

Q2 2018 AMG Advanced Metallurgical Group NV Earnings Call

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TEXT version of Transcript

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Corporate Participants

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* Eric E. Jackson

AMG Advanced Metallurgical Group N.V. - COO, Member of Management Board & President of AMG Critical

* Heinz C. Schimmelbusch

AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO

* Jackson M. Dunckel

AMG Advanced Metallurgical Group N.V. - CFO & Member of Management Board

* Steve Daniels

AMG Advanced Metallurgical Group N.V. - SVP

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Conference Call Participants

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* Frank Claassen

Banque Degroof Petercam S.A., Research Division - Analyst

* Henk Veerman

Kempen & Co. N.V., Research Division - Research Analyst

* Krishan M. Agarwal

Citigroup Inc, Research Division - Analyst

* Philip Ngotho

ABN AMRO Bank N.V., Research Division - Analyst

* Stijn Demeester

ING Groep N.V., Research Division - Research Analyst

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Presentation

Operator [1]

Good day, and welcome to the AMG Earnings Second Quarter 2018 Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Steve Daniels. Please go ahead, sir.

Steve Daniels, AMG Advanced Metallurgical Group N.V. - SVP [2]

Thank you, operator. Welcome to AMG's second quarter 2018 earnings call. Joining me on this call are Dr. Heinz Schimmelbusch, the Chairman of the Management Board and Chief Executive Officer; Mr. Jackson Dunckel, the Chief Financial Officer; and Mr. Eric Jackson, the Chief Operating Officer. AMG's second quarter 2018 earnings press release issued this morning is on AMG's website.

Today's call will begin with a review of the second quarter 2018 business highlights by Dr. Schimmelbusch. Mr. Dunckel will comment on AMG's financial results, and Mr. Jackson will discuss operations. At the completion of Mr. Jackson's remarks, Dr. Schimmelbusch will comment on strategy and outlook. We will then open the call to take your questions.

Before I pass the call to Dr. Schimmelbusch, I would like to comment on forward-looking statements. This conference call could contain forward-looking statements about AMG Advanced Metallurgical Group N.V. Forward-looking statements are not historical facts, but may include statements concerning AMG's plans, expectations, projections, objectives, targets, goals, strategies, future events, future revenues or performance, capital expenditures, financing need, plans and intentions related to acquisitions, AMG's competitors' strengths and weaknesses, plans or goals related to forecasted production, reserves, financial position and future operations and development, AMG's strategy and the trends AMG anticipate in the

industries and the political and legal environment in which it operates, and other information that is not historical information. When used in this conference call, the word expect, believe, anticipate, plan, may, will, should and similar expressions and the negatives thereof are intended to identify forward-looking statements. By their very nature, forward-looking statements involve inherent risks and uncertainties, both general and specific. And risks exist that the projections, forecasts, predictions and other forward-looking statements will not be achieved. These forward-looking statements speak only as of the date of this conference call. AMG expressly disclaims any obligation or undertaking to release publicly any update or revisions to any forward-looking statements contained herein, to reflect any change in AMG's expectations in regard thereto; or any change in events, conditions or circumstances on which any forward-looking statements is based.

I will now pass the floor to the Dr. Schimmelbusch, AMG's Chairman of the Management Board and Chief Executive Officer.

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [3]

Thank you, Steve.

During the second quarter 2018, AMG generated \$329 million of revenue and \$51 million of EBITDA. The sharp improvement in profitability during the quarter was once again driven by improved pricing and higher sales volume in the AMG Critical Materials, most notably in our vanadium business in Cambridge, Ohio. Furthermore, relentless improvements in productivity have resulted in an upward trend, both in terms of profitability and return on capital employed.

AMG Critical Materials generated EBITDA of \$45 million during the second quarter '18, an increase of 89% from \$24 million in the second quarter of '17 thanks to strong financial performance in vanadium, chrome metal and aluminum products. Driven by higher vanadium sales volumes and prices, improved chrome metal product mix effects and strong sales of aluminum products.

AMG Engineering signed \$86 million in new orders during the second quarter of '18, representing a 1.39x book-to-bill ratio due to strong orders of turbine blade coating furnaces for the aerospace market and heat treatment furnaces for the automotive market. Order backlog was \$263 million as of June 30, '18, a 3% increase from last quarter.

AMG Engineering generated EBITDA of \$5.5 million during the second quarter '18, a reduction of \$2.5 million compared to the second quarter of '17, due to higher SG&A expenses and lower gross profit generated from the heat treatment services division. On a full year basis, AMG Engineering expects '18 EBITDA to be in line with the prior year.

I would now like to pass the floor to Jackson Dunckel, AMG's Chief Financial Officer. Jackson?

Jackson M. Dunckel, AMG Advanced Metallurgical Group N.V. - CFO & Member of Management Board [4]

Thank you, Heinz.

AMG's financial performance in the second quarter was very strong, with revenue, profitability and return on capital employed all showing considerable improvement versus prior year. Revenue for the quarter grew by 26% to \$329 million, thanks to 32% increase in revenue in our Critical Materials segments and a 5% increase in our engineering segment.

EBITDA increased 59% to \$51 million in Q2 2018 from \$32 million in Q2 last year, which is also due to a very strong financial performance in AMG Critical Materials.

Q2 net income attributable to shareholders increased to \$17.3 million compared to \$13.1 million in the prior year. And fully diluted earnings per share followed that increase to \$0.54 per share from \$0.42 per share in the prior year. Net income attributable to shareholders in Q2 2018 was adversely impacted by a revaluation of our tax assets in Brazil due to the weakening of the Brazilian real versus the dollar. This is a noncash effect and increased our tax expense, and consequently reduced our net income by approximately \$6 million in the second quarter. It's worth pointing out that if we were to exclude this noncash currency effect from our second quarter tax expense, AMG's net income attributable to shareholders would have been approximately \$23 million, an improvement of 78% compared to prior year. And fully diluted earnings per share would have been \$0.73 per share, an increase of 74% versus the prior year.

On a year-to-date basis, cash from operating activities decreased by \$4.9 million or 17% compared to the first half of last year. This decrease was mainly due to the higher working capital balances driven by increased metals prices, but these increased balances were partially offset by improved profitability in AMG Critical Materials. As we've noted in the past, due to the nature of our business, the absolute value of working capital in AMG Critical Materials tends to increase in line with rising metals prices.

AMG ended the quarter with net debt of \$34.8 million, an increase of \$25.4 million from March 31, 2018 due to the higher levels of working capital and capital expenditures incurred in Brazil in relation to our lithium project.

I'll turn now to a review of our 2 segments and starting with AMG Critical Materials. Q2 2018 revenues increased in Critical Materials by 32% to \$267 million versus the prior year. This improvement was driven by improved vanadium, silicon metal, aluminum, graphite, chrome metal and tantalum prices and higher sales volumes of vanadium, aluminum, tantalum and titanium products.

Critical Materials gross profit increased by \$24.6 million or 65% over last year's second quarter. At the business unit level, we had substantially improved gross profit in vanadium, chrome metal and aluminum products. This higher gross profit was driven by higher vanadium sales volumes and prices, improved chrome metal products mix effects and strong sales volumes of aluminum products. This improvement was partially offset by lower gross

profit in silicon metal, which was driven by lower volumes as a result of unplanned furnace maintenance during the quarter following mechanical issues, and an accrual of the repayment of the subsidy granted to AMG Silicon in 2012 and 2013. AMG Silicon was notified recently that the subsidy granted by the German government contravened EU rules, and as a result, AMG Silicon is liable for repayment.

Critical Materials SG&A expense in Q2 2018 increased by \$3.4 million or 16% compared to the same period in the prior year, due to foreign exchange effects related to the strengthening of the euro-dollar rate as well as higher personnel costs.

EBITDA for the Critical Materials segment was \$45.3 million, an improvement of 89% quarter-over-quarter, driven by considerably higher gross profit and partially offset by the increase in SG&A expenses. It is worth noting like all processing businesses, that in a period of rising prices, we tend to experience higher profitability as working capital moves through our plants.

Moving on to AMG Engineering. \$86 million in new orders were signed up in Q2 2018, representing a 1.39 book-to-bill ratio. This exceptionally strong order intake was driven by orders for turbine blade coating furnaces for the aerospace market and heat treatment furnaces for the automotive market. Order backlog was \$263 million as of June 30, 2018, an increase of 3% from March 31, 2018 and the highest in over 9 years.

AMG Engineering revenue increased by \$2.7 million to \$62 million or 5% compared to last year. Higher revenue generated from the sale of vacuum furnaces was partially offset by lower revenue in the heat treatment services division, as automotive customers transitioned to new engine platforms. This transition was fully expected and planned for by AMG Engineering, and we expect to see heat treatment service revenues return to normal levels once this transition is completed in early 2019.

Gross profit in the quarter increased slightly by \$0.2 million quarter-over-quarter. However, gross margin decreased slightly to 27% from 28%, driven by lower gross profit in the heat treatment services division as a result of the engine platform transition mentioned earlier.

SG&A expenses increased by \$1.8 million quarter-over-quarter due to foreign exchange effects related to the strengthening of the euro-dollar rate as well as higher personnel costs.

As a result of the higher SG&A expenses and increased currency impact, Engineering EBITDA decreased by \$2.5 million to \$5.5 million in Q2 2018. However, to reiterate the comments made earlier by Dr. Schimmelbusch, on a full year basis, we expect AMG Engineering EBITDA for 2018 to be consistent with the prior year.

Moving on to SG&A costs. Our SG&A costs in the quarter were \$37.2 million or 16% higher than the prior year, primarily due to foreign exchange effects related to a higher euro-dollar rate and to a lesser extent, higher personnel costs. When compared to the second quarter of 2017, the average euro to U.S. dollar exchange rate strengthened by over 12%, resulting in higher expenses on a U.S. dollar basis for AMG's units operating within the Eurozone.

Finance costs. AMG's second quarter 2018 net finance costs increased to \$5.3 million compared to \$1.8 million in the second quarter of 2017. The increase was due to higher interest expenses associated with AMG's new long-term credit facility, which has resulted in

higher levels of gross debt and a higher interest rate due to the 7-year -- due to the 7-year tenor of our new bank facility.

Taxes. AMG recorded an income tax expense of \$19.5 million in the second quarter of 2018 as compared to a tax expense of \$7.7 million in the same period of 2017. The increase in tax expense was driven by higher levels of profitability, the full recognition of AMG's U.S. operating loss carryforwards in 2017 and the revaluation of AMG's Brazilian tax balances. Due to the significant movement of the Brazilian real against the dollar, AMG incurred a noncash tax expense of \$6 million in the second quarter.

AMG does continue to benefit from net operating loss carryforward balances, primarily in the United States, to offset taxes payable. As a result, AMG paid taxes of \$7 million in Q2 of 2018 as compared to tax payments of \$3.4 million in the same period in 2017. AMG's effective cash tax rate rose to 19% in Q2 -- in Q2 versus 16% for the same period in the prior year.

Due to substantially higher levels of profitability in the United States, we expect to fully utilize our U.S. net operating loss carryforwards in 2018. As a result, the cash tax rate will increase from 2019 onwards, and we anticipate the rate will be in the region of 20% to 25%.

Capital expenditures. Q2 2018 capital expenditures decreased slightly to \$18.4 million from \$18.6 million in Q2 2017. Once again, the largest expansion capital project in the second quarter was AMG's lithium project in Brazil.

AMG's liquidity and cash flows. In terms of liquidity, AMG's balance sheet is exceptionally strong, and we are in full compliance with all debt covenants as of June 30, 2018. AMG had \$512 million of total liquidity as of the end of Q2 2018, following the successful refinancing of our credit facilities during the first quarter of 2018. As mentioned earlier, operating cash flow was impacted during the quarter by the increased profitability in Critical Materials, offset by increased working capital positions due to higher metal prices.

Net debt as of June 30 was \$35 million, an increase of \$25 million during the quarter, driven by significant capital expenditures and the increase in working capital.

That concludes my remarks. I would like to now pass the floor to Eric Jackson, AMG's Chief Operating Officer.

Eric E. Jackson, AMG Advanced Metallurgical Group N.V. - COO, Member of Management Board & President of AMG Critical [5]

Thank you, Jackson.

As we noted last quarter, from a market perspective, demand continues to be strong and prices for many of our key products continue to move higher. With 1 or 2 minor exceptions, market prices in the second quarter once again showed improvement, both compared to the second quarter of 2017 and the prior quarter.

AMG Vanadium's profitability improved considerably compared to the second quarter of the prior year, due to higher vanadium prices and strong sales volumes. Ferrovandium index prices averaged \$34 per pound during the second quarter, and have further strengthened in recent months with spot prices presently just over \$39 per pound.

AMG Superalloys gross margin also improved substantially during the quarter due to product mix improvements and higher prices. AMG Superalloys continues to focus on sales of high-purity chrome metal for the energy storage and aerospace market, and recent investments made to expand our capacity of those high-margin products are having a positive effect on profitability. AMG Superalloys has doubled its production and sales of high-purity chrome products in the last 2 years.

In AMG Tantalum & Niobium, our new tantalum concentration plant continues to perform very well. And sales volumes were substantially higher compared to the second quarter of 2017, when production was impacted by ongoing repair work following the fire in early 2017. The truckers' strike in Brazil in May 2018 had minimal impact on our production, but did delay our scheduled deliveries for June 2018 by 1 month, impacting revenue recognition in the quarter. This is purely a timing issue.

Elsewhere, sales volumes improved quarter-over-quarter in AMG Titanium Alloys & Coatings, driven by increased titanium aluminide volume, and in AMG Aluminum, due to increased volumes sales of grain refiners, specialty alloys and aluminum powder products.

In AMG Silicon, sales volumes declined versus the prior year due to unplanned maintenance work in our furnaces during the quarter.

In AMG Engineering, strong demand for our industry-leading vacuum furnace solutions resulted in a further increase in our order backlog at the end of the quarter. From an operational standpoint, AMG Engineering is in the process of expanding its workforce in response to the strong order book. However, we will maintain great flexibility on staffing levels going forward. Inevitably, the workforce expansion is resulting in higher expenses in the short term, but will enable AMG Engineering to expand its production capabilities from 2019 onwards. To support this planned expansion, AMG Engineering is also in the process of expanding its assembly facility in Hanau, Germany having recently acquired the property adjacent to our current facility.

In 2018, we will continue to focus on those issues that we can control, namely, operational improvements, working capital management and price risk management to drive operating cash flow and return on capital employed. We're also working extremely hard to progress our lithium and vanadium investments as an integral part of realizing AMG's strategic and financial objectives.

I would now like to pass the floor to Dr. Heinz Schimmelbusch, AMG's Chief Executive Officer.

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [6]

Thank you, Eric.

As demonstrated through our second quarter results, our business portfolio continues to perform exceptionally well. With respect to strategic project activities, I can confirm that the ramp-up of AMG Mineração's first lithium concentrate plant, called spodumene 1, continues on schedule in line with the timetable set out in our EPC contract with Outotec.

Detailed engineering work on AMG's second lithium concentrate plant, spodumene 2, in combination with the expansion of the Mibra mine, is progressing towards completion. And we are working hard to finalize an EPC contract for the delivery of that second plant. Negotiations are ongoing, and we expect to finalize the contract before the end of September '18. Once completed and as announced previously, total annual production capacity from AMG's Mibra mine will increase to 180,000 tons of lithium concentrate and 600,000 pounds of tantalum concentrate. AMG expects to complete the expansion by end of '19.

Intensive project development activities for the downstream lithium chemical plant are proceeding. We accept -- we expect to communicate the specifics of our strategy later in September.

In parallel, the development activities of AMG Vanadium to expand our spent catalyst recycling capacity are progressing as planned, also in the context of our recently announced agreement with Criterion.

With regards to current year guidance, and encouraged by the first 6 months of '18, AMG expect full year '18 EBITDA to improve by between 40% and 50% compared to prior year.

Operator, we would now like to open the line for questions.

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Questions and Answers

Operator [1]

(Operator Instructions) We'll take our first question from Philip Ngotho.

Philip Ngotho, ABN AMRO Bank N.V., Research Division - Analyst [2]

I'll start with maybe the most obvious one, and we -- it keeps occurring every call. But it's on the guidance, and I know that you always choose to be conservative when stating -- when giving earnings guidance. So I won't ask you to upgrade, that would be more specific. But I'm just wondering if you'd be willing to follow my thoughts on what we might expect in the second half of the year versus the first half of the year. Because the way I look at it, you're at \$95 million EBITDA at the moment, and for you not to -- I think it should be easily achievable, the \$200 million EBITDA level. But I mean I appreciate that you won't comment on that, but maybe just the most important moving parts. So what I have here is, if I look at vanadium, I assume that you should still see a benefit, a significant benefit if spot price remain where they are, the 26% above average first half year prices. And then on the lithium spodumene plant that will come online that you are ramping up, I assume that you'll also be having an EBITDA contribution there as well. I don't know if you're willing to give a guidance on that. How much -- what kind of order magnitude we could -- we should expect? And then I guess you still see some benefit on some lost volumes from the silicon -- downtime from the silicon (inaudible) facility, and the margin uplift in Engineering versus Q2 results. So I don't know if you can comment on that. Am I I'm missing anything here, either being positive or negative? That's my first question.

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [3]

Well, that's quite a question. First of all, let me comment on what -- let me, in friendship, comment on when you said, it should be easily, achieve easily \$200 million. I'll tell you something. \$200 million would be an all-time record. And to term that as "easily" is a little bit diminishing the whole of this excellent management board, because we work very hard on trying to achieve this exceptional result. Is that okay with you?

Philip Ngotho, ABN AMRO Bank N.V., Research Division - Analyst [4]

Yes, that's okay. I didn't mean to put it that way. But given the macros, it seems realistic, let me put it that way, although it's hard work, I know.

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [5]

Yes, I realize that. That's all good, all good, all good. Now at lithium, you have to note we will have meaningful -- expect meaningful of commercial of quantities starting September, end of August, September, but shipping the revenue recognition is CIF China. And that takes

into account a long logistics chain from the Mibra mine into the harbor, from the harbor to the destination in China. So revenue recognition is delayed a little bit [as regard to, so below par] in the fourth quarter, but that is not -- that's not moving the needle in any way. So please recognize that this is CIF China. When we were summarily -- when we were discussing the 40% to 50% guidance, then we multiplied and took into account very detailed risk analysis. And we are conservative by principle, because we have established a record of credibility in exceeding -- meeting and exceeding, mostly exceeding our guidance. Because we have a feeling that if we miss a guidance, then we would destroy this series of successful guidance statements. And you're right, we are conservative. To multiply, -- I, by the way, subscribe to your principle also. When unit executives report a month which is a good month, so I always say, "Okay, times 12," and they loudly protest in each case. And then each quarter, I multiply it by 12 if it's a good quarter, and I get also loud protests. So I don't protest your -- I don't protest, but -- but always these multiplications are a little bit simplified.

Philip Ngotho, ABN AMRO Bank N.V., Research Division - Analyst [6]

Okay, okay. Fair enough. Then maybe just -- could you be -- could you give an indication of - - because if I look at silicon metal, it actually was a material gross profit contributor last year. And I believe that was Q1. And this quarter, it's according to the presentation, I think, there's no contribution at all, but that's on a gross profit level. But can you also give us what on EBITDA you approximately lost this quarter? And should we -- will you be able to recoup some of the lost volumes in Q3? How is that going?

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [7]

The -- I understand. The lost production was primarily caused by quality problems in electrodes. And these things take time to be rectified. And I don't think that we will be in very good shape in the [fourth quarter.] We will be continuing our performance of the third quarter.

Philip Ngotho, ABN AMRO Bank N.V., Research Division - Analyst [8]

Okay, very clear. Then maybe my last question for now, very helpful comments on the strategic initiatives and when you expect to announce further plans. The only thing where you didn't give a timeline on is the agreement with Criterion. I don't know whether that was intentionally, or that you are able to provide any more details when you think there could be more clarity on that.

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [9]

More clarity?

Philip Ngotho, ABN AMRO Bank N.V., Research Division - Analyst [10]

Oh yes, in terms of timeline.

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [11]

Yes, I understand. The Criterion agreement is a business concept, which embraces a very interesting offering, a new offering to the market, cradle to grave. And that means that if one of the parties, namely Criterion, offers fresh catalysts, and if that is connected to an offer of taking back spent catalysts, then we do that in a joint fashion. So that is a memorandum which is signed and has these certain exclusivity [boundaries.] And we are now exploring worldwide the opportunities jointly under this agreement, which is a very elaborate exercise. In parallel to that, we are preparing the expansion of our Ohio facility. That is maybe a -- So we announced the 30% decrease -- increase of the capacity. We have announced that. That might be replaced by an increase -- a doubling of the capacity actually. The demand for the recycling services is continuing very strong and is growing. And that's for several reasons, which would be too long to explain here. But we believe that we can justify, or we shoot, we shoot for a larger capacity increase in Ohio. And the best way to look at is a doubling of the capacity, which if that is affirmative, we will announce.

Philip Ngotho, ABN AMRO Bank N.V., Research Division - Analyst [12]

Okay. And that is to, just to get this clear, that is separate from the Criterion business case concept?

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [13]

Well, that's our normal business.

Eric E. Jackson, AMG Advanced Metallurgical Group N.V. - COO, Member of Management Board & President of AMG Critical [14]

Yes.

Philip Ngotho, ABN AMRO Bank N.V., Research Division - Analyst [15]

Yes, indeed. Clear.

Operator [16]

We'll take our next question from Frank Claassen.

Frank Claassen, Banque Degroof Petercam S.A., Research Division - Analyst [17]

Frank Claassen, Degroof Petercam, 2 questions please. I noticed that your cash position has increased quite a bit. Is there a specific reason for this? Or are you thinking of bringing down your gross debt and using your cash position for that, firstly? And secondly, can you update us on your CapEx guidance for 2018? And also is there any Phase 2 CapEx -- Phase 2 lithium CapEx already included in 2018? Or will the bulk of this 110 million come next year? And then finally, you talked about the subsidy on the silicone repayments. How big was that exactly? And is it already in the numbers? Or does that still have to come?

Jackson M. Dunckel, AMG Advanced Metallurgical Group N.V. - CFO & Member of Management Board [18]

It's Jackson Dunckel here. On cash, we refinanced our debt facilities. So we raised \$350 million of term loan B in January, and that was the cause for the increase in the cash. That is sitting on our balance sheet, ready to fund capital expenditures as we move forward. On CapEx guidance, we would expect 2018 to be \$85 million to \$90 million. And on the subsidy, the -- the accrual for the subsidy is in the numbers. And we would expect to resolve that in September, so it shouldn't be very long. But given that we're in the middle of negotiating with the government, we don't really want to disclose the number.

Frank Claassen, Banque Degroof Petercam S.A., Research Division - Analyst [19]

Okay. That's fair enough. And the \$85 million to \$90 million, how much do you already spend on the Phase 2? So let's say, of the 110 million guidance for the Phase 2 lithium, how much is already expected for '18? Or will the bulk come in 2019?

Jackson M. Dunckel, AMG Advanced Metallurgical Group N.V. - CFO & Member of Management Board [20]

Yes. It includes about \$20 million to \$30 million for spodumene 2 for the year, we achieved for 2018, of the 110 that you referenced.

Operator [21]

And we'll take our next question from Henk Veerman.

Henk Veerman, Kempen & Co. N.V., Research Division - Research Analyst [22]

Some remaining questions from my side, firstly, on the engineering and specifically on the heat treatment. You mentioned there's some weakness because some key clients are changing their engine design. Now I was wondering what's more or less the timing of that into the second half of the year? Will you see an uptick? And will you sort of fully make up for the volumes in Q3 or maybe Q4? And whether you've already signed it, let's say, these agreements with these key clients regarding their new engine design. That's the first question.

Jackson M. Dunckel, AMG Advanced Metallurgical Group N.V. - CFO & Member of Management Board [23]

On the engine platforms in our heat treatment services business, that has been planned for the last 2 or 3 years. So we have signed contracts, and our customers are performing on those contracts. And we are experiencing a ramp in volumes and expect to be at full capacity by the end of this year.

Henk Veerman, Kempen & Co. N.V., Research Division - Research Analyst [24]

Okay. And secondly on vanadium beyond the extent already discussed, if I look at the chart on Page 33, what I actually see is the gross profit year-on-year. I think the growth there from - or 54 million towards the 80 million is solely contributable to the vanadium business. And from what I always understood is that the profitability always largely depends on the profit sharing with your clients. And also what I always understood is when the prices are increasing rapidly, the sort of part you give back to your clients is relatively low. And also what I understood is there's quite a large backlog in vanadium. I was wondering in the second half of the year, will [FAD] profitability sequentially would have declined in vanadium, let's say, at gross profit of around 35 million from the same prices. Will it go down because you are actually recycling catalysts, which have a sort of a larger profit sharing agreement?

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [25]

Well, when prices rise, then of course you have a positive effect. And if the incoming inventory positions are at higher prices, then of course, that will lead to previous periods where the prices were rising and the inventory were valued low from previous periods, then you have the declining effect of the vanadium contribution. By the way, the percentage we mentioned, the guiding percentages they are, actually not be guiding. They are fixed contractually.

Henk Veerman, Kempen & Co. N.V., Research Division - Research Analyst [26]

Okay, yes. But what I understood is that actually should the prices be stable as of now, the -- let's say the marginal profitability from the first half into the second half in vanadium would actually decline a bit, because the profit sharing is a bit larger. Is that what we should expect? Or...

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [27]

You are correct. The relative profitability, that's -- your observation is correct.

Henk Veerman, Kempen & Co. N.V., Research Division - Research Analyst [28]

Okay, yes, yes. So that sort of explains that's a policy conservativeness in your guidance today...

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [29]

That's exactly right. The guidance, the guidance reflects a detailed discussion of the various contributions and their specifics also including inventory position, movement, et cetera. So it is not -- it is more than just -- as I mentioned earlier, it's more than a simple multiplier. It's microeconomics.

Henk Veerman, Kempen & Co. N.V., Research Division - Research Analyst [30]

And on tantalum, I've read some industry reports recently on the tantalum markets, which are actually quite bearish, because some other lithium or future lithium producers also expect to ramp up their tantalum production. What is your view on this, on this tantalum market, let's say in the next year and the next few years?

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [31]

Our view of the tantalum market is very, very strong. We expect rising prices.

Henk Veerman, Kempen & Co. N.V., Research Division - Research Analyst [32]

Sorry, price increases, you said?

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [33]

Yes, in line with customers.

Henk Veerman, Kempen & Co. N.V., Research Division - Research Analyst [34]

Okay. Then on interest costs, I actually see that for the, let's say for the first half of the year which you are refinancing, there's -- it actually equals 12 million. Should we expect around 24, 25 million for the full year? Because it's actually quite a step up versus last year, just to check that.

Jackson M. Dunkel, AMG Advanced Metallurgical Group N.V. - CFO & Member of Management Board [35]

Well, we did have a write-off of debt issuance costs in the first quarter associated with the refinancing of our old facility. So that increased the amount of interest costs in the first quarter. So I think we should be running around \$20 million to \$24 million, depending on debt levels.

Henk Veerman, Kempen & Co. N.V., Research Division - Research Analyst [36]

Okay. Now last question on lithium to end with. Has there any -- has anything changed, like first the last time you spoke during the Q1, in terms of contracts being let's say negotiated in the market. I think it was around 13k to 14k per tonnage. Is there -- has anything changed that would sort of change your view on that now?

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [37]

When we are selling under a long-term spodumene agreement, those prices are negotiated and contractually certain, and nothing is changed on that. The only contractual happenings in the lithium area, as I mentioned, are the finalization of EPC contracts for spodumene 2 and for carbonate 1 -- oh no, not carbonate. Downstream 1, chemical 1.

Operator [38]

(Operator Instructions) We'll take our next question from Krishan Agarwal.

Krishan M. Agarwal, Citigroup Inc, Research Division - Analyst [39]

Most of my questions are answered. I have 2 left. You mentioned the impact from the truckers' strike on Brazil had impact for -- on volume for 1 month. So do you have any catch-up to be done in the third quarter on those volumes? And is there any material impact on this that you would expect in the third quarter? That's one.

Eric E. Jackson, AMG Advanced Metallurgical Group N.V. - COO, Member of Management Board & President of AMG Critical [40]

Yes. This is Eric Jackson. The number is not really material. But yes, there is a shipment that will be in our third quarter, that should have been in our second quarter. So there's a small catch-up in the third quarter.

Krishan M. Agarwal, Citigroup Inc, Research Division - Analyst [41]

Okay. And on the SP 1, I mean you commissioned it in May. And then you said the revenue recognition is a bit delayed maybe to the fourth quarter. So how was the cost recognition? Was there any amount recognized in the cost into second quarter in the P&L? Or is it still being capitalized?

Eric E. Jackson, AMG Advanced Metallurgical Group N.V. - COO, Member of Management Board & President of AMG Critical [42]

if I understood your question quick, there was no cost change because of timing. Our shipments, as Dr. Schimmelbusch mentioned though, are CIF China. So revenue recognition really will be in the fourth quarter. There is no delay in -- from our -- what we have contractually agreed in our EPC contract with Outotec.

Krishan M. Agarwal, Citigroup Inc, Research Division - Analyst [43]

Okay. So -- But there is no cost which you have now booked into the P&L on the account of no ramp-up or start-up in the second quarter?

Eric E. Jackson, AMG Advanced Metallurgical Group N.V. - COO, Member of Management Board & President of AMG Critical [44]

No. That's correct.

Operator [45]

We'll take our next question from Stijn Demeester.

Stijn Demeester, ING Groep N.V., Research Division - Research Analyst [46]

I ask -- I have a couple of questions on tantalum and then one follow-up on vanadium. So in tantalum earlier in July, H.C. Starck sold a part of its tantalum business to a Japanese company, Nippon metals and mining. Will that affect your operations in any way, as I believe H.C. Starck is a customer of you in tantalum? And secondly on that, I think it was Roskill that rumored that you were also interested in the assets. Would that be an M&A strategy for you to vertically integrate yourself in tantalum -- for tantalum in particular?

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [47]

Well, the ownership change of Starck to Nippon mining is a good thing because it has some improved, in our interpretation, the financial position of Starck, and -- So that is -- it was private equity-owned. And exit was received and the exit has occurred. And now it has a strong strategic parent, and that is a positive thing. And we -- Starck is a very valuable customer of us. We -- your second question of were we interested in that, not really. We are not an acquisition company. We are focused on organic growth project. As the intrinsic profitability of our organic portraits exceeds materially the multiples which you have to pay in acquisition. That's the fundamental statement. And we are not excluding that we, one of these days, buy something, but it has to be very, very accretive in order to stay in our profitability metrics. If you want to have a project approved in AMG, you better have a multiple of 3 or so, and that is very difficult to achieve. Then you have to pay 9.5, like I think was paid in the Starck acquisition. We can't afford that, because you have to work then quite some time to pay for the premium, or to get your premium back. We rather stay in this organic project. Which is really not an answer to your question, which was are you planning to go downstream. We are constantly analyzing our value chain. We are constantly analyzing our value chain. And of course, the know-how which is in AMG actually got to downstream tantalum is rather extensive. And you think about the fact that almost everybody who produces tantalum, produces tantalum in furnaces bought from us.

Stijn Demeester, ING Groep N.V., Research Division - Research Analyst [48]

Okay. So any concrete plans towards that goal?

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [49]

Otherwise, there -- if there are plans that would be material, then we would announce them.

Stijn Demeester, ING Groep N.V., Research Division - Research Analyst [50]

Okay. Clear. Maybe then also on tantalum, I realize it's a bit sensitive. But could you give us an update on the legal dispute with GAM? As I understand there is still a claim due to the lost contract last year. GAM is also expanding its operations then in Talison. So could you give us some insight there?

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [51]

No.

Stijn Demeester, ING Groep N.V., Research Division - Research Analyst [52]

And -- okay. What's your view on their expansion plan?

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [53]

We don't comment. I mean, the -- I can't comment because we are still a shareholder. And that prevents me of -- you know...

Stijn Demeester, ING Groep N.V., Research Division - Research Analyst [54]

But any view along the sidelines?

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [55]

If there's a lawyer in the room, If there was a lawyer in the room, the lawyer would now wave to me to slow down. So I'm slowing down.

Stijn Demeester, ING Groep N.V., Research Division - Research Analyst [56]

Maybe we should profit from the fact that there's no lawyer. No. A follow-up on vanadium, you said that you are also contemplating so a doubling of capacity instead of the announced 30%. Can you give an insight in what are the current considerations which prevent your -- or prevent you not to do that? And with the CapEx involved which was, if I'm right, 35 million, would that increase to the same extent? Or how should we look at it?

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [57]

No. The announced project was essentially a debottlenecking. And the debottlenecking is not a building of a completely new facility. And therefore, if we switch to that mode, that would increase the investment relative to the project announced, because it would mean another big facility. You have to please understand that the main first step in such a facility is a hosting operation and the second step is a melting plant. And the announced expansion margin, also debottlenecking expansion, was focused on the expansion of the hosting facility. When you build a new hosting facility including a new melting facility, that of course is a different ballgame. And it eminently justifies in the view of -- in my view, it eminently justifies to build a new plant. And therefore, we are analyzing to build a new plant. And when we have -- and when we have finished that analysis, we will announce it. And if we announce it, you will probably read in that announcement that the investments are considerable.

Stijn Demeester, ING Groep N.V., Research Division - Research Analyst [58]

And is that now based on negotiations with clients? Is there -- are these considerations that you are now looking at?

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [59]

Yes. Exactly.

Operator [60]

(Operator Instructions) We'll take a follow-up question from Philip Ngotho.

Philip Ngotho, ABN AMRO Bank N.V., Research Division - Analyst [61]

Yes. I have 2 follow-up questions. First of all on the working capital, there was a large working capital outflow this quarter. As you indicated also, because of high commodity prices, some metal prices. Can you indicate what you expect for the second half? Do you assume that metal prices remain stable? Do you think there will still be some reversal of the working capital investment that you saw this half year? And my second question is still on the vanadium, related to the vanadium, what you explained before, the benefit that you are having from purchasing -- or having a lower raw material sourcing and the increasing prices. So the way I see it, it's a positive inventory revaluation. In the past, you always disclosed what the impact was when it was a negative revaluation impact. So can you indicate on what it approximately would be in EBITDA terms or in percentage margins, if indeed price remain at these levels? So order of magnitude, what are we talking about?

Jackson M. Dunckel, AMG Advanced Metallurgical Group N.V. - CFO & Member of Management Board [62]

So in terms of the working capital outflow, assuming that prices stay where they are today, the working capital change will be flat for the second half. But that means that the operating cash flow will be much higher, because it won't be burdened by any working capital outflows. So there's no reversal. We don't expect a reversal of prices.

Philip Ngotho, ABN AMRO Bank N.V., Research Division - Analyst [63]

Okay. So I meant, are there any additional inventories that you are holding in terms of volumes, that you might see it coming back in the second half of the year. But it's just solely price-driven.

Jackson M. Dunckel, AMG Advanced Metallurgical Group N.V. - CFO & Member of Management Board [64]

No. We -- our days on hand and our volume -- our inventory volumes are pretty consistent. It's purely price that drove the working capital increase. And then on the -- you're referring to our lower of cost or market, which is an accounting, a noncash accounting charge that we need to take, if we have a different price at the end of the quarter from the price we had at the beginning of the quarter. We don't do that in the other direction. We don't have to, by accounting rules. It's always a noncash charge. And calculating what the difference would be and applying EBITDA to it is something that we're not prepared to do.

Philip Ngotho, ABN AMRO Bank N.V., Research Division - Analyst [65]

Okay. But it is included in your EBITDA at the moment, right? So...

Jackson M. Dunckel, AMG Advanced Metallurgical Group N.V. - CFO & Member of Management Board [66]

Yes.

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [67]

No. It's a misunderstanding.

Jackson M. Dunckel, AMG Advanced Metallurgical Group N.V. - CFO & Member of Management Board [68]

Sorry. Please repeat what you think is included in our EBITDA.

Philip Ngotho, ABN AMRO Bank N.V., Research Division - Analyst [69]

Okay, so -- indeed, maybe to prevent misunderstanding. Because earlier the question was raised that if prices remain at these current levels, vanadium prices, you will see margins actually drop. Those are for Q2 base, I guess. And then actually my -- so the way I see it is because that's -- you're working with a certain inventory that you purchased at a lower price, and you're selling it now, selling it on -- at a higher price. So I'm wondering what the impact would be indeed if price remain at these levels? What's the margin impacts? Any -- or what's the EBITDA impact?

Heinz C. Schimmelbusch, AMG Advanced Metallurgical Group N.V. - Chairman of Management Board & CEO [70]

The margin -- Yes, again there is -- if you buy inventory at a higher price and the -- then of course there is a tendency to reduce the margin. When you apply that principle to the fourth quarter versus the third quarter, there is an effect of that, but it's not very large.

Operator [71]

There are no further questions at this time.

Steve Daniels, AMG Advanced Metallurgical Group N.V. - SVP [72]

Thank you, operator. If there's no further questions, we will close the call. Thank you, everyone, for your participation today.

Operator [73]

That concludes today's call. Thank you for your participation. You may now disconnect.