right here. Yes. we'll have to get back to you on that one.

Richard Kus: That's okay. no problem. And then what was the overall currency impact on adjusted EBITDA on a year-over-year basis this quarter?

George Knight: Adjusted EBITDA, it was slightly positive. So we had the increased expenses. But then also, from a business perspective, the stronger euro did impact us. So it was positive by a couple million.

Richard Kus: Okay. And then lastly for me, can you be a little bit more specific about what kind of demand increase you may have seen on the base epoxy side of the business? How much was that up on a year-over-year basis?

George Knight: Jody, you want to take that one?

Joseph Bevilaqua: I'm sorry, I didn't hear the question.

Richard Kus: Yes, I mean--

Craig Rogerson: Just volume increase in base epoxy year-over-year.

George Knight: Yes, I mean, I think volumes were fairly flat. Most of the improvement that we saw on the BERI side was margin related.

Operator: Our next question is from Juliano Torii with Descartes.

Juliano Torii: My question is regarding the cost saving actions. So the way I understand, if you have completed your cost saving initiatives, you're not going to have any further cash restructuring costs for the rest of the year. Is this correct?

George Knight: No. That -- we took the actions as far as notifying the people that were going to be leaving. A portion of those restructuring costs are going to be paid out over time, so we'll continue to have some restructuring costs in the next couple quarters.

Craig Rogerson: So severance is paid out over time.

George Knight: Yes.

Juliano Torii: Okay. And can I have a basic idea of how much do you expect in terms of cash out for that this year versus last year?

George Knight: Yes. I think overall, the restructuring costs for the year should be about $29 million versus last year, it was slightly over $50 million because we closed our Norco facility and we had clean-up and demolition costs related to that as well as severance last year. So it'll be down probably about $16 million year-on-year.

Juliano Torii: Okay. And one last question. Including this cost, do you expect to generate cash after -- free cash flow after the interest this year?

George Knight: Yes, we expect to be slightly better than breakeven this year.

Operator: Our next question is from with Svet Nikov with Cyrus Capital.

Svetoslav Nikov: Just a quick question on forest products. The volumes of the (inaudible) business is negative this quarter after a string of kind of low to mid-single digits for the last few quarters. Can you comment on that?

George Knight: I'm sorry, can you repeat the question?

Svetoslav Nikov: Yes. So forest product volumes were negative 1% year-over-year, and that breaks a string of 6-or-so positive quarters over the last, I guess, 1.5 years. What drove the negative earnings?

Craig Rogerson: And what are the--

George Knight: Yes.

Craig Rogerson: Yes. And one of the things that hurt us early in the year was the extremely cold and snowy weather up in the Northeast and throughout the a lot of the U.S. that slowed things down.

But for the year, there's still the expectation that the forest products business is going to show growth, certainly recognizing the fact that we've started to see some positive inflection point relative to housing starts, with the most recent number being over 1.3 million. So I think, yes, again, I think the first quarter that saw that slight decrease was the anomaly due to weather, and you'll see a pickup as we go on.

Operator: Our next question is from Tim Raeke with Alcentra.

Tim Raeke: I had a question on the proppants business. And I presume the mobile unit is a relatively small percentage of your overall volume, but maybe you can speak to sort of, is there a margin differential there?

And you spoke of the fact that you didn't to see resin coating kind of regaining its share as a percentage of uncoated, and I wonder if you could just kind of maybe big picture speak to the economics of why drillers wouldn't be convinced at $70 oil to maybe switch to coated. I just don't really know the -- what the decision process is in there.

Craig Rogerson: Jody, you want to do that one?

Joseph Bevilaqua: Yes. I mean, working backwards, it's really the depletion curve and the idea that over time, the wells produce less. So the argument is that, that completion strategy for the engineers have shifted towards lots of double, sometimes triple the amount of sand per well, significantly increasing if you were to put that same percent through a resin coke plant and put chemicals on it, arguably 3 to 4x more costly.

And the size of these wells today or just using millions of pounds a lateral length is significantly increasing year by year, so more and more sand. So it's just the general economics or the pure amount that you're putting into a frac job significantly increasing and that premium play for resin coats really got to give you more gas over the depletion curve.

And at this point in time, the last few years, that -- just the data is not significantly supporting the increased cost of resin coat. So pure economics is understandable. And again, you're going to see resin coat continue to improve. I don't think it's going to get back to the high watermark that it was 3 years ago, but you are going to get to see it improve, just not at the rate and I think at the end of the day, the total percent resin coat as a percent of the total is going to be lower than it was in the previous peak.

Craig Rogerson: And Jody, maybe comment on Voyager, where we are now and the advantages for us and for the end user.

Joseph Bevilaqua: Yes, it's like any new startup, right, we're continuing to work on productivity and reliability, maintenance. All those things we're learning an awful lot to get ready for the next wave of investments. Our productivity is improving on a monthly basis.

We continue to believe that elimination of a lot of the freight costs to move material around makes a lot of sense to get this closer and closer to point of origin and really keeping a very good look on the last mile delivered costs. And we still believe this is going to continue to be very beneficial for the market.

Tim Raeke: Okay. And can I ask you a question on forest products, too? You mentioned down volumes in Q1, but you expect to be up for year-over-year. I don't know how to think about the capacity utilization of the forest products plant in North America. Do you have the capacity if housing demand picks up as some people expect? Is it another shift you add? Or you just try to squeeze the plant for more production? Any (inaudible) would be helpful.

Joseph Bevilaqua: Well, I think if the question is that do you believe it's going to go back to pre-highs of 2 million housing starts, of course there'll be capacity issues. But if the current growth rate at relatively GDP types of growth or maybe a bit better, there's not going to be anything in the foreseeable future that would indicate significant tightness of phenolic resin for forest products.

Operator: And our next question is from Nathan Schubert with JPMorgan.

Nathan Schubert: Just a follow-up for me. Can you just remind me about your thoughts around the waterborne coatings market, how big that market is, where you see the growth there and kind of what kind of EBITDA contribution you think that business is capable of once you kind of get to your sort of steady state?

George Knight: Yes, I think from a total market standpoint, right now it's in the--

Craig Rogerson: Shipping container.

George Knight: Shipping container side. So it's about $100 million market size. And the upside for us, we figure, is as the regulations change and we start to see that moving into other sectors like the heavy construction equipment, those types of things. So I think there's a lot of upside as you think about the other types of markets that our waterbornes could spread into.

Craig Rogerson: And one of the keys I mentioned during the scripted comments was we started up a new facility and new lines in January to meet customer demand. And again, we have to set up another tranche of those lines midyear to be able to continue that through the end of the year. And this is really driven by the container coatings at this point.

As the regulations, a lot of which are already in place but just aren't necessarily fully implemented yet, come into play in 2019, '20 and further on, we're going to have to continue to add capacity, and that's kind of our expectation in our capital plan and certainly in our growth numbers. But at this point, we continue to be essentially selling all we can make.

Nathan Schubert: Great. And then just can you give us an update on where you're at with the asset sales? I know you said you're not going to really comment, but have you been productive in your talks? I mean, it seems like the market has been kind of choppy. So just there any incremental color there would be helpful.

Craig Rogerson: As we said, we don't comment. Let me just -- just one thing. It's a normal process. The process is under way. We expect a kind of a normal time line, and I'd say we're where we expected. So everything is moving ahead as planned.

Operator: And our next question is from James Finnerty with Citi.

James Finnerty: Just on the ABL, you drew an additional almost $80 million in the quarter. What's the thoughts with regard to that as the year goes on and the working capital build unwinds? Would you be paying it down? Or is that yet to be determined?

George Knight: Yes, I mean, that fluctuates with our build on working capital. So consistent with prior first quarters with the working capital build, we did see some usage of the revolver. As we said, we expect the working capital to come down in the second half. And correspondingly, with excess cash, we will pay down the revolver as that happens.

Operator: Our next question is from the line of (inaudible) with PSAM.

Unidentified Participant: Could you clarify your comment around free cash flow breakeven to positive for the year? Does that factor in the $50 million in asset sale proceeds that you realized in Q1?

George Knight: Yes, that does.

Operator: And our next question is from David Troyer with Seaport.

David Troyer: Once again, I know you're not going to comment on the specifics of the asset sale. But can you remind us of what some of your many key objectives (inaudible) on the metrics you might look at when you're making a decision whether to sell an asset or not sell an asset? Does it need to be deleveraging? Does it mean to enhance liquidity? It doesn't need to be a philosophical discussion.

Craig Rogerson: Well, and yes, I mean, clearly, deleveraging is a consideration. The absolute value of the debt is a consideration. Liquidity, we think and I think we've got that managed. It's not a requirement. All of these things are enhanced by the continued improvement of the EBITDA, and I think that relative to any refinancing, continued positive evolution of that performance is going to be critical.

But yes, I mean, clearly, we're looking at the maturities that we have in 2020 and looking at this as a way to effectively deal with that while having a company, at the end of the day, that makes a lot of sense, that's got growth potential and is worth continuing the investment.

David Troyer: Okay. And then, Craig, you just brought something up about the liquidity you have at hand. Can you reconcile that comment with what occurred in this quarter? You had one of your stronger EBITDA quarters in, say, 3 years. Seasonally, we'd expect it to be stronger, plus the improvement in the fundamentals. You had an asset sale. Yet liquidity is down over $100 million. I know some of that is the working capital components.

And you'll get some of that back, maybe not all, on a higher raw material environment, but what -- how do you define ample liquidity, particularly in a growing environment where raw materials may have the margin be higher?

George Knight: Yes, I mean, we've operated at different liquidity levels over the years. As far as your comments on the first quarter, working capital went up by almost $100 million. So that's really with the big usage on the working capital side and the liquidity side there. As we disclosed, we've got more than enough liquidity to continue to operate. And the -- as working capital come down, our liquidity will also improve, and we expect to see those improvements the rest of the year.

Craig Rogerson: And my comments around the improved liquidity is based on our expectation and recent performance of improving EBITDA. And clearly, from our overall cash flow, that's the key component, and we continue to expect to see that improve throughout the year.

So I don't want to imply that it's not a concern. We continue to have, liquidity is a continued focus for us, but it's an improving situation. And the proceeds from any significant asset sale aren't considered as part of the improved basket relative to improving liquidity, it's to deal with--

George Knight: The debt.

Craig Rogerson: The debt.

Operator: And I'm not showing any further questions, so I'll now turn the call back over to Craig Rogerson, CEO of Hexion, for closing remarks.

Craig Rogerson: Appreciate everybody's interest. We look forward to talking about another strong quarter in Q2 as we release earnings again after the season. So again, I appreciate your attention and your interest. Thanks.

Operator: Ladies and gentlemen, this does conclude the program. You may now disconnect.

Everyone have a great day.