ICL

Q2 2017 Conference Call

August 3, 2017

Operator: Ladies and gentlemen, thank you for standing by and welcome to the ICL Analyst conference call.

Our presentation today will be followed by a question and answer session, at which time, if you wish to ask a question, you will need to press "star 1" on your telephone. I must advise you that this call is being recorded today. If you experience any technical difficulties, please press "star 0" on your telephone.

I'd like to hand the call over to your first speaker today, Mr. Dudi Musler. Please go ahead sir.

Dudi Musler: Thank you. Hello, everyone. Welcome and thank you for joining our second quarter 2017 conference call. Earlier today we filed our reports to the securities authorities and the stock exchanges in the U.S. and in Israel. The reports, as well as the press release, are available on our website.

For your reference, this meeting is being webcast live at www.icl-group.com. There will be a replay available a few hours after the meeting and a transcript will be available within 48 hours. The presentation that will be reviewed today was also filed to the securities authorities and is available on our website.

Please don't forget to review slide number two with the disclaimer. Our comments today will contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements are based on management's current expectations and are not guarantees of future performance.

We will begin with a presentation by our acting CEO, Asher Grinbaum, followed by Kobi Altman our CFO. In addition, ICL executives are either here or on the line and will be available for questions following the presentation. Thank you all for joining us today, looking forward to talk to you and see you soon. Asher? Please.

Asher Grinbaum: Thank you, Dudi. Good morning or good afternoon to all of you joining this call today.

Let's turn to the summary of the quarter on slide 3. As in the first quarter of 2017, this quarter we continue to deliver on our operational capabilities, as well as on our ability to reduce G&A expenses and to generate strong positive free cash flow despite the challenging business environment we face in some of our businesses. Our Specialty Solutions division performed solidly, mainly its bromine, acid and fire safety businesses, while the business environment in commodity fertilizers, and especially in phosphate fertilizers, remains challenging. Nevertheless, our continued efficiency and operational excellence efforts, combined with our reduced exposure to commodity phosphate fertilizers, resulted in a significant operational improvement at our YPH JV in China. Our financial results were impacted by an increased tax burden in Israel, and as a result of increased financial expenses, mainly due to early payment of a long-term debt. Kobi will elaborate on those shortly.

During the quarter we signed a contract to divest our 50% holding in IDE, another step in our plan to divest low-synergy businesses to further strengthen our balance sheet, reduce debt ratios and support our strategic plans, primarily in our specialty businesses.

Turning to slide 4, as I just mentioned, the business environment under which we operate continues to present multiple challenges. The quarter was negatively impacted by the delay in signing potash contracts in China, declining commodity fertilizer prices – especially phosphates, the strengthened Israeli shekel, rising seaborne transportation costs and the Ammonia shortage in Israel. Nevertheless, I would like to highlight the positive developments which occurred during the quarter:

Our specialty business continued to demonstrate solid performance, we continuously and successfully executed on our efficiency and cost control measures and we demonstrated further significant operational improvement at our YPH JV in China. We are also pleased with the resolution of the Catalan Supreme Court which approved our suggested roadmap for the continued operation of the Sallant potash site, allowing us to operate at the site for one more year, with an option for a second year, until we complete the expansion of our Suria site and consolidate both operations.

While it did not affect the 2nd quarter, we are currently dealing with the unfortunate phosphogypsum event at our Rotem phosphate operations in Israel, about which I will elaborate later.

Moving to slide 5...
Despite lower sales, our Specialty Solutions operating income remained stable. ICL Advanced Additives demonstrated another strong quarter which was driven by higher acid and fire safety sales and our bromine business continued its positive trend, presenting yet another quarter of strong operating profit. The division's decrease in sales is mostly a result of our food businesses being negatively impacted by a dairy protein customer's destocking activity. Nevertheless, the business unit's profitability was almost flat compared to Q2 2016, and partially offset the reduced sales to that customer with increased sales to new and other existing customers. We expect that trend to continue in the second half of the year.

Our Essential Minerals division saw lower sales and operating income on the back of lower commodity fertilizer market prices, the delayed signing of potash contracts in China, and $26 million in insurance income recorded in the second quarter of last year.

Following the recent signing of new contracts to supply 925,000 metric tonnes of potash to our Chinese customers at a higher price than last year, we expect our second half potash sales and operating income to significantly increase over the first half.

(Slide 6) Before I conclude and pass the presentation over to Kobi to discuss our financial results, I'd like to elaborate on the Rotem incident. As you all know, on June 30, there was a partial collapse of a dyke in Pond 3 which is used for accumulation of phosphogypsum water that is created as a by-product of production processes at our ICL Rotem plant.

We immediately ceased our use of the active phosphogypsum ponds and took immediate steps to stop the flow of phosphogypsum water from leaking out of the accumulation pond. I would like to emphasize that we have a history of environmental responsibility and we are committed to taking all measures necessary to rehabilitate the Ashalim dry riverbed.

During the time that has passed since the event, we have worked diligently and in full cooperation with the authorities in order to minimize damage to the Ashalim riverbed. As part of the actions that we have taken, we sent a professional team, using helicopters carrying generators, pumps and equipment, to pump out the phosphogypsum remnants from cisterns to which access is difficult or limited. Teams from ICL Rotem and ICL Dead Sea, together with the Ministry of Environment Protection and the Nature and Parks Authority, have laid three kilometers of new pipes to flow potable water to the area.

This water is intended to irrigate the vegetation near the dry riverbed and supply water for animals at troughs placed in the field.
I am glad to say that our efforts have proven effective and we have begun to observe animals in the region drinking water from the troughs that were placed alongside the stream. We will continue our restoration efforts and our work with the authorities to find solutions to restore full activities at the plant and the pools.

With that, I would like to turn the call over to Kobi to review our financials.

Kobi Altman: Thank you Asher and good day everyone. Let's take a look at our financial results on slide eight. Q2 presented yet another quarter of solid operational performance, mostly hampered by continuous challenging business environment in our commodities businesses.

Below the operating profit line, we had higher financial expenses and a high effective tax rate. Sales growth and operating profit were slightly lower than last year and slightly better than the first quarter. We've continued to demonstrate our ability to reduce cost and expenses and generate strong positive free cash flow.

Our results continue to be affected by the declining market price environment in the commodity markets. Especially in the commodity phosphate fertilizer market as well as by the strong Israeli shekel compared to the dollar and euro.

Our bromine business, as Asher noted, continued its strong performance and along with advance additives margin expansion contributed to ICL's solid performance this quarter. Potash prices remain stable in the second quarter and volumes were only slightly higher due to the late signing of the annual contract in China.

Similar to what we've experienced in 2016, we believe that our potash business will perform much better in the second half of the year as our shipments in to China are expected to ramp up now. Our net income was affected by both higher than normal finance expenses and increased tax expense this quarter, which I will elaborate on shortly.

Our disciplined approach to reduction of cost in the CapEx may be possible to record another strong quarter of positive free cash flow. Cash flow generation will remain a priority for the company with actions taken to reduce our debt ratios and enable us to further invest in growth projects.

In slide 9, we drill down to the main components of our financial expenses. As you can see our net interest expenses are relatively stable as the decrease in our financial debt was offset by an increase in the average interest rate we pay. The increase this quarter came mostly from a long term loan early repayment fee of $13 million that we paid as part of our overall refinancing activities.

The hedging transactions we make are contributing to the volatility of our financial expenses as the underlying exposure is booked in other line items. As we turn to slide 10, I would like to walk you through the reasons for the increased tax expenses. ICL's tax burden in Israel has increased in 2017.

This is due to the Israeli natural resources tax on potash and bromine and the exclusion of some of our Israeli operations from the encouragement tax law. The tax expenses further increased this quarter due to the strengthening of the new Israeli shekel versus the dollar. We estimate that the tax rate for ICL in the next few quarters to be around 35 percent with volatility between quarters.

On a longer term we expect to slightly go down toward the 30 percent range. Turning to slide 11, we saw a reduction in the specialty solution sales which was almost entirely related to a destocking activity of a customer in the dairy protein business as we discussed in Q1. However, operating income remains stable in line with our strategy to focus on value added products and services and to increase profitability.

The solid performance demonstrated by the division was highlighted by profitability in our bromine business line and continued strong performance in our acid and fire safety businesses. On slide 12, as we already mentioned our essential mineral division continued to operate under a challenging business environment of low commodity prices.

It has also been impacted by the strengthening of the shekel against the dollar and euro. The division has managed, however, to significantly improve the performance in the YPH joint venture by successfully executing efficiencies and cost reduction measures and by reducing sales of loss making commodity products while shifting to increased sales of specialties.

Bear in mind that in the second quarter of 2016, we had a $26 million in income from an insurance payment. Removing that out of the equation operating profit remains fairly stable. We believe the second half of the year will look even better on the back of higher potash shipments due to the signing of the contract in China, and hopefully in India as well.

And, finally, on slide 13, we continue with our disciplined balance sheet management, which is reflected in another quarter of stronger free cash flow. For the first half of the year we generated free cash flow of $190 million versus $123 million in the first half of 2016. We intend to maintain the positive improvements we made in managing our working capital and generating solid cash flow for the remainder of 2017.

This, along with lower CapEx and our divestment plan will serve to further strengthen our balance sheet and support our goal of reducing our debt ratios while still committed to providing solid returns to our shareholders.

Thank you for your time and we will be happy to take your questions now.

Operator: Thank you very much. We will now begin the question and answer session. If you would like to ask a question please press "star" and "1" on your telephone and wait for your name to be announced. If you wish to cancel your request please press the "hash" key. Once again that's "star" and "1" if you wish to ask a question.

Your first question comes from the line of (Lisa DeNeve) please ask your question.

(Lisa DeNeve): Good afternoon. Thanks for taking my question. So yourselves, as various other potash players, have flagged higher seaborne shipping rates, how should we see this in light of the high year on year signed Indian and Chinese potash contracts? Well Chinese by you and Indian last week by Uralkali.

Could you just sort of quantify what the high year on year net price retention is? That's my first question. And, secondly, on a similar note, so last Friday Uralkali signed the Indian Potash contact for 2017 starting from June to next June 2018 and I wonder if you can provide me some color if you have already started negotiations, as well, and, if yes, if you expect these to be concluded, sort of in a short term. Thank you.

Ofer Lifshitz: Hello, this is Ofer Lifshitz. I'm the president of the Essential Mineral Division. Regarding the first question, the negotiation in China actually took into consideration the higher rate of the marine logistic cost. And this was part of the negotiation as far as we know because as you know we were not part of this negotiation.

We can say that from our point of view the $11 increase that was concluded there and we concluded it as well. If we are looking on the net increase we are saying it's between $3 to $5 and the rest is for the logistics. Important to say that if you compare our logistic costs compared to other companies, so our logistic costs to China - we have an advantage of cost compared to if they ship material from the United States or other places. So, this is regarding the first question. Kobi, do you want to add something?

For the second question regarding India, as you know the Russians just concluded their agreements one week ago. We are starting our negotiation as well and we believe we will conclude it in the coming few weeks.

(Lisa DeNeve): Thank you.

Kobi Altman: Maybe just to clarify because I'm not sure if we missed this point, in China we did sign contracts a few days ago for 925,000 tonnes and we are commencing shipping now and we will proceed for the next five months until the end of the year.

(Lisa DeNeve): OK. Thank you very much. That's very helpful.

Operator: Thank you and the next question comes from the line of Jeffrey Schnell. Please ask your question.

(Jeffrey Schnell): Hi, good morning. Could you provide a little detail on how you're thinking about capital allocation and as a related question, ICL has committed to divesting noncore assets. Could you elaborate on what you define as noncore? Is it any thing not related to the Dead Sea and downstream of that?

Or would you consider any of your assets elsewhere in Europe? And, a second question just on the China Potash contract, you've agreed for 925,000 this year and you've sold under a million in 2016. Is there an escalation in year three to get to the terms originally defined under the original framework? Thank you.

Kobi Altman: Hi Jeff, I will start with the first question. On the capital allocation, as we mentioned earlier we are trying to balance all the time between securing enough funds to create and to continue to grow our growth engines for the longer term prosperity of the company, on the second part to manage our balance sheets and our debt ratios, and the third angle is to provide the shareholders return.

We have done a significant reduction in our capital expenditure this year versus last year and versus the years before. And this is obviously helping us to manage our debt ratios down as well and we will continue to do that. I will just mention that we are still investing in CapEx in a range that is more than our depreciation level. So I'm just emphasizing that because we are still continuing on our investment to ensure that we are improving our existing assets and beyond just maintaining them, and looking into growth projects, as well. In terms of the divestitures, as Asher mentioned earlier, we signed this quarter a deal to sell our 50 percent stake in the IDE company and we are working toward closing this deal and we still hope, as we announced when we signed the deal, to close it within 2017.

So far, the approvals process is in line with our expectations. Further divestitures as we announced in June, we are looking at a few assets with the less synergistic value to ICL, to our core mineral chains and mineral legs. We are looking at a few assets and we did not decide yet what of those few assets we will sell in the end.

Obviously we are trying to find the most attractive price for those assets and once we will see the proposals, we will decide what to do with that. The next question on the contracts …

Ofer Lifshitz: I will answer regarding the quantities to China. Actually the agreements that we have this year are part of the framework agreements that we have for three years starting last year. And the quantities that we have signed are similar to the quantities that we sold in China last year, 2016.

This is the quantities that if we find ourselves at the end of the year that we can send some more material and it will suit our Chinese customers we are able to do it, but currently we assume this is the quantities we can ship to China in 2017.

(Jeffrey Schnell): Great, thank you very much.

Operator: Thank you very much. And the next question comes from the line of Fahad Tarik. Please ask your question.

(Fahad Tarik): Hi, this is Fahad on for Joel, thanks for taking my questions. My first question is on the YPH Chinese phosphate J.V., what was the actual loss in the quarter? If you can quantify that and what improvement, if any, are left in terms of operational improvements or a cost reduction? Thanks.

Asher Grinbaum: Asher speaking. The actual loss in the second quarter was more or less in line of $2 million or $3 million. About the improvements that should be done, what we already did in the joint venture, if you remember, when we entered to this joint venture the intention was to convert the joint venture from commodity joint venture to specialty products.

The plan was to do it in three or four years, but because of the very competitive situation that we're facing in China mostly in the bulk products, we decided to cut this three or four years, immediately and to implement our plans to convert the joint venture from commodities to specialties.

We did it in the beginning of this year, and of course, there are also other complimentary activities that we did in the efficiency area, operation excellence and so on. At the end of the day, we came to the conclusion and we got also the results. And if you compare the results to what has happened the last year, we can see the major steps that were done and hopefully we shall keep it and we shall improve it, improve it during the coming quarters.

(Fahad Tarik): My second question was the focus for ICL in the past has been growing the specialty solutions business and including selling non-core assets and really investing in that business. The sales and operational earnings have been flat year over year. What's the major catalyst in that business? What will cause it to grow going forward? Thank you.

Eli Glazer: Good afternoon, it is Eli Glazer speaking, the head of the specialty solution division. The growth path which we are looking is growing mainly on our innovation part of the core business, which is the bromine derivatives and the phosphate and the phosphate derivatives, by going into more and more sophisticated products and to get to unique products. We're also thinking that if we have some opportunities for small, medium acquisitions, this will be also part of our growth path.

Operator: Thank you very much. The next question comes from the line of Patrick Rafaisz. Please ask your question.

(Patrick Rafaisz): Thank you and good afternoon. Three, or maybe four questions. One is on the Rotem incident. Will that have any implications from a CapEx perspective maybe in 2018 when you have to fix that or invest otherwise to restore production? Then the second question is a follow up on the low synergy businesses, do you have a timeline for the other businesses you're looking for divestment or is that a firm commitment to divest these assets or will it also depend on the price you will get, i.e., is there a risk factor in that that you might end up not divesting some of them? Then two short ones, maybe on guidance, net financial expenses with that early repayment of the long term debt, where would you guide the net financial expenses for the full year of '17?

And a similar question for volumes in Potash, assuming you sign the Indian contracts as planned now, where would you guide us for total shipments in 2017? Thank you.

Ofer Lifshitz: This is Ofer, I will answer the Rotem questions. As we see it right now in regard to the future CapEx we will need as part of this event. First of all, we have to take into consideration that we have the insurance that cover us in such cases. And of course if it will be needed we will ask the insurance for this issue.

As we see it right now for the future operations, and it was not concluded yet, of course how much we need to invest and when. But right now, we don’t see it as a major issue that will affect us and we can see that even this year and in 2018, we will be able to operate with not big CapEx that was not already for future CapEx investment that we already took. And as I said, if it will be needed as part of this event, then we will activate the insurance that we have.

(Patrick Rafaiz): Thank you.

Kobi Altman: I will take the next two questions. First with regard to the divestitures, we do not have a definitive timetable and this is why I also mentioned earlier that we are looking at a few assets, potential assets, potentially worth more than $500 million because we want to evaluate the options. And to choose what to divest at the end after we see proposals regarding a few assets and taking the more attractive ones from our perspective. We are looking diligently at those divestments. We do want to do the divestment of around $500 million, including the one we already did, IDE, in order to reduce our debt ratios and to secure sources for future growth. But there is no time limit that is very, very strict, here.

In terms of the finance expenses, I would say by and large that if you take out the $13 million of the prepayment fee, you get to around $35 million of finance expenses for this quarter. I think that this represents more or less kind of a good average to try to think of our finance expenses on a quarterly basis.

However, I must mention that we expect this amount to be relatively volatile on a quarterly basis because of all the various components that are impacting our finance expenses, mainly the currency ones that are relatively volatile but $35 million I think is a good average for the quarter.

(Patrick Rafaisz): Thank you, yes.

Ofer Lifshitz: Just one more comment on the first question, we want to make sure that its clear that the production plan that was stopped for a few days because of the event, this is the sulfuric acid plant is now of course working. Rotem is working in the full capacity. Sorry, sorry, the phosphoric acid plant was stopped for a few days because of the event went back to operation in full operation after a few days. So now the Rotem plant is fully working.

(Patrick Rafaisz): OK. And the volumes for 2017 in potash?

Ofer Lifshitz: I can say that the Potash volumes that we sold in the last few years and we expect to sell more or less the same this year is around 5 million tonnes. And this quantity we assume if all the agreements, including India, would materialize. So more or less these are the quantities that we will sell also this year.

(Patrick Rafaiz): OK, thank you, thank you very much.

Operator: Thank you very much, once again, if you'd like to ask a question please press "star" and "1" on your telephone. And our next question comes from the line of Roni Biron. Please ask your question.

(Roni Biron): Hi, everyone. Kobi, could you provide some more color on the profitability of your non-Potash agriculture units, mainly phosphate and specialty fertilizers? It seems that in aggregate; it was, if I get it right, it was lower than in the first quarter despite the reduced losses in China.

Is that correct and if so, was it driven by the Israeli phosphate business specialty fertilizers, magnesium, etc? And as a related question, should we expect some expansion in these non-Potash units and to what extent will the situation with Haifa chemicals could impact margins?

Kobi Altman: I will take the first part and maybe Ofer will elaborate. On the non-potash businesses in our agro division, Asher mentioned in the opening remarks, that last year we had a $26 million income from insurance during this quarter and this is why if you compare it to that, taking out of the equation this amount, it was doing relatively well.

We also mentioned that the commodity prices in the phosphate are still going down, so we still see if we are comparing to the second quarter of 2016 a price reduction in terms of the main commodity product, the rock, the basic fertilizers, reduction of price by more than 10 percent. Again, versus the second quarter of '16, over the last two, three quarters we do see more stability but still when we are comparing year over year, we see this impact.

So this is in terms of the non-potash agro businesses. And Ofer, do you want to elaborate more?

Ofer Lifshitz: Yes, I want to elaborate a little bit more about the specialty fertilizer business unit. We saw also price decrease in this business unit, not as much as the phosphate, but also some price decreases over there, as well. But the quantities went up quite nicely, and I think that the overall, overall performance of this business unit is doing quite good in this second quarter.

One of the issues that we had since there has been no ammonia in Israel and we had to stop the production in Rotem of the MAP, one of the products of the specialty fertilizing unit. We produce it now in China and we can compensate all the losses here by producing it in China. So overall the specialty fertilizer as part of the agriculture business unit which is not potash is doing quite well in the second quarter.

(Roni Biron): Thank you. And one more question regarding CapEx. First half of the year reflects a run rate of less than $450 million which appears lower than your full year guidance, how sustainable this is and should we assume higher levels in the second half?

Kobi Altman: I will answer that. We do believe that there will be a slight ramp up in the second half. So we continue with our guidance of around $500 to $550 million of CapEx, we believe that this is the range that you should take.

(Roni Biron): OK. Thank you very much.

Asher Grinbaum: I would like to refer to the questions about the ammonia.

(Roni Biron): Yes.

Asher Grinbaum: In the bottom line it will be a very marginal impact on ICL production and ICL results.

(Roni Biron): Thank you.

Operator: Thank you very much. We have no further questions at this time. Please continue.

Dudi Musler: Well if there are no further questions, with that we will conclude our Q2 2017 conference call. Is there another question?

Operator: We've just had one additional question come through from the line of Lisa DeNeve. Please ask your question.

(Lisa DeNeve): Hi, just a small question on the food specialties. If you could provide a little bit of outlook on food specialties in general for the second half of 2017 as well as particularly for dairy proteins. How we should look at it in the light of the changing Chinese regulations and if you expect sort of sales to sort of recover in the second half of 2017 or even further more should we be looking more at (inaudible) for that? Thank you.

Eli Glazer: Hi, it's Eli again. Related to food proteins, especially to, with regards to China, the new regulation will come into effect in next year in January 2018. In the meantime, there are some restrictions which all the suppliers in this market are doing all the preparation which is necessary in the market.

Therefore we expect that during next year, we'll see some improvement. And all in all, the Chinese markets for infant proteins is going to be better at least from what we know and what we predict in this market. The other business which we have, we are in line of what our plans and we continue to innovate new products, especially related to our phosphate and phosphate plants. And this part is going according to our plans.

(Lisa DeNeve): OK. Thank you.

Dudi Musler: OK, then. If there are no more questions, we can now conclude the Q2 2017 conference call. Thank you very much everybody for joining us and we look forward to seeing you and talking to you soon.

Operator: Thank you very much. That does conclude our call for today. Thank you all for participating, you may now disconnect.

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