PPG

Fourth Quarter 2018 Earnings Conference Call

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CORPORATE PARTICIPANTS

Michael McGarry – *Chairman & Chief Executive Officer*

Vincent Morales – *Senior Vice President & Chief Financial Officer*

John Bruno – *Director Investor Relations*

PRESENTATION

Operator
Good afternoon and welcome to the PPG Fourth Quarter 2018 Earnings Conference Call. My name is Andrea and I will be you conference specialist today. All participants will be in listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star key followed by zero. After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press star then one on your telephone keypad. To withdraw your question, please press star then two. Please note this event is being recorded.

I would now like to turn the conference over to John Bruno, Director of Investor Relations. Please go ahead.

John Bruno
Thank you, Andrea, and good afternoon, everyone. Once again, this is John Bruno, Director of Investor Relations. We appreciate your continued interest in PPG and welcome you to our fourth quarter 2018 financial results conference call. Joining me on the call from PPG are Michael McGarry, Chairman and Chief Executive Officer and Vince Morales, Senior Vice President and Chief Financial Officer.

Our comments relate to the financial information released on Thursday, January 17, 2019. I will remind everyone that we've posted detailed commentary and the company presentation slides on the Investor Center of our website, www.PPG.com. The slides are also available on the webcast site for this call and provide additional support to the opening comments Michael will make shortly.

Following Michael's perspective on the company's results for the quarter and the full-year, and a brief update from Vince, we will move to a Q&A session. Both the prepared commentary and discussion during this call may contain forward-looking statements reflecting the company's current view of future events and their potential effect on PPG's operating and financial performance.

These statements involve uncertainties and risks which may cause actual results to differ. The company is under no obligation to provide subsequent updates to these forward-looking statements. The presentation materials may also contain certain non-GAAP financial measures. The company has provided, in the appendix of the presentation, materials which are available on our website, reconciliations of these non-GAAP financial measures, to the most directly comparable GAAP financial measures. For additional information, please refer to PPG's filings with the FCC.

Now, let me introduce PPG Chairman and CEO, Michael McGarry.

Michael McGarry
Thank you, John, and good afternoon, everyone. Today, we reported fourth quarter and full-year 2018 financial results. For the fourth quarter, our net sales were approximately $3.6 billion and our adjusted earnings per diluted share from continued operations were $1.15. Our adjusted EPS were impacted by continuing raw material and logistics cost inflation, materially lower automotive builds in China and Europe, and significant foreign exchange translation headwinds.

While our net sales and adjusted EPS results did not meet our growth expectations, we continued our momentum and operating margin recovery. Although we continued to experience additional inflation during the quarter, we made further progress in selling price realization and continued our legacy of

strong cost management. For the fourth quarter, our sales in local currencies increased about 2%, supporting the higher local currency sales were selling price increases of nearly 2.5%, marking the seventh consecutive quarter of sequential improvement.

Our sales volumes were down about 1% and were flat excluding the previously communicated customer assortment changes in our US architectural coatings DIY business. Foreign currency translation was slightly unfavorable to sales as the US dollar continued to strengthen during the quarter in several major currencies. Sales were unfavorably impacted by approximately $110 million US dollars and pre-tax income was impacted by about $12 million.

Moving to some business trends in the fourth quarter. In the performance coating segment, aerospace continued to deliver outstanding results with second consecutive quarter of volume percentage growth in the low teens. We also had good sales growth contributions from protective marine coatings. Automotive refinish sales were lower, as expected, due to continuing customer inventory destocking in the US. We believe the destocking has run its course and we expect better sales trends in the first quarter of 2019.

Overall, architectural coating sales volumes in the Americas and Asia-Pacific business decreased due to lower DIY sales of about $40 million stemming from the customer assortment change. Same store company-owned sales growth in the US and Canada continued, albeit at a lower level than the third quarter, impacted by more difficult comparisons to the prior fourth quarter when there was a spike in demand due to rebuild activity after the hurricanes of last year.

We finished the year with about 900 company-owned stores consistent with prior years. We added stores in certain targeted growth areas and closed underperforming stores. We also moved certain geographies to a delivery model. PPG Comex also delivered another solid quarter, capping off another great year for this business. For the year, PPG Comex added nearly 200 new stores in 2018, bringing their total to over 4,600.

In our industrial coatings reporting segment, sales volumes were negatively impacted by very weak industrial production activity in China. In the quarter, automotive builds were down 16% in China for the industry with lower builds in each successive month during the quarter. Automotive demand was also soft in Europe. Overall, our automotive sales volumes were lower by a mid-single digit, which is consistent with lower global industry demand.

The industrial weakness in China also impacted our general industrial business this quarter, including softness in coil, appliance, and extrusion subsegments. Globally, our general industrial sales volumes were up a low single digit percentage as sales volume growth was achieved in other major regions. Our packaging coatings sales volumes grew a low single digit percentage driven by higher volumes in the US and Canada and Latin America.

As we said after the third quarter, which we expect growth to moderate with more modest level of technology conversions in the industry and a reflection of the growth we delivered in prior years. From an earnings perspective, our fourth quarter adjusted earnings per diluted share was $1.15 which is $0.04 lower than the prior year. In the quarter, raw material costs increased about 4% year-over-year and that flattened on a sequential basis.

This is the ninth consecutive quarter of year-over-year raw material inflation with an accumulative total of more than 10%. Prices increased about 2.5% on a year-over-year basis with solid contributions from both of our reporting segments. We have secured further price increases for the first quarter and will continue to prioritize working with our customers on further selling price initiatives during 2019, as we are still trailing the raw material cost inflation we've incurred to date.

In addition to successfully selling price increase initiatives, we continue to make progress through aggressive cost management. We are able to achieve savings from our business restructuring actions of more than $20 million in the fourth quarter 2018 and reduce our selling, general and administrative costs, as a percentage of sales, by 130 basis points.

We are pleased to report that we were able to increase price in both automotive OEM as well as China. These are significant milestones on our way to margin recovery, but both OEM and China are well below prior margins and more price increases are required to offset raw material inflation.

Now, I'd like to quickly comment on our full-year results from continued operations. On a full-year basis, our sales from continued operations were approximately $15.4 billion or more than 4% higher than prior year. This growth was realized despite weakening automotive OEM market conditions and the partial year unfavorable impact from customer assortment change in our US architectural DIY business. Our sales growth was also aided by higher selling prices of about 2%.

For the full-year 2018, adjusted earnings per diluted share was $5.92, higher than prior year despite significant raw material and logistics cost inflation incurred throughout the year. In addition, earnings per share benefitted from our ongoing past deployment actions. This included the impact of our repurchase of nearly $400 million of PPG stock in the fourth quarter, bringing our full-year 2018 share repurchase total to more than $1.7 billion or over nearly 16 million shares. In the quarter, average diluted shares outstanding were 6% lower than the fourth quarter of 2017.

We continue to drive operational execution. Some of our more significant actions included continued successful integration from prior and current year acquisitions. We announced 6 new acquisitions and now have completed or announced 21 acquisitions since the beginning of 2015 continuing the commercialization of new products and technologies, allowing us to deliver above market growth in several of our businesses, delivering on our previously announced restructuring program including achievement of our cost savings commitments which totaled about $80 million for the full-year, and reducing selling general administrative cost as a percentage of sales by 90 basis points.

In addition to these operational items, we strengthened our relationship with key customers all over the world. As an example, we are very proud with the opportunity we've been given at the Home Depot and expect that this will deliver further benefits as we move into 2019. We also continued our strong cash generation, with about $1.5 billion generated from continued operations for the year.

In addition, consistent with our capital allocation commitments, we returned cash to our shareholders with nearly $2.2 billion in share repurchases and dividends. Regarding dividends, we are proud that 2018 marked the 119th consecutive year of annual dividend payouts and the 47th consecutive year of annual payout increases after a 7% per share increase in September 2018.

As we start 2019, while we are confident that the global economy will grow in 2019, there's a heightened level of uncertainty over the level of growth. In addition, we see short-term pressures such as a sluggish industrial activity in China and slowing demand in Europe that will negatively impact the first half of 2019. We have provided further details to our 2019 financial objectives which Vince will cover in a few minutes.

Let me briefly cover our expectations at a regional level. We anticipate positive economic growth rates to continue in the US and Canada, albeit at a lower level than experienced in 2018. Higher interest rates will likely drive slower growth in the US housing market and also impact auto sales, as we expect US automotive builds to modestly decline in 2019. In Latin America, we anticipate economic expansion in

Mexico and in South America we expect continued improvement in addition to our 2018 growth. Growth rates in Asia are expected to be moderate with softening industrial production growth in China in the first half of 2019.

Regional automotive build growth is expected to be flat to slightly up for the year, reflecting higher projected builds in the second half of 2019. Economic growth in Europe is expected to be modest and varied by subregion and country. Favorable end-use market trends are expected to continue. We expect very modest growth in automotive OEM coatings as industry build growth rates are expected to remain slightly positive.

With a more challenging economic landscape forecast for 2019, we will aggressively manage all elements of our business within our control to ensure that we remain competitive. We'll continue to execute our restructuring actions focused on reducing our overall cost structure and pursue additional growth-related initiatives. We expect raw material inflation to persist at current levels, at least through the first two quarters. We'll continue to work with our customers for additional selling price increases in 2019.

Finally, we ended the year with about $1 billion of cash in short-term investments and continue to believe that there are many coatings acquisition opportunities and our acquisition pipeline remains active across geographies and in use markets. We will continue to pursue accretive acquisitions.

As I noted in the press release earlier today, PPG remains well-positioned strategically and financially to deliver increased value to our shareholders as well as to our customers worldwide given the company's outstanding team, differentiated industry experience, broad footprint, and product innovation engine. We are looking forward to delivering on the targets we announce in 2019.

Before I ask Vince to comment on 2019 financial assumptions, I wanted to provide an update on the remediation measures we have taken to address the accounting matters that were the subject of the Board Audit Committee investigation in 2018. As I have previously mentioned, I have been personally involved in monitoring the remediation activities and can now report that, as of the end of 2018, all of the remedial measures that we have previously disclosed have been implemented.

This has been a top priority for me, and my leadership team and I want to thank everybody that was involved in supporting our efforts. The company continues to fully cooperate with the SEC's ongoing investigation relating to these accounting matters and is also fully cooperating with an investigation into the same accounting matters commenced by the US Attorney's office for the Western District of Pennsylvania.

As I have stated before, we take these matters very seriously and remain fully committed to actions that are consistent with our ethics and values and fully meet the expectations of both internal and external stakeholders. Since these are open investigations, we will have no further comments.

Now, I'll turn it over to Vince who will cover some 2019 financial assumptions.

Vince Morales
Thank you, Michael, and good afternoon, everyone. Earlier today, we published certain 2019 financial targets. Additionally, and similar to prior years, we've included in today's presentation materials various detailed financial assumptions for the first quarter and full-year 2019. They're located on slides 10 and 11. I will discuss a few of these financial assumptions, both for the quarter and the year.

With regard to the full-year 2019 assumptions, we did provide annual sales guidance and annual EPS guidance. With respect to the sales guidance, we anticipate sales growth in local currencies of 3% to

5%. This includes the acquisitions we recently announced and also includes the unfavorable impact from the customer assortment changes in our US architectural coatings business that will be realized throughout the first half of the year.

From an EPS perspective, we expect EPS growth, excluding the impact of foreign currency translation of 7% to 10%. As we noted in our financial target press release, the earnings portion of our long-term management incentive compensation will be predicated on us hitting a minimum of 10% EPS growth as our earnings-related metric for the variable incentive comp that ensures very strong alignment with shareholder value creation.

What is very important to note is that we do expect certain headwinds to carry over from 2018 and they will be impactful to the first half of 2019. Due to these carryover headwinds, we expect year-over-year EPS to be down in the first and second quarters and EPS growth in the third and fourth quarters. We expect full-year 2019 segment margins to be higher than the prior year for the full-year. Naturally, we are working to offset these headwinds with increased selling pricing, aggressive discretionary cost management, however we will not be able to fully offset these headwinds in the first half of 2019.

In particular, for the first half of ’19, we have carryover impact of first half 2018 raw material inflation. We experienced inflation for all of 2017. That continued well into 2018 before moderating in the latter part of 2018. On a year-over-year basis, we will experience inflation in the first half of ’19 until we anniversary the prior year commodity cost increases.

As discussed earlier by Michael, there has been a contraction in the global automotive OEM industry production rates, most prominently in China and Europe. We expect global auto production to be down, a low single-digit percentage in the first half of 2019 before growth returns in the second half of 2019. In addition, and more broadly, we also experienced low to negative growth in other parts of the Chinese economy in the latter part of the year. We expect that to continue as we enter into 2019.

Overall economic activity in Europe, in the first half of 2018, was solid and we hoped that would continue through the remainder of the year. Unfortunately, the European economic indicators turned down in the second half of 2018 and we currently do not expect any improvement in the near-term. Therefore, on a year-over-year basis, we expect overall economic demand to be lower in Europe in the first half of ’19 in comparison to 2018. We are not assuming any large, unfavorable economic impacts from Brexit in our current guidance. This is obviously a fluid situation.

Specific to PPG, we will anniversary the unfavorable customer assortment change in our US architectural business at mid-year. As a result of this, our first half sales will be down by a net of about $110 million, split roughly, equally between the first and second quarters. We are continuing to restructure the business, including the recent closure of four production facilities. We are targeting to be neutral on an EBIT dollar basis, in that business, beginning in the third quarter.

Additionally, we expect our corporate costs to increase based on the expectation that we will achieve our 2019 financial targets resulting in increased year-over-year management incentive compensation versus 2018 where incentive compensation was reduced. We are also anticipating higher interest costs reflective of our increase in leverage stemming from the cash we deployed in 2018 along with the increase in interest rates throughout 2018.

Finally, we expect our ongoing tax rate to be in the range of 23% to 25%, up from just below 22% for the full-year 2018. Last, although this is not included in our full-year guidance, is significant unfavorable currency translation based on current exchange rates. We currently anticipate a $400 million to $500 million unfavorable translation impact of sales in a relating $50 million to $70 million impact on earnings.

Given that the US dollar weakened in the first half of 2018 and strengthened in the second half of 2018, the currency translation impact is primarily a first half 2019 headwind to our sales and EPS.

We also provided EPS guidance today for the first quarter of 2019. This guidance is $1.18 to $1.23 and this does include the unfavorable impact from foreign currency translation. Embedded in this guidance is an expected foreign currency impact for the quarter of $0.07 to $0.08 per share to aid in your reconciliation back to our full-year guidance.

As in the past, we will provide the full impact of foreign currency translation to both our sales and EPS in earnings each quarter. As I mentioned, a summary of these financial assumptions is included in our presentation materials. This concludes our prepared remarks. Once again, we appreciate your interest in PPG.

Now, operator, would you please open the line for questions?

QUESTIONS AND ANSWERS

Operator
We will now begin the question and answer session. To ask a question, you may press star then one on your touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press star then two.

Our first question comes from Ghansham Panjabi of Robert W. Baird. Please go ahead.

Ghansham Panjabi
Hi, everyone. Good afternoon.

Michael McGarry
Hi Ghansham.

Ghansham Panjabi
I guess, first off, on Europe and the higher sales volumes in 4Q, the context of a macroeconomic slowdown in the region, were there any end markets that surprised you, the upside, or did it come in basically where you thought at the beginning of the quarter?

Michael McGarry
No, I think it was pretty consistent, Ghansham. We tried to signal in the past that we were still down on volumes because we'd been aggressive in raising price. We see our competitors now getting out there and raising price, and so some of that volume is flowing back to us. You saw we had a positive volume in architectural in Europe. We expect to have a positive volume in architectural in the first quarter as well. So I think things are fairly consistent in that manner.

Ghansham Panjabi
Okay. Then, I guess my next question is on the 3% to 5% sales growth FX. Can you break that out, price versus volumes? How should we layer in the $70 million in cost savings, first half versus second half? Also, the outlook for the back half of next year, the back half for 2019, specific to raw materials. Can you share that as well? Thanks so much.

Vince Morales
I'll start and Michael may chime in here as well. This is Vince. If you look at the sales guidance, again, we're expecting pricing somewhere in the same level as we received this year. We had 2% pricing in

2018. We're targeting something in a comparable range in order to recover our raw material inflation over the past couple of years. We do expect some volume growth, that's tempered by what I just mentioned earlier, which is the assortment change, so net volume growth will be probably in the 1% to 1.5% range depending on how certain end markets break. Then, we have some acquisition sales that are included in our financial metrics pages that we put in the presentation.

From a respective restructuring savings, that's going to be pro rata throughout the year so that's what I would assume.

Michael McGarry
Ghansham, the only thing I would add is right now we're expecting Whitford to close in Q1 and Hemmelrath to close in Q2.

Ghansham Panjabi
Okay. Thank you.

Operator
Our next question comes from John Roberts of UBS. Please go ahead.

John Roberts
Thank you. Is your portfolio review narrowly focused on the Trian proposal to split architectural from industrial? Are you likely to find some non-core and underperforming areas separate from the Trian proposal?

Michael McGarry
Well, first of all, John, what I would say is that we always look at our portfolio. This has been, as you know, an ongoing thing since 1998. We're always looking for ways that we can improve our mix of businesses. We just wanted to be transparent that this work was underway. I would tell you that there's always certain countries we look at and we always say is this a good use of shareholder money? We're not signaling one way or the other, but the intent is to take a complete look at everything that we have within PPG and make sure that we're aligned to the most shareholder value creation.

John Roberts
Then, secondly, in auto OEM in China, do you have e-coat tanks that are idled? I think the inventory in those tanks is yours, I think, so does the customer close down the tank, you take back your paint and are you going to reuse that somewhere else, or how does that work when volumes drop this much?

Michael McGarry
We don't have any idled tanks. There is maybe one guy that's been shutdown for an extended period of time, but they own that paint. One plant out of hundreds in China is not even a rounding error, so these guys are just running at a slower rate. They've taken a little bit more down time. So far, in Q1, we've seen continuation of about a -15% build rate across the industry, both ourselves as well as the entire industry. We expect that to get better after the Chinese New Year.

There have been some indications that there is going to be some incentives. We don't know exactly what they are yet. Obviously, they lowered the reserve rate. That frees up some capital that the banks can use but right now we do anticipate a better back half of Q1 than the first, let's call it, 45 days that we have strong visibility into.

John Roberts
Okay. Thank you.

Operator
Our next question comes from David Begleiter of Deutsche Bank. Please go ahead.

David Begleiter
Thank you. Michael, just on pricing versus raw, is Q3 now where we will see the first positive margin comparison year-over-year rather than maybe Q2?

Michael McGarry
Well, I guess it depends how you define it, Dave. In Q4 2018, we actually had price exceeding raws, but remember, we have to catch up all the raw material inflation from 2018, so the segment margin gap will grow bigger in Q1 2019 because inflation is still going up but moderating at a lower level. Of course, Q2, we were forecasting even less inflation but still inflation and we are going to continue to get price.

So I would say that our goal is to capture all the raw material inflations since it began late in the fourth quarter of 2016 and obviously, we're trying to create shareholder value for everybody by returning to our pre-inflationary margins.

David Begleiter
Got it. Just on capital deployment, what's your target for buyback acquisitions in 2019?

Vince Morales
David, we didn't give a target. If you look historically, we've given a cash deployment target over the past couple of years. Part of the reason for us giving a target the past couple of years is we did lever down at the end of 2016. We tried to do an acquisition that didn't work so we wanted to give confidence that we were going to deploy the excess cash from our balance sheet.

As we sit here today, we have a solid investment grade balance sheet. We think that's at a premium in today's economic climate. We're going to sit tight and analyze what's going on economically. We're not going to give a cash deployment target in the near-term. Our preference remains acquisitions. We do have a very active pipeline I'm sure we'll talk through on the call today. That's evidenced by the three acquisitions we announced here in the last 90 days or so and we still have acquisitions in the pipeline.

David Begleiter
Thank you.

Operator
Our next question comes from Bob Koort of Goldman Sachs. Please go ahead.

Bob Koort
Thanks very much. Michael, can you talk about where we stand on the penetration of BPA free or non-BPA in the packaging markets? How much is there still in front of you to convert or are we going to hit a lull here?

Michael McGarry
I think, Bob, in my opening comments I tried to give some flavor to that. The amount of new conversions are slowing. We've converted, let's call it 70% to 80% of the food guys and then we've probably converted 50% of the beverage guys.

So there's still more out there but the folks that are left are being, I would say, they're being cautious in the route that they're taking. They're also challenging everybody on their other alternatives besides just

the products that we're offering and so we're going to say is probably the low single-digits is where we would be as opposed to the mid- to high-single-digits where we've been previously.

Bob Koort
Then, if I could follow up in both marine and aerospace, you've had some really strong growth. Those tend to be really long lead-time businesses. How far in the future do you see that, I mean you mentioned you'd see some maybe deceleration in aero, but how long is the confidence band in that growth rate sustaining?

Michael McGarry
Well I would say in aerospace it's a very high confidence level. Probably the one metric we don't talk a lot about is only 1% of the people in China have ever flown on a plane and the amount of people, and the amount of planes that are going to go into China, the number of new airports they're in the process of building is significant. The fuel economy of the planes are significantly better than what's flying and so we anticipate this continuing to be strong. Of course the military's getting stronger. So, I think those are all positive signs. So with my current time horizon, I see this being a good market for quite an extended period of time.

PMC, we tried to convey previously that we thought 2018 was a bottom of the cycle. We do paint 18 to 24 months after we start to get orders, we took more orders through I think it was July or August than we took all of '17 and we're off to a pretty good start. So, I think we're in the beginning of a slow recovery in the ship building business. The shipyards in Korea are still hurting financially. So they're still getting support locally but the Chinese shipyards are doing better. So, I anticipate that this should be the beginning of a multi-year recovery.

Bob Koort
Great, thanks for the help.

Michael McGarry
You bet.

Operator
Our next question comes from Alex Yu of RBC Capital Markets. Please go ahead.

Alex Yi
Hi, this is Alex Yi on for Arun. It seems like based on your Q1 guidance, it appears to imply sequential deteriorations. I was just wondering in the second half based on your 2019 full-year guidance it goes back up sharply. Could you maybe just give some insight onto what's driving that?

Vince Morales
Yes, Alex, this is Vince. As I said I think in my opening remarks we do have a variety of headwinds in the first half and in Q1. We anniversary mid-year. Those include the assortment change. We do expect automotive globally to get better in the back half of the year than the first half of the year. We have the currency translation impacts and several other headwinds in the first half that we have talked about throughout all of '18 and again most of those anniversary as we approach the middle of the year. Plus, we're continuing to get pricing in place and we have growing benefit from restructuring. So those will be the big causation factors that give us confidence that the back half will be better than the first half.

Alex Yi
Okay, thank you and just a follow-up, would be it seems like on the strategic review, it seems like it's going to address the split between architectural industrial coatings. Maybe is there any other further announcement that we could see on any divestitures beyond that? Any other leverage you guys expect?

Vince Morales
No, Michael addressed it just a few questions ago again. We're evaluating what we put out in the press release. We've targeted a commitment to complete that evaluation by the second quarter. We always look at our portfolio business by business, product by product, region by region but that evaluation strategically is the one we announced in the press release today.

Alex Yi
Okay, thank you.

Operator
Our next question comes from Duffy Fischer of Barclays. Please go ahead.

Duffy Fischer
Yes, good afternoon, fellas. Question just around your goal for your 10% EPS annually. If you looked at a typical year between organic and inorganic, what type of topline number do you get or do you need to consistently drive that 10% EPS growth, do you think?

Michael McGarry
Duffy, I would tell you there's multiple factors that will drive that 10% EPS growth. First if you have the volume growth and Vince talked about that earlier, probably 1% to 2% range, you have price. Obviously that's going to be a positive. You have raw materials that are moderating right now. You have the share count is down. You have costs are going to be lower and then you have the positive impact from acquisitions. And each one of those things are going to help us build to the 10% number that's in there.

Vince Morales
If you look over a longer period of time for the company, and again this is averaging, so it doesn't match in any particular year, we're typically two-thirds organic, one-third inorganic in terms of our ability to grow. We've done acquisitions, as Michael mentioned, over 20 in the last couple of years. We've done over 50 in the last decade plus. So that'll be the inorganic piece. Organically, whether it's price, whether it's volume growth, depending on what's going on with raw materials, that'd be the two-thirds.

Duffy Fischer
Okay, and then with the deals or acquisitions that have been announced so far, assuming they feather in kind of on the timeline you project, how much is that already adding to the top line in '19?

Vince Morales
Again, if you look at our presentation materials, Duffy, we put in there that the announced acquisitions would add somewhere between $225 million and $275 million to the calendar year. That's assuming they close when we expect. That's obviously our expectation. They have to go through the required regulatory process which we don't control. But that would give you the top line marker.

Duffy Fischer
Okay, great. Thank you, guys.

Operator
Our next question come from Jeffrey Zekauskas of J.P. Morgan. Please go ahead.

Jeffrey Zekauskas
Thanks very much. You're contemplating the split of your company into an industrial and a consumer side. How will you conduct that review? Will you hire an outside consultant? Will you work with various bankers? Can you talk about the mechanism of your decision making process?

Michael McGarry
Yes, so Jeff, we're using both inside and outside resources. And it's important for us to look also historically. So, if you go back and look at the synergies that we've created as we've done these acquisitions plus the sales growth that we've created, the best practices, so we're taking a look at all that. We'll also be looking externally at obviously other examples outside of PPG and we'll see how those performed. And obviously we have a super experienced board of directors. They have their own experiences that they'll be feathering questions to us. So I think it'll be a pretty exhaustive review.

Jeffrey Zekauskas
Okay, one of the categories that wasn't mentioned in your financial goals is there wasn't a comment on operating cash flow as a percent of sales, in that over the past five years I think PPG's operating cash flow as a percentage of sales is a little bit lower than some of your competitors. Is that an area that you think needs addressing or isn't it?

Vince Morales
Yes, Jeff, this is Vince. We definitely have been targeting improvement in our working capital metrics. Unfortunately in 2018, in the back part of the year the metrics worsened a little bit. We attributed a little bit of that to we ended on a 3 or 4 day weekend so our receivables are higher than we had hoped. We did continue our normal payment process. So we did make payments through our normal schedule. So our payables were lower on a comparative basis. But we definitely have stretched targets in 2019 for working capital. And that's definitely a focal point for both Michael and I and the senior team here is to get working capital back moving in the right direction.

Jeffrey Zekauskas
Okay, great thank you so much.

Operator
Our next question comes from PJ Juvekar of Citi. Please go ahead.

PJ Juvekar
Yes, Michael, good afternoon. I have a question about your new store opening strategy. You mentioned that you're closing some stores. You're opening some new stores in some areas. So how many stores do you plan to open in 2019 on a net basis? And do you want to accelerate that growth in '19 and '20?

Michael McGarry
Yes so I think as we've talked about in the past PJ, we do run a global architectural business. So we have probably in the US somewhere in that 10 to 25 store range. In Mexico, it'll be over 200. In Europe, it'll be in that 10 to 15 range. So, in Australia we don't have a firm number but it's at least 3 to 5. So I think those are the kind of numbers you can be expecting.

PJ Juvekar
Okay thank you. Now I want to go back to this split that you talked about, splitting PPG into architecture and industrial segments. This is the first time that we are hearing about it from you. So what are the dissynergies of splitting? And do you expect the pieces to create different multiples? Substantially different multiples if they're split.

Vince Morales
PJ this is Vince. We're not going to speculate on trading multiples. That's the job of the equity markets. We're going to analyze and evaluate what we said again in the press release. We're going to determine what the synergies or dis-synergies are of that. We'll get all our commitment to complete that. We're not going to do that evaluation over the phone today.

PJ Juvekar
Okay, thank you very much.

Vince Morales
Thanks, PJ.

Operator
Our next question comes from Kevin Hocevar of Northcoast Research. Please go ahead.

Kevin Hocevar
Good afternoon, everybody. You mentioned raw material inflation of low single-digits in the first quarter, and then mitigating a little bit in the second quarter, and then maybe turning favorable in the back half. If we think about it for the full-year, what's the expectation for raw materials for the full-year as best as you can tell it now where current rates are at?

Vince Morales
Yes, just one correction, Kevin, we didn't say turning favorable in the second half. Our current expectation right now is low single digit inflation for the year, again more of that in the beginning of the year. Obviously this is a dynamic situation with the price of oil, etc. But again our expectation is very low single-digit inflation averaged for the full-year but front-loaded.

Kevin Hocevar
Okay, got you. And then I know freight and logistics has been a headwind this year. I think last quarter you got into mid-teens type inflation this quarter. So what was the overall inflation from freight this year? And what's your expectations for that in 2019?

John Bruno
Hi, Kevin, this is John. We averaged well over 10%. There's a little bit of benefit in Q4. Some crude oil prices started impacting certain elements of that area. But we're still having lack of transportation availability and other issues that are keeping the prices higher. So we still expect inflation in that area as we go into 2019.

Kevin Hocevar
Okay, got you. Thank you very much.

Operator
Our next question comes from Don Carson of Susquehanna Financial Group. Please go ahead.

Emily Wagner
Good morning, this is Emily Wagner on for Don. Just staying with the raw material inflation, in terms of how you expect gross margin recovery to roll out in 2019. I know it's back-half loaded but could we see 100 to 200 basis points and what's kind of the magnitude of contributions there from price and cost savings?

Michael McGarry
Well, again we, we expect the margins to be up in 2019 for the full-year. We're not going to provide it by quarter. There's too many moving pieces and parts in each quarter. But again, it'll be back-half loaded.

Emily Wagner
Okay. And then within auto OEM, if there were to be a tax incentive for the Chinese, how long would that take to increase auto production? And how long would that take to benefit the coatings producers?

Michael McGarry
Well, we deliver in real time. So it's a just-in-time delivery. In the Chinese market, they're probably up about five to seven days of inventory. But if they were to put incentives out there, what we saw in 2016 when they did this, we saw pretty immediate improvement in operating rates and pretty immediate improvement in sales rates. So, I would tell you we'll just have to wait and see what the actual incentives are and when they're effective. But historically that has translated very quickly into improvement in sales.

Vince Morales
If I could, Emily, I just want to emphasize what Michael said. There isn't a significant inventory overhang in China. Inventory's up a few days, but inventory's relatively well in check, so it wouldn't take a long time for this to have a meaningful impact on production.

Emily Wagner
Thank you.

Operator
Our next question comes from Christopher Parkinson of Credit Suisse. Please go ahead.

Harris Fein
Hi, this is Harris Fein on for Chris. Thank you for taking my question. I was just wondering what expectations you have that are embedded into your guidance on US housing? And is there anything that you're seeing, either from the data that's out there, or just qualitatively from being on the ground, that gives you confidence that resi repaint activity can keep growing, even in an environment where we have lower housing turnover? Thank you.

Michael McGarry
Yes, so we have 1.3 million builds, and for the new housing starts we have about the same 5 million and change for overall units turning over. So we don't have a big difference. Resi paint, for us, I would say we're undersized in that market. We're much more a commercial and maintenance type painter in that area. So that probably will not have a significant impact on us. We're still anticipating that architectural will have a good year. There's a significant amount of backlog with our painters, and they feel very comfortable that their order book looks good.

Harris Fein
And just kind of keeping with this topic, due to the weather that we had during October and November, did you see a lot of commercial projects get pushed out, and do you see any sort of recouping any lost business, as we enter into the paint season in the spring and summer?

Michael McGarry
Well, we don't allow our sales team to use weather as an excuse, so we're not going to use it here. Our customers are trying to paint every single day, and it's up to us to try to make sure they're equipped to

be productive. All I will tell you is that we're anticipating to be back to that mid-single digit kind of numbers in Q1. It's way too early to tell because January's a month that's seasonally exceptionally slow, and March is, by far, the most important number in that.

Harris Fein
Got it, thank you.

Operator
Our next question comes from Frank Mitsch of Fermium Research. Please go ahead.

Frank Mitsch
Hi, good afternoon, gentlemen. Maybe if I ask that question a little bit differently. If I look at the fourth quarter by month, October, November, December, can you talk about the pace of business that you saw, Michael, in each of those months, and how is January starting out?

Michael McGarry
I would tell you that there wasn't that much of a meaningful difference. For us, I would say it'd be more guess work than splitting hairs on trying to figure out that impact, because you have different days, you have different regions, you have different impact of weather. So, I would just tell you that we're pretty confident going into next year that architectural buying in our stores is going to continue. The do-it-for-me trend is a positive, and that trend is going to continue.

Frank Mitsch
Got you, and I guess a broader question. Europe was a bit of a surprise, positive surprise, in the quarter, other than, I guess, auto OEM, but you mentioned that indicators had turned down a while ago, and so you have some concerns there. In terms of economic activity, PPG has always been one of the best ones in terms of forecasting what's going on economically. How would you guys gauge the percent chance that we enter into a recession here?

Michael McGarry
I'm not forecasting that, Frank, right now. We are forecasting a slowdown in Europe, but not a recession. The big unknown, of course, is Brexit. That could be a significant factor. But we do see significant differences by country, and that's the bigger thing. Even Germany slowed down in the fourth quarter, and that's not necessarily a good sign, but we'll wait and see how that continues.

Frank Mitsch
And if I look at Asia, do you have an expectation that China comes back post-Chinese New Year, or more the same is how you guys are looking at that region?

Michael McGarry
Well, if you tell me what would happen with the tariffs, then I would have an answer for you. We see a lot of positives in certain of our businesses; Marine is a positive there, refinish is a positive there, aerospace is a positive there. So we see a number of good indicators, but clearly, consumer confidence is down, appliance is down, coil is down, OEM, obviously, is down. So I think it'll come back. I mean, it is too big of a market not to come back. And we know that they have plenty money over there, and so, it's just a matter of getting that consumer confidence back. So we have a very positive long-term outlook on China.

Frank Mitsch
Thank you very much.

Operator
Our next question comes from Vincent Andrews of Morgan Stanley. Please go ahead.

Vincent Andrews
Thanks. Good afternoon, everyone, and thank you very much for the detailed full-year guidance. It's very helpful. Question for you on, if we have raw materials have peaked and has come down, and you have negative auto builds in a decelerating macro economy, what gives you the confidence that you're still going to be able to achieve the pricing that you need to get?

Michael McGarry
Well, first of all, the pricing is catchup, right, so we don't price just in the real-time environment of today. We have to look at how it's been the last nine quarters, now it's ten quarters of inflation, so our customers understand that. They see it in their own numbers. They see it in their own freight and logistics numbers. So the question isn't a matter of if, it's a matter of how much.

Vincent Andrews
Okay. And then if I can just ask you on the incentives, why did the board choose EPS as the metric, as opposed to net income or EBITDA, or something that isn't influenced by share count?

Michael McGarry
We've always used EPS as one of our metrics, has been for quite some period of time, and so we didn't make a change. What we wanted to do is reinforce that the executive incentives will be paid out on the upper end of the range at 10%.

Vincent Andrews
Okay, thank you very much.

Operator
Our next question comes from Kevin McCarthy of Vertical Research Partners. Please go ahead.

Kevin McCarthy
Good afternoon. Michael, I was wondering if you'd flesh out the auto OEM pricing in perhaps a bit more detail. You obviously had the press release back in October. Are you seeing better realizations in that market on a sequential basis, and has pricing turned positive at this juncture?

Michael McGarry
Yes, Kevin, I think I tried to make that point clear on my opening remarks. We had positive price in OEM in all regions, and that was a first. So now we have all eight business segments reporting positive price. We even had positive price in China, which was—if you remember, our two biggest challenges were, A, automotive, and B, China, so we had both positive.

So, we're going to get price in automotive. We're going to get more price in Q1, and then we'll get more price in Q2. So, these guys are large, sophisticated buyers, and it's not easy, but they do understand the challenges that we have. And, obviously, they very much want to have access to our technology, and in exchange for that, they're willing to pay a fair price.

Kevin McCarthy
That's helpful. And then a second question, if I may, on raw materials. The cost of propylene has come down rather sharply since November, at least in the US market, down $0.10 in November, and $0.08 on top of that in December. And so, my question is, is that sort of volatility likely or not likely to precipitate a shift in resin systems, away from acrylics, for example, into vinyls or styrenics?

Michael McGarry
Well, we're always looking and optimizing our resin portfolio, and we don't typically change them on a quarterly-basis basis, what's happening with propylene and ethylene. I think from a long-term perspective, we're still bullish that the PDH expansions will drive more consistent pricing in propylene, and that there'll be more capacity out there. They struggle getting these plants to consistently run, but there are more of them coming on. So, I think right now you probably should not assume that we're going to be shifting systems, resin systems.

Kevin McCarthy
Thank you very much.

Operator
Our next question comes from Steve Byrne of Bank of America Merrill Lynch. Please go ahead.

Ian
Hi, thanks, this is Ian on for Steve. The strategic review, when did that kind of kick off, and what are you hoping to learn that you don't know already?

Michael McGarry
Well, like I said earlier, we do strategic reviews of all our businesses on a continuous basis, so there was really no kick off, if you will. What we wanted to do was let people know that we take all the feedback we get from investors seriously and that we're going to evaluate. We don't always have the best ideas internally, that there could be external ideas that we need to consider, but we're not going to predict what the outcome is going to be. I think we want to take a very serious look at all our businesses, and all our regions, and then decide what's the best path forward.

Ian
Okay, thank you. And I would echo the comments earlier about the 2019 guidance as being very helpful. I'm just curious about, I think, historically, PPG didn't offer more details in full-year 2019 guidance, and what drove that change?

Michael McGarry
Yes, so, Ian, we have a very choppy environment right now, right? We have currency moving all over the place; you have China, you have automotive, you have tariffs, you have raw materials, so I think those are all things that we wanted to be a little bit more transparent on. And we knew that in the second half of the year we were going to be different, and we wanted to provide that kind of clarity so that you could put that into your models.

Ian
Thank you very much.

Operator
Our next question is from James Sheehan of SunTrust Robinson Humphrey. Please go ahead.

James Sheehan
Thanks. You guys targeted a $2.4 billion of capital deployment in 2018, and it looks like you fell short of that by about $300 million. Is there another deal in the pipeline that will make up that shortfall relatively quickly, or can you just provide more color on capital deployment plans?

John Bruno
Yes, Jim, this is John. We met our target. What we talked about in fourth quarter was that we were going to include any deals we announced in that $2.4 billion, so including Whitford and Hemmelrath, we're a little bit over that target.

James Sheehan
Got it. And regarding synergies that you have between industrial and architectural coatings, would you say that those all have been fully captured over the last two to three years, or has something held you back?

Michael McGarry
Oh, no. We continue to capture more synergies. I mean, I'll take Comex as a perfect example, right? We closed on Comex four years ago, and protective sales in Mexico were up significantly. We built a new architectural business in Central America. We've grown our Industrial. We've grown our architectural sales into the automotive plants down in Mexico. Our Mexican business is up significantly since the Comex acquisition, and that's just one illustration of the synergies between the industrial and architectural businesses.

James Sheehan
Could you give us some color on the synergies you expect from the SEM acquisition?

Michael McGarry
Sure. There'll be two major ones, of course raw materials is one, that's an easy one. The second one would be sales synergies. So, SEM, of course, has a small sales force. They're pretty much a US, and a little bit of a Canadian business, very, very little international business to speak of. Also, there'll be some reverse synergies. They have the capability of packaging aerosols. So that'll be something that we'll be looking at, whether that makes sense for us to move that in-house, versus us currently outsourcing it. So this should be a good acquisition for us. So they're a very profitable company, and they're excited to be part of the PPG team.

James Sheehan
Thank you.

Operator
Our next question comes from Laurence Alexander of Jefferies. Please go ahead.

Dan Rizzo
Hi, this is Dan Rizzo on for Laurence. Is the expectation that buybacks should accelerate if end-market trends were to diminish, that is, should we treat the EPS range more as a commitment or as a benchmark?

Vince Morales
No, we haven't talked about cash deployment, and again, our focus right now is to maintain our balance sheet today in the economic times we're in. We do have an active pipeline, as I mentioned earlier, that would be a priority for us. The EPS range we put out there is our best guess of what we know today. We put a stake in the ground with respect to our incentive comp metrics on the top end of that range. So, I'd certainly say that's a commitment from the management team. But again, it's based on our best guess of the economy today, and there's a bunch of moving pieces as we talked throughout the call.

Dan Rizzo
Alright, thanks. And then, with order patterns, have you seen volatility increase over the past few months? I mean, I know things are, obviously, changing a lot, but I was wondering if volatility from month to month has gone up in 2018?

Vince Morales
Yes. I'd say the only place where we've seen, what I would call dramatic shifts in orders, is really in the automotive market, particularly in China, but a little bit in Europe, we've seen extended downtime. Again, that's not a PPG specific issue, that's an industry issue. Everywhere else things get a little choppy in the winter. Things get a little choppy around year end as there's inventory management by our customers. So there's nothing uncommon, other than in automotive.

Dan Rizzo
Thank you very much.

Operator
Our next question comes from John McNulty of BMO Capital Markets. Please go ahead.

Colton Bina
Hi, this is Colton Bina on for John. Thanks for taking my question. On auto refinish, with it being flat for the quarter, what were some of the positive impacts you saw there offsetting the weakness in the US from destocking?

Michael McGarry
Well, refinish is a global market. I mean, Europe was slightly positive; China was slightly positive; India was positive; Mexico was flat. I would say, overall, the quarter came in about where we expected.

Colton Bina
Okay, that's very helpful, thanks.

Michael McGarry
Thank you.

Operator
Our next question comes from Mike Harrison of Seaport Global Securities. Please go ahead.

Mike Harrison
Hi, good afternoon. I was wondering, it sounds, from your commentary, like you expect to continue to be pretty aggressive on the pricing front, but just wondering, as we're seeing some softening in demand in certain markets, we're just wondering if you're maybe rethinking your approach on pricing at all? And maybe can you talk a little bit about how aggressive you think you'll be able to be on pricing when you look at, maybe three buckets, architectural, industrial, and then auto OEM getting into 2019?

Michael McGarry
So we are not backing off on our price. We still have significant margin recovery that we need to capture because of 2017, and the start of it in the fourth quarter 2016. So the sales teams are focused on that. Automotive is the furthest behind, so that will continue to have significant amount of pressure. We've had good increases in our industrial businesses, and so we would expect that to continue. And then from an architectural standpoint, we're pleased to see that all the players in the marketplace are finally serious

about getting price globally, and that is helping getting more traction. So I don't anticipate anybody letting their foot off the accelerator at this point, given the fact that we still have significant raw material inflation capture.

Mike Harrison
Alright. And then, the Europe architectural business, it sounded, to me, like what you were saying is that you had been losing volume because you've been very aggressive on price. Now you've seen some competitors pushing price, and that volume is starting to come back. Is that the main variable that explains what's been happening to improve your business there, or what else may be at play in Europe?

Michael McGarry
That's not the only variable, right? I mean, we have certain key markets that are performing very well. Our Romanian business had a record year, our Czech Slovak businesses were good, the Benelux was solid. Surprisingly, retail, we were a little surprised retail in France was better than we expected. So we'll wait and see if that's a short-term anomaly or what, but that was a positive. So our big challenge still is trade France, that's still the biggest business we'd like to see click back into a positive number. We are gaining share in the UK and Ireland, but it's really choppy with Brexit right now, so we're not going to be drawing any conclusions at this point in time.

Mike Harrison
Alright, thanks very much.

Operator
Our next question comes from Dmitry Silverstein of Buckingham Research. Please go ahead.

Wahid Amin
Hi, good afternoon, this is Wahid Amin on for Dmitry. Just a quick question on your outlook for US and Canada same-store sales. Can you break that up a little bit? And on that note, do you see a much slower pace in the DIY market with the whole shift in DIFM? And do you hold a bullish outlook in that towards the latter half of 2019?

Michael McGarry
Yes, so the trend line of do-it-for-me is going to continue over DIY, so that trend line is not going to change. The same-store sales is going to be a combination of volume and price, it's going to be both. So I would anticipate that that will continue to be a good story for PPG in 2019.

Wahid Amin
All right, thanks, and if I can ask one more. You've talked about 225 to 275 in added acquisition towards sales, would you mind breaking that a little bit? Is that more towards the latter half of 2019? Do you see that more materializing toward the first or second quarter? Just any color on that.

Vincent Morales
Yeah, this is Vince. That’s the target is for the full-year, based on when we expect the pending acquisitions to close. Again, we expect Whitford, as Michael mentioned, to close sometime between middle to late first quarter. We expect Hemmelrath to close in the second quarter. We don't have as much visibility on timing. Those two acquisitions, plus the Whitford acquisition which we closed in the fourth quarter—I'm sorry, SEM, I apologize—that we closed in the fourth quarter. So that'll grow throughout the year, based on when those acquisitions close.

Wahid Amin
Okay. Thank you very much.

Operator
Our next question comes from Daniel Chong of Redburn. Please go ahead.

Tony Jones
Oh, thanks everybody, it's Tony Jones from Redburn. I just had two quick ones left. So one was on opex, R&D, and SG&A cost, they were down pretty significantly in Q4. Is that sustainable in the next few quarters, or likely to trend back up?

Vince Morales
No, if you look at SG&A costs, they were down on an absolute basis, but they were comparable in the prior quarters on a percentage of sales basis. Since we buy, make, sell local, we do have a lot of currency translation effects that run through all the P&L lines. But again, on a percentage of sales basis, we were pretty consistent throughout the year. We were down about 100 basis points in most quarters year-over-year on SG&A. Again, the anomalies by quarter are more driven by currency translation.

Tony Jones
Thank you, and just one final one. Just coming back to the strategic review, will the study also examine the potential for a second step, so maybe synergies, or other value creation from a merger with a competitor post-breakup? Thank you.

Michael McGarry
No, again, our focus is what we put out on the press release. We're going to study the portfolio we have today, we're not going to another derivative.

Tony Jones
Great. Thank you.

CONCLUSION

Operator
This concludes our question and answer session. I would like to turn the conference back over to John Bruno for any closing remarks.

John Bruno
Thank you, Andrea, and thanks, everybody, for your time and interest in PPG. If you have any further questions, please contact our Investor Relations department. This concludes our fourth quarter and full-year 2018 earnings call.

Operator
The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.