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MTX - Q3 2018 Minerals Technologies Inc Earnings Call

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PRESENTATION

Operator

Good day, everyone, and welcome to the Third Quarter 2018 Minerals Technologies Earnings Call. Today's call is being recorded.

At this time, I would like to turn the call over to Cindi Buckwalter, Vice President of Investor Relations and Corporate Communications for Minerals Technologies. Please go ahead, Ms. Buckwalter.

Cindi Buckwalter - *Minerals Technologies Inc. - VP of IR & Corporate Communications*

Thank you, Vicki.

Good morning, everyone, and welcome to our third quarter 2018 earnings conference call. Today's call will be led by Chief Executive Officer, Doug Dietrich; and Chief Financial Officer, Matt Garth. Following Doug and Matt's prepared remarks, we will open it up to questions.

I would like to remind you that beginning on Page 13 of our 2017 10-K, we list the various risk factors and conditions that may affect our future results. And I will also point out the safe harbor disclaimer on this slide.

Statements related to future performance by members of our team are subject to these limitations, cautionary remarks and conditions.

Now I'll turn the call over to Doug. Doug?

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

Thanks, Cindi. Good morning, everyone.

I will start off today by covering the highlights from our third quarter. I then want to take some time to walk you through how the company is positioned from a global trade standpoint. We've been getting a number of questions around how current and potential future tariffs impact us, so I thought I'd provide some information on the call today.

I also want to take some time to review our growth performance, the multiple levers we're using to manage inflationary cost pressures and the margin expansion we're driving and will continue to drive going forward. Then I'll turn it over to Matt for a more detailed discussion of our third quarter results and fourth quarter outlook.

We had a stronger third quarter with earnings per share up 7% to $1.27. Sales increased 9% to $464 million, which marked our fifth consecutive quarter of sales growth. Over this period, our top line growth has averaged 8%, and excluding foreign exchange and the Sivomatic acquisition, our real organic growth has averaged 5%. In a few moments, I'll take you through aspects of what's behind this and how our teams are driving it.

Combined sales in our minerals businesses grew 9% over last year. We continued our solid performance in Metalcasting and Household and Personal Care and had a strong sales quarter in Environmental Products, Ground Calcium Carbonate and Talc.

Sales in our services businesses grew 12%, driven by our Refractories business, which is benefiting from stronger market demand and higher steel mill capacity utilization rates.

Operating income grew on both a year-over-year and sequential basis to $69 million, and we achieved sequential margin improvement across all of our segments.

While we continue to be impacted by inflationary cost pressures, we offset all of the higher incremental costs in the quarter with higher prices and strong operating performance with focus on cost control and productivity improvements. We also made significant progress on a number of our growth initiatives. Construction of our new PCC satellite facilities are under way, we continue to ramp up our Bleaching Earth facility in Turkey and we commercialized several new products. In addition, Sivomatic has been fully integrated into the company, and the business is performing well and accretive to our earnings.

Several quarters ago, I mentioned that accelerating new product development was a key initiative and driver of growth for the company. We've made significant progress on this front and are bringing new, value-added products to market faster. I'll discuss this in more detail in a few minutes.

We continue to maintain our balanced approach to capital allocation. We made $30 million in debt repayments in the quarter, along with additional share repurchases.

As I mentioned, earnings per share grew 7% over last year to $1.27. Notably, this was a record level of EPS for a third quarter for the company. Year-to-date, earnings have grown 5% over last year. Matt will provide more guidance for our fourth quarter in a few minutes. However, we do see continuing this momentum and finishing with 5% to 6% EPS growth for the full year.

Over the past several months, many of our shareholders have been asking about how the current global trade dynamics and tariffs impact MTI, particularly as it relates to changing trade policy between China and the United States. So I thought it would be helpful to give some insight into our global raw materials and finished goods flows.

Each of our businesses, with the exception of Refractories, are primarily localized such that they source raw materials, manufacture and sell end products within the same country. We do, however, import a small amount of raw materials into the U.S. as well as export products to customers around the world. The quantity of these imports and exports are outlined in the 2 charts at the top of this slide.

As you can see, our trade flows into and out of the U.S. are relatively minimal. The pie chart on the top left shows the portion of raw materials we import into the U.S. from China as well as from the rest of the world. In total, these imports are less than 5% of our total manufacturing costs. Our primary raw material import is magnesium oxide for our North America Refractories business, which we - as well as our competitors - source from China and which does not currently have an imposed tariff into the U.S. We also export raw materials, primarily bentonite clay, from our Western U.S. mines to our international manufacturing locations. At the moment, only the bentonite going into China carries an 8% tariff.

The pie chart on the top right shows our finished goods exports from the U.S. Again, our main export from the U.S. is high-quality sodium bentonite from Wyoming sold as a finished good to third-party customers around the world. These exports are also relatively small, representing less than 2.5% of our total sales.

Given these relatively small trade values, the impact on MTI from the current tariff structure is less than $1 million. We've made adjustments to our pricing, where applicable, to cover these costs.

I also want to give some perspective on the geographic mix of our sales in order to dimension how changes in economic growth in each region may affect us.

The chart on the bottom right breaks out our sales by major geography for 2018 on a year-to-date annualized basis. The Americas is by far our largest sales region. Europe, the Middle East and Africa currently represent 24% of our sales. You can also see that China and the rest of Asia are relatively smaller regions for us, each at 9%.

Thus far, we've not seen any significant change in demand for our products in China. As you recall from our second quarter call, demand for both our PCC and green sand bond products in China are driven primarily by substitution of existing products rather than purely by end market demand.

We are seeing a slowdown in the automotive market in China, which is a significant end market for our foundry customers. However, our other industrial product foundry customers have remained strong. Thus far, we have not seen a significant impact on our green sand bond volumes. In fact, our green sand bond sales in China grew 7% in the third quarter, driven primarily by the successful conversion of foundry customers of existing in-house blends to our custom-engineered green sand bonds.

Paper production and our PCC volumes are also currently stable in China, and we see PCC volume growth into 2019 with a new 150,000-ton satellite we're constructing.

I hope this gives you some insight into how MTI is positioned from a global trade standpoint. We continue to keep a close eye on tariffs and the longer-term impacts that changing trade policies could have across all of our major products, end markets and geographies.

Before turning it over to Matt, I want to review some examples of how MTI's continuous improvement culture is being leveraged to deliver profitable growth, maintain strong operating performance and, over the past year, to navigate inflationary cost pressures.

For the past decade, we've advanced operational excellence and fostered a continuous improvement culture throughout our organization, facilitating a work environment where employees can engage with energy and suggestions to help solve problems. You can see from the charts in the middle of the page, our global team continues to drive out waste with a number of kaizen events aimed at improving our processes, growing over last year. Likewise, the number of suggestions from our employees for how we can do things better have also increased. These activities and suggestions compound each other and benefit the company's performance over long periods of time and through changing economic environments. These improvement activities have helped to accelerate our sales growth, to drive returns higher and recently to mitigate the cost pressures we've experienced. Let me give you a few examples.

For the past 2 years, continuous improvement activities have helped to drive accelerated new product development at MTI. Our innovation pipeline remains robust. As you can see from the small chart on the left side, we've increased the speed of product development by 20% from 2016 to 2018. This means we're developing our value-added products and services and delivering them to customers more quickly - in an average of 27 months.

So far this year, we've commercialized 31 new products, 24 of which were initiated, developed and commercialized within the past 3 years. A number of our newest technologies commercialized over this time frame are expected to contribute to revenue growth in the coming year, including Envirofil, a new, innovative recycling technology for the paper industry; and variations of our NewYield technology, which converts paper production waste into a usable filler. We've also been focused on leveraging our capabilities in water filtration, and applying them to large water remediation problems with our first sale of a new product called FLUORO-SORB, which is proving to be an economical process for removing fluorinated compounds from contaminated water.

We're also using these tools to support our geographic growth. Through standard processes and designs, we have the capability to simultaneously construct and start up multiple PCC satellite facilities in different regions. We are in the midst of the design and construction of 1 of 2 PCC facilities in Indonesia and another large satellite in China, which will add over 250,000 tons of PCC over the next 12 months, and we expect this growth to continue.

Standard processes are also used to drive value from acquisitions. We've applied them previously to the acquisition and integration of AMCOL, and we have, again, applied them to the integration of Sivomatic.

Across the company, our teams are focused on productivity improvements, identifying cost savings opportunities and finding ways to increase the utilization of our assets. For example, in India, our team found opportunities to expand the capacity of an existing PCC satellite by 15% without the need to spend capital to support volume growth for our customer. And we recently held a kaizen to improve our railcar loading processes at one of our large facilities, again avoiding capital expenditure, to expand shipping capacity to support volume growth.

Activities like these are occurring each day at MTI. There are thousands of similar examples across the company, each of them helping to drive our performance improvement to overcome challenges and to position the company for continued sales and profit growth.

Now I'll turn it over to Matt to give a deeper dive into our financial performance for the third quarter and the outlook for the fourth. Matt?

Matthew E. Garth - *Minerals Technologies Inc. - Senior VP of Finance & Treasury and CFO*

Thanks, Doug, and hello, everyone. I'll review our third quarter results, the performance of our 4 segments and also provide you with our outlook for the fourth quarter.

Third quarter sales grew 9% versus the prior year or 11% after adjusting for foreign exchange. Our sales growth was driven by higher pricing and higher volume across several product lines as well as the acquisition of Sivomatic, which generated $23.3 million of revenue or 5 percentage points of growth in the quarter.

In the third quarter, we continued to face inflationary increases in our raw materials, freight and energy costs, which has reduced our gross margin year-over-year. Strong business performance gains offset these higher costs, and in a few minutes, I'll show you how the actions we are taking are offsetting increasingly more of these inflationary costs and driving margins higher.

We continue to tightly manage SG&A and have reduced both the absolute and percentage expense year-over-year, including the addition of Sivomatic. SG&A costs were 10.9% of sales in the quarter, a 1.1 percentage point reduction from the prior year.

You can see from the operating income bridge on this slide that our business performance, including higher pricing and strong productivity improvements, delivered $13.6 million and more than offset higher inflationary costs of $12.9 million. Operating income rose 1% to $68.8 million and operating margin was 14.8% versus 16% in the prior year. On a margin basis, pass-through items such as freight sales combined with the higher inflationary costs to more than offset the margin benefit from our actions.

Earnings per share were $1.27, a 7% increase from the prior year, driven by the strong operating performance as well as the tax rate change.

Our effective tax rate was 19% in the quarter, which was relatively unchanged sequentially.

Now let's take a closer look at our progress in expanding our margins and driving profitability in the current inflationary environment.

On this slide, I'm comparing the second and third quarter of this year as MTI business conditions were similar in terms of seasonal customer demand. As you can see, inflationary costs have not reduced sequentially. In fact, they have increased by $3 million versus the second quarter primarily due to higher raw materials and energy costs. However, the actions we are taking to grow operating income and margins have outpaced these cost increases.

While our ability to drive pricing has been the largest factor in margin improvement, we are also seeing benefits from increased productivity, cost reduction and the commercialization of new products that Doug mentioned earlier, all of which helped to deliver $13.6 million in higher operating income year-over-year and an increase of $9.6 million from the second quarter. As a result, our operating margin has increased 90 basis points sequentially.

While we will experience typical seasonality on our sales and operating income in the fourth quarter, we will continue to take actions to drive margins higher into 2019.

So now let's go through our segments in more detail.

Performance Materials sales increased 16% compared to last year and operating income increased by 4%. The sales growth was driven by Household, Personal Care & Specialty Products, also known as HPC, as well as Environmental Products and Metalcasting. Excluding the sales from Sivomatic, HPC grew 14% on strong pet care demand in the U.S. and higher fabric care sales in Europe. In the quarter, the business absorbed $4.5 million of higher raw material and logistics costs, which we more than offset with $5.7 million of higher pricing across multiple product lines, improved operating conditions at our Western mines and the full integration of Sivomatic. Segment operating income was $31.8 million and operating margin was 14.5%, a sequential improvement of 50 basis points versus the second quarter.

Now looking to the fourth quarter, operating income will be lower by $2 million to $3 million due to the typical seasonality we experience in the Building Materials and the Environmental Products lines. We will see continued strong sales in Metalcasting and HPC. However, we also expect higher inflationary costs, which we will offset with higher pricing and productivity improvements.

Now let's turn to our Specialty Minerals segment.

Specialty Minerals sales were down slightly year-over-year at $146.3 million. In PCC, growth in Asia and stronger specialty PCC sales partially offset the paper machine shutdowns in North America earlier this year. As Doug mentioned, we continue to make good progress on our new Paper PCC satellites.

Processed Minerals sales grew 4% as higher volumes in the automotive and construction markets increased sales in Talc and Ground Calcium Carbonate, respectively. Segment operating income was $25 million, down $1.6 million from last year. The segment faced inflationary cost increases of $3.1 million comprised of higher energy and lime costs, as well as lower North American PCC volumes due to the previously mentioned shutdowns. We partially offset the higher costs through price increases, including contractual pricing in Paper PCC and higher pricing across our Performance Minerals businesses.

Turning to the fourth quarter, we expect Paper PCC volumes to be stable in North America and Europe and for volumes to grow in Asia. We will be absorbing higher lime costs, as is typical in rising energy price periods, that we cannot contractually pass on to our customers until the first quarter of 2019. In Performance Minerals, we will continue with pricing actions to recover higher costs. However, this business will experience its typical seasonality moving from the third to the fourth quarter. Overall for this segment, we expect operating income to be lower by $2 million sequentially.

Now let's turn to Refractories.

Refractories segment sales increased 15% and operating income increased 16%. Refractory product sales were up 18% on steel utilization rates trending around 76% globally and in the North American and European regions, where we are most concentrated. We are making good progress on our pricing and innovation activities to mitigate raw material inflation, which has totaled $15 million year-to-date, including increases in magnesium oxide and our other raw materials. This segment continues to perform well in the current environment, and operating margin remained strong at 14.5% in the quarter.

Now looking to the fourth quarter, we see continued strong steel market conditions and expect segment operating income to be similar to the third quarter.

Let's move to Energy Services.

Sales in Energy Services were at a similar level to the prior year and operating income was $1.4 million versus $1.6 million last year. On a sequential basis, operating income increased 27%, driven by a shift in mix to filtration work. Overall offshore market activity remains relatively low, while competitive bidding activity continues to be high in the Gulf of Mexico across all of our product lines. Currently, we see a similar operating income to the third quarter, and we have a healthy pipeline of projects for the first half of 2019. As a reminder, the incremental margins are very strong in this business, and a pickup in offshore activity will quickly yield higher profitability.

Now let's review our liquidity and debt highlights.

Our cash and short-term investments stand at $211 million at the end of the third quarter. We continue to take a balanced approach to strengthen the balance sheet and improve the position of our businesses.

Let me highlight a few actions that we have taken this year.

First, over the last 3 quarters, strong cash flows have allowed us to make additional discretionary pension contributions of $13 million to take advantage of a one-time opportunity in 2018 to maximize our tax benefit related to pension funding.

Second, we have deployed $56 million of capital in our business to strengthen and maintain our current operations and fund expansion to support new customer demand globally.

Third, we have returned cash to shareholders through the repurchase of $16.4 million of shares year-to-date, which more than offsets dilution from employee share plans over the last 2 years.

And finally, we repaid $30 million of debt in the quarter, bringing our net leverage ratio to 2.4x EBITDA.

Adjusting for discretionary pension contributions, we have generated $90 million of free cash flow year-to-date, and we expect strong cash flow generation in the fourth quarter as well. For the full year, we estimate free cash flow, adjusted for pension contributions, to be in the range of $140 million to $150 million.

So now let me summarize.

We expect a strong fourth quarter versus last year, along with the typical seasonality sequentially. Versus the third quarter, we see operating income to be lower by $2 million to $3 million in Performance Materials, lower by $2 million in Specialty Minerals and similar operating income to the third quarter in both Refractories and Energy Services. Strong top line growth will continue across our product lines. And while we will see higher costs, we don't expect them to increase at the same pace as the first 3 quarters of this year. We remain focused on driving pricing actions and operational excellence to expand margins. In addition, the accretion from Sivomatic will fully offset the year-over-year impact from our exit of the bulk chromite business. In total, fourth quarter earnings per share will be around $1.15, continuing our trend of 5% EPS growth this year.

And now let's move to the Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And we will take our first question today from Daniel Moore with CJS Securities.

Daniel Joseph Moore - *CJS Securities, Inc. - Director of Research*

One, to start, Environmental Products saw a nice uptick in revenue in the quarter. The projects that drove revenue higher in Q3 are those largely completed. Did some of that spill into Q4? And more critically, just talk about the pipeline and the outlook there for increased activity as we look into '19.

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

Yes, Dan, let me start off and I'll pass it over to Jon. We did have some -- a nice sales increase in the quarter. We've had some larger projects. We're also starting to see some sales, as I mentioned, in some higher-margin products and new technologies that we've been releasing. Some of these probably won't move into the fourth quarter. I think what we see is the third quarter being a peak and timing of landfill lining and other lining. The weather gets a little bit adverse for doing this type of work in the fourth quarter. So I think we've completed most of those.

Jon, you want to talk a little bit about what you see in the pipeline going forward?

Jonathan J. Hastings - *Minerals Technologies Inc. - Group President of Performance Materials*

Sure. Dan, It's Jon. I guess a couple of things. So like Doug said, the growth was really in 2 sectors. We serve a variety, but the focus over the quarter was in mining and also in remediation. In mining, what we saw is continued progress with our base GCLs. And the remediation, it's using some of our specialty products. So fairly well balanced. And as we go forward, what we're looking forward at is a construction market that's expected to slow somewhat. But we still expect to continue to outpace the market, and that's because of some of the innovations that we're bringing forward. We've launched our FLUORO-SORB. We mentioned that on the highlights. We've launched the FLUORO-SORB technology that's aimed at water remediation, and we continue to innovate and tailor our products specifically to the needs of the customers. So again, we continue to see some growth going forward.

Daniel Joseph Moore - *CJS Securities, Inc. - Director of Research*

Helpful. And then switching gears to bigger PCC. Doug, what would you -- how would you characterize the sort of worldwide outlook for sales in 2019? And then given the 250,000 tons coming online for your business, can you just kind of remind us as to when you - we would expect revenue growth to inflect positively once again?

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

Yes. So we're currently building, as I mentioned, those facilities, 3 facilities. We've got 200 -- we've got 450,000 tons under contract we'll probably be building. We expanded 40,000 tons already this year, one of our facilities in Indonesia. Another 250,000 tons, we feel, coming online next year. And that last one in Indonesia right now, we're looking at working at the mix of products. It might not only be a pure filler plant. We might be looking at mixing in some of our newer technologies like NewYield into that one. So that one's a little bit delayed only because we're working through exactly what products the customer and technologies the customer would like to use. We see that adding growth all throughout next year. I mentioned that in my comments. I think the inflection point you'll see probably coming in the second -- late second quarter as these start to come online, into the third. We're still getting some year-over-year impact in the first quarter from the shutdowns we experienced this year. So I think in the second and third quarter, you'll see those come online and you'll see that inflection.

Overall for paper, the market has been pretty stable right now in China. Seen some good results here in North America as well. We're benefiting from that. But as you know, our demand growth and our -- and how we grow internationally has been in conversion of existing products. So as the paper market remains slow growth in China and India, we're growing very quickly by converting other pigments to PCC. We've got a strong pipeline. Why don't I let D.J. take you through a little bit of the pipeline for those projects and also our new technologies?

D. J. Monagle - *Minerals Technologies Inc. - Group President for Specialty Minerals & Refractories*

Yes. Thanks, Doug. Dan, thanks for the question. So Doug hit 2019 pretty well, but I'd also just start off with saying that there's an awful lot of conversations. When I say awful lot, something in the neighborhood of 5 to 10 locations where we're just talking about some incremental expansions. They range -- a couple in the U.S., but there'll be further expansions in the Asian market. On top of that, we're actively pursuing several satellites that we think we can capture in the coming months. So it's hard to predict exactly when those come in. So we've highlighted the pipeline is pretty robust everywhere. Right now it's pretty active conversations between half a dozen and a dozen papermakers going around the world in China, India, some in the U.S. even and some conversations in Brazil and Europe as well. And they are the standard PCC products but also advanced conversations with both NewYield that Doug alluded to earlier and Envirofil. And in regard to Envirofil, we believe -- we know we'll be commercializing Envirofil in Europe in the coming months. And then, I guess, to cap it off, we've been doing an awful lot of work in packaging. And it's packaging in white boxes and brown boxes. And we're in advanced conversations on some new satellites that would support business in the packaging sector. So quite a bit going on that Doug highlighted in the 2019 outlook, but we think we'll be bringing on some -- even more to take us beyond that.

Daniel Joseph Moore - *CJS Securities, Inc. - Director of Research*

Excellent, very helpful. Last one from me. I'll jump out. Maybe a question for Matt. Slide 10, I thought, was really helpful. Maybe just delineate the improvement in business performance sequentially. How much of that was price versus operating efficiency improvements?

Matthew E. Garth - *Minerals Technologies Inc. - Senior VP of Finance & Treasury and CFO*

Yes. Of the $13.6 million, about $11 million of it was price and the rest was split between other productivity improvements.

Operator

Next is Rosemarie Morbelli with Gabelli & Company.

Rosemarie Jeanne Pitras-Morbelli - *G. Research, LLC - Research Analyst*

If you -- Doug, if you eliminate the shutdown of the machines in the U.S., on the paper machines, what was the PCC growth in China versus a decline here?

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

Year-to-date PCC volumes, I believe, are up above 2% to 3% in total for the year. I've got to make sure that that's the correct number. I think that we've seen higher -- we've seen volume growth in Europe. We've seen flat PCC volumes in Latin America. Net net, I think our volumes are slightly down for the year, but that's largely due to those tons that came out of North America. So the rest of the regions have been up despite that North American beginning of the year.

Rosemarie Jeanne Pitras-Morbelli - *G. Research, LLC - Research Analyst*

So you say -- and can you -- do you have a number for the growth rate in China?

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

Matt, do you have our growth rate in China?

Matthew E. Garth - *Minerals Technologies Inc. - Senior VP of Finance & Treasury and CFO*

Yes, let me calculate that for you. So sales were up about 13% in China, Rosemarie.

Rosemarie Jeanne Pitras-Morbelli - *G. Research, LLC - Research Analyst*

Okay. And no real price in that? So it's mostly volume? Or is it half and half?

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

It's mostly -- well, it's probably equal price and volume. We do have some price pass-through from higher lime, but it's probably balanced between price and volume. Volumes are up in our Asia region.

Rosemarie Jeanne Pitras-Morbelli - *G. Research, LLC - Research Analyst*

Okay. And then moving on to Metalcasting growth in -- it seems to be softer in -- than it was in the first half. So can you go all of the reasons other than owe to slowing down, but then you said that you are substituting. So what is really happening in terms of the level of growth second half versus first half or Q3 versus first half?

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

Yes, we see another strong quarter in the fourth quarter in Metalcasting in China. The third quarter is a little bit slower. I know we've been giving you kind of double-digit numbers over the past couple of quarters in terms of growth in China. August, it was a very slow period for automotive, and it's just in general. It wasn't just automotive, it was industrial production. And it typically does that in August in China. So we saw that this year and so that our growth was about 7%. I think in the second quarter, it's probably 12%. So we don't see that that's due to a major slowdown. We do see that automotive has started to slow. That will impact our demand somewhat. I still think we can maintain the 7% to 8%-type growth rate on an annualized basis despite the automotive slowdown. And like I said, this quarter, that was driven by the conversion of customers to our engineered products. And so those are higher-margin, higher-revenue-type tons. And so we've been successful in that conversion, and we continue to do so. Jon, you want to give a little more color on how we're doing that?

Jonathan J. Hastings - *Minerals Technologies Inc. - Group President of Performance Materials*

Sure. And talking about China specifically, you'll see that our sales go in a couple of different sectors, Rosemarie. The first is auto that we talked about. But we also have the engineering segment. That remains very robust year-on-year. I think it's grown about 50%. So very good, strong growth there. Also, we sell into the construction industry. That remained flat, but all those foundries right now are running at capacity. So we see that continuing. Of course, the way we do this is we work with our customers. We understand what their lines are and what their rates are. As far as any imperfections in the foundries themselves, we tailor our products specifically to them. And we work with them once we actually commercialize and implement the products going forward. So we kind of continuously tailor our products, the blends and the composition of those blends. We do have a sales team that's focused on continued growth. And like I've said, as we look out to Q4, although we had a bit of a slowdown there in Q3 due to some heat-related events, we do see high single-digit growth going into the fourth quarter.

Rosemarie Jeanne Pitras-Morbelli - *G. Research, LLC - Research Analyst*

Okay. And then lastly, if I may, on the margin side, you have been improving margin sequentially. And obviously, the actions you're taking in-house plus price increases are offsetting some of your raw material cost inflation. When do you think you will be able to fully offset the inflationary environment and go back to prior year margin?

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

We've said that we do lag a little bit, some of it contractually, Rosemarie. We are going to absorb lime cost increases, as we typically do in rising cost periods, in the fourth quarter. And we won't be able to pass those through until the beginning of the year, the first quarter. So there is a lag. We are -- we feel we'll be getting ahead of this. It'll be into next year. But that will depend on how these inflationary costs continue to taper or start to taper. We've seen some of that in the fourth quarter, but we are facing higher costs in other areas, logistics, energy and, as I just mentioned, lime. I think as we get through the first quarter of next year, I think we're going to be on track to catch back up to those historic margins. I will caution you, though, that some of our product mix has changed. And so you do see with chromite, we've highlighted that before, and some other product mixes has changed our mix a little bit. But nonetheless, we still see kind of that 15% -- plus 15% to 16% range possible for the company over the coming quarters.

Operator

Next is Silke Kueck with JP Morgan.

Silke Kueck-Valdes - *JP Morgan Chase & Co, Research Division - VP*

So in the quarter, I guess, sales were like 9.5%. Your SG&A was down a little bit. And I think your R&D was down like $1 million, like 15%. Is that still like a level that you can maintain? So like the cost controls were really noticeable in the quarter. Is that something that you'll -- that we'll see in the fourth quarter and that you'll continue to manage in this way?

Matthew E. Garth - *Minerals Technologies Inc. - Senior VP of Finance & Treasury and CFO*

Yes, Silke, I think we've proven this year we've been able to significantly lock down our SG&A expense. And like I said in the prepared remarks, we were able to absorb Sivomatic SG&A and still generate lower overall SG&A for the company through the course of the year. Let's put there, like you said, SG&A is holding and R&D is coming down a little bit. So -- and I think Doug also laid out for you, and Doug will probably want to share a few more words on this, how we're improving through operational excellence our R&D program and the product development pipeline.

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

Yes, Silke, I think when you look at the R&D number, it is a bit lower. Part of our R&D spend that goes in there is trial activity, and so you might see a quarter that has a number of trials that were -- that have come across or -- with customers throughout our company, and this quarter, I think, might have been a little bit lighter. But I wouldn't read too deeply into that lower R&D. Like Matt said, though, it's part of our -- I kind of mentioned the culture of the company to maintain a cost. And we look to keep our overhead as tight as possible. Something new comes in that we want to spend money on, and we think that there's probably something that's out there that we shouldn't be doing anymore and we eliminate it. Something in, something out. But we do that as -- just as a matter of course to hopefully get that leverage from all those new sales that are coming in internationally. As you know, we've got a shared service environment in the company. We leverage that through -- in a great way -- for acquisitions. Matt just mentioned we took on Sivomatic and yet expenses are flat. And that's largely because we found ways to offset that increase by leveraging the existing system we have in place. And so that's how we do it. I think you're starting to see the higher sales over a similar base, drop that ratio. And that's what happened in the quarter.

Silke Kueck-Valdes - *JP Morgan Chase & Co, Research Division - VP*

Secondly, it looks like for the quarter, price or price mix was maybe up 3% or maybe it's up at 3.2%. How much of that is freight pass-through and how much of that is price/mix?

Matthew E. Garth - *Minerals Technologies Inc. - Senior VP of Finance & Treasury and CFO*

Yes, the freight was about $6 million in the quarter, Silke, and that, if you'll remember, is similar to what we had last quarter. So on the revenue line, that's where it puts you. Freight ended up being about a $7 million increase when you look at it on a year-over-year basis. So that's part of that higher raw material, freight and energy cost bucket, about $1 million is related to freight.

Silke Kueck-Valdes - *JP Morgan Chase & Co, Research Division - VP*

Okay. Okay. On the -- in the Performance Materials segment, with the chromite business now exited. It's sort of like some -- like in the $24 million and $25 million, is that like a right run -- level of sales that you expect for that particular division in Performance Materials?

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

I'm sorry, our current...

Silke Kueck-Valdes - *JP Morgan Chase & Co, Research Division - VP*

I apologize. And so there's a Basic Minerals segment within Performance Materials that you set the chromite business in it. And -- but it looks like it now sort of generates sales of like $24 million and $25 million a quarter. Is that the right -- is that sort of like the way to think about it going forward? Or is there more fluctuation than that?

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

No, that's -- the chromite -- I think that's the current run rate. We do see some increase in sales with Basic Minerals. What's in there are 3 major items -- or 2 major items. One is our drilling products. So oil and gas drilling, that's basic bentonite that's sold into that market but also iron ore pelletizing. And so you'll see possibly some increase as steel activity but also drilling activity increases. Those are in those categories. But yes, this is a -- probably a good adjusted run rate now that chromite, which used to be in that category, is now out on a full year basis.

Silke Kueck-Valdes - *JP Morgan Chase & Co, Research Division - VP*

Yes. And in Building Materials, you had sort of like the seasonal slowdown, and -- but other companies have talked about their building product divisions slowing. So like DowDuPont talked about it. I think like Sherwin-Williams talked about it. Are you beginning to see that, that business is generally softer in the U.S. end markets?

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

We've seeing a little bit, I guess. Last year, we had a lot of major projects mostly in the West Coast. And so a lot of our waterproofing projects kind of around the world are sizable. We do have some smaller projects that come on here and there, but these are pretty sizable projects. So what you saw at least this quarter over last was more of a year-over-year comparison for something we had in California last year that didn't repeat itself. We had a really strong -- having a pretty strong year in Europe. And so far this year in North America, it's been okay. We are cautious, though, that we're going to start to see some slowdown in construction, but we haven't seen it yet, Silke. I do think that our pipeline of projects, as Jon just mentioned environmental, will probably carry us into the beginning of next year. But beyond that, that's about the time frame of our pipeline that we can see in terms of what's really out there. And probably, I'll have a little bit more information if things are changing after the fourth quarter. But right now it looks pretty solid.

Operator

(Operator Instructions) And we will now go to Curt Siegmeyer with KeyBanc Capital Markets.

Curtis Alan Siegmeyer - *KeyBanc Capital Markets Inc., Research Division - Associate*

Most of my questions have been answered, but you've talked about a 5% higher volume growth in your Talc business driven by auto and construction. So I was just wondering, given some of your commentary around being a little bit more cautious around those end markets, if you think that volume growth in that business is sustainable over the next couple of quarters.

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

I do. But there's a couple of other components to that. Heavy truck is where we supply Talc, into catalytic converters. It's been very strong. Also highway. And that's a global business. We do ship our talc globally. So it's not just automotive. The automotive piece of that Talc business is plastics, which still is remaining fairly strong. We have a sizable position in that market in North America. And so -- and we've been growing it with some higher-quality talc products. So right now we see that that's pretty solid. Like I said, it's not just automotive. We've been seeing some very strong markets in heavy truck as well, which has really been driving this past quarter's growth.

Curtis Alan Siegmeyer - *KeyBanc Capital Markets Inc., Research Division - Associate*

Got it. And then your balance sheet is in pretty good shape, under 2.5x leverage post acquisition. So just wondering how you'll be thinking about M&A in 2019.

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

Well, M&A is a core piece of our growth strategy. Yes, we'd like to highlight the fact that we can -- we feel we've got a balance sheet that's strong enough for something like a Sivomatic, to buy it, integrate it and pay for it all in the same year. And I think you'll probably see that happen this year. So that's the first piece. The second piece is so continuing to keep the balance sheet in a good spot to enable us to act on something that -- an acquisition that comes our way. Right now, like I said, we've got a good pipeline of targets. We're pretty patient, though, with that. We know what we're looking for and not always that -- that's not always for sale, as we've seen. But we have a good pipeline. We meet weekly as a team to go through those activities. And yes, keeping the balance sheet in shape to not only act on acquisitions but also in shape to continue to position the company for organic growth and to weather cycles, if that make -- and come out right in the next couple years. So yes, it's a strategic part of what we do, and we've got a good -- we have a good pipeline of targets out there that we can act on with our balance sheet.

Matthew E. Garth - *Minerals Technologies Inc. - Senior VP of Finance & Treasury and CFO*

And Curt, let me just add on to that, that I think you probably know, but for everyone's edification, the target is to be 2x levered, net leverage against EBITDA. And as Doug said, we have a pathway to get back to around 2x over the coming quarters, which will allow us, over the course of a full year of owning Sivomatic, to have it paid down.

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

Does that help, Curt?

Curtis Alan Siegmeyer - *KeyBanc Capital Markets Inc., Research Division - Associate*

Got it. Yes.

Operator

And Rosemary Morbelli with Gabelli & Company has a follow-up question.

Rosemarie Jeanne Pitras-Morbelli - *G. Research, LLC - Research Analyst*

I was wondering, talking about M&A., if you're seeing a decline in the valuations or if people -- I mean, property owners still want the high-values -- if they are going to sell.

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

There's quite a bit of -- fewer transactions the past couple of months. I think in the first half of this year over the summer like we mentioned, I think, on the last call, that multiples were pretty high. We've looked at some opportunities, but things had been going for north of 13x, which is something that we just felt that it's obviously not something we're going to be able to generate a return on. So I think that they could be coming down into more reasonable levels. I haven't seen that yet. But right now, stuff that we've seen transacted are pretty high, still pretty rich in terms of multiples.

Rosemarie Jeanne Pitras-Morbelli - *G. Research, LLC - Research Analyst*

And then lastly, could you give us a feel for the internal growth at Sivomatic year-over-year?

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

Sure. How about I let Jon talk about that?

Jonathan J. Hastings - *Minerals Technologies Inc. - Group President of Performance Materials*

Yes, Rosemarie, Sivomatic on an annual basis is now growing at about 8% per year. That's a little bit north of where we predicted. But they've done some really nice things. They've got a really unique ore deposit in Turkey that they leverage in all the markets in Europe. They continually innovate with that ore position. They introduce some new products on a fairly frequent basis and are targeting that high end. So they're customizing and they're going into the high end of the -- or the market in Europe. So continued growth. We do look to other potential geographies within the European continent to enter. And also, we're thinking about what we might be able to do with that ore in other regions of the world. So it's been a very nice position for us, and their growth has been very, very acceptable.

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

And I'll add to that, Rosemarie, that we've talked a lot about just Europe and that new position in packaged cat litter in Europe but also in Asia. We've been introducing -- we've talked about -- we haven't talked about it in a few calls, but China and Southeast Asia, where we're introducing new fragrance packages, our lightweight cat litter program, and so we've had some nice growth there as well. So this is shaping up to be a nice business for us. We like that consumer product business. It's -- we're now a bigger footprint around the world, where we have dialogues with global consumer products companies. And it puts us in one of the larger positions from a private label kind of cat litter business. And that's a good position to innovate from - to drive premiumization - and now we have kind of a global spot to do that from. So we like the acquisition, as Jon said, and we're looking at other ways to leverage it from those mines in Turkey.

Rosemarie Jeanne Pitras-Morbelli - *G. Research, LLC - Research Analyst*

You didn't say anything about introducing it in the U.S. Is it that the U.S. market would not be interested in a vanilla-smelling cat litter, for example?

Douglas T. Dietrich - *Minerals Technologies Inc. - CEO & Director*

We have, I don't know, how many variations? We -- I probably shouldn't say we probably have too many SKUs in North America, but we like to customize and meet customers' demands. And so we've got a number of different categories of cat litter for our customers. I can't say vanilla is one of them, but we have the capability to pretty much meet what our customers are looking for. I have to say we are taking -- Sivomatic is very good at what they do, as Jon mentioned. And so we are leveraging some of that knowledge and that marketing capability that -- or they've accomplished in Europe and North America.

A little bit different business for us here. We supply all channels. We have our own brands. We supply private label to customers, and we sell bulk throughout the United States to other branded customers as well. So a little bit different business for us here, but a nice position in both regions.

Operator

And there are no other questions. At this time, I'd like to turn it back to Ms. Buckwalter for any additional or closing remarks.

Cindi Buckwalter - *Minerals Technologies Inc. - VP of IR & Corporate Communications*

Thank you, Vicki.

Thank you all for joining us today. We look forward to speaking with you again very soon. Have a good day.

Operator

Thank you very much. That does conclude our conference for today. I'd like to thank everyone for your participation, and you may now disconnect.
