PPG Industries, Inc.

Second Quarter 2019 Earnings Conference Call

Thursday, July 18, 2019, 2 PM Eastern

CORPORATE PARTICIPANTS

John Bruno - *Director of Investor Relations*

Michael McGarry - *Chairman & Chief Executive Officer*

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

PRESENTATION

Operator
Good afternoon, everyone. Welcome to the PPG Industries Second Quarter 2019 Earnings Conference Call. My name is Jamie, and I will be your conference specialist today. All participants will be in listen-only mode. Should you need assistance, please signal a conference specialist by pressing the "*" key followed by "0."

After today's presentation, there will be an opportunity to ask questions. To ask a questions, you may "*" and then "1.". To withdraw your questions, you may press "*" and "2." Please also note, today's event is being recorded.

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

John Bruno
Thank you, Jamie, 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 second quarter 2019 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, July 18, 2019.

I will remind everyone that we have posted detailed commentary and accompanying presentation slides on the investor center of our website, 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, we will move to a Q&A session.

Both the prepared commentary and discussion during the 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 risk, which may cause actual results to differ. The company is under no obligation to provide subsequent updates of these forward-looking statements.

This presentation also contains certain non-GAAP financial measures. The company has provided in the appendix of the presentation materials, which are available on the 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 SEC.

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

Michael McGarry
Thank you, John, and good afternoon, everyone. I want to thank you for your continued interest in PPG. Today, we reported second quarter 2019 financial results. For the quarter, our net sales were slightly more than $4 billion, and our adjusted earnings per diluted share from continuing operations were $1.85.

Consistent with our improvement targets, we delivered higher year-over-year operating margins for the second consecutive quarter, as both gross profit and segment margins improved versus the prior year.

Our margins benefited from continuing selling price realization and strong cost management across all our businesses and regions. We are still in the early phase of margin recovery, and while we are building some momentum, we still have more work to do. Our overall objective is to return to the aggregated segment margins that we have maintained prior to this recent inflationary cycle.

To provide some additional color on our second quarter results, our net sales in constant currency were higher than the prior year by about 1 percent. Sales volumes were down nearly 4 percent, impacted by weaker global industrial production that significantly affect the global automotive production in many of our general industrial end-use markets and was evident in all major regions.

Also, about one-third of the total sales volume decline relates to the prior year customer assortment changes in our U.S. architectural coatings DIY business. We have now reached the one-year anniversary of these changes, and it will no longer be a comparison deviation. We remain committed and are on track to fully offset the earnings impact of this assortment change in the third quarter.

Selling prices were 2.3 percent higher, marking the ninth consecutive quarter of higher selling prices. We will continue to work with our customers to ensure we are receiving fair value for our products and services and expect selling prices to increase at a similar rate in the third quarter despite comping against improving gains in the prior year third quarter.

Finally, our net sales were affected by significant unfavorable currency translation of more than 3 percent for about $130 million. Going forward, we expect unfavorable currency translation to continue, albeit at more modest levels, with our current estimate for the third quarter of an unfavorable sales impact of between $30 million and $50 million.

Moving to some business trends in the second quarter, in our performance coatings reporting segment, aerospace coatings continue to deliver very strong volume growth, outpacing industry performance in most major regions.

In the automotive refinish, sales volumes were lower year-over-year, reflecting lower collision claims in the U.S., which were down 2 percent for the industry in the second quarter and in comparison to strong sales volumes in the prior quarter. We expect refinish volume comparisons to improve on a year-over-year basis in the third quarter, as our prior year included an unfavorable impact of PPG-specific customer inventory destocking.

Year-over-year organic sales were higher in our architectural coatings EMEA business, driven by higher selling prices. Aggregate sales volumes were slightly lower, as wetter than normal weather patterns impacted overall regional demand during the quarter.

In Mexico, our PPG COMEX business increased organic sales, aided by higher selling prices. Sales volumes were tepid, as consumer demand reflected increased uncertainty around Mexico's economy and economic policies. The PPG Comex business continues to perform very well and continues its growth by adding nearly 70 concessionary locations in the first half of 2019.

Sales volumes in architectural coatings Americas in Asia Pacific decreased due to lower net DIY sales of about $60 million, stemming from the prior year customer assortment changes. Same-store, company-owned sales growth in the U.S. and Canada was relatively flat, including impacts from fewer shipping days year-over-year and wet weather that impacted most of this region during the quarter.

Led by strong growth in the Asia region, our protective marine coatings business continued to deliver above industry organic sales volume--excuse me, organic growth, a high single-digit percentage during the quarter. We are very excited that this business was recently awarded a five-year contract with the U.S. Navy to supply coatings and technical services to the Military Sealift Command, which includes about 125 ships.

In our industrial coatings reporting segment, sales volumes were adversely impacted by soft industrial demand in most regions of the world. Most acute were automotive OEM industry build break which declined by nearly 20 percent in China and remain soft in Europe.

In aggregate, PPG's automotive sales volumes were lower by high single-digit percentage, consistent with reduction of global builds. One statistic we track is automotive OEM dealer inventories, which decreased as the quarter proceeded, which may help demand in the second half of the year. As a partial offset, our automotive OEM business realized higher selling prices in each major region for the second consecutive quarter, with similar expectations for Q3.

Softer global industrial production activity impacted many of our general industrial coating business sub-segments, most notably coil, general finishes, appliances, and transportation and markets. Also, our packaging coating sales volumes decreased modestly in comparison to above-market growth in the prior year, driven by customer adoption to our INNOVEL interior can coatings products. Our packaging business has achieved above-market growth in the past five years of about 20 percent compounded. We expect this business to return to growth by the end of the year.

From an earnings perspective, as I mentioned earlier, our second quarter adjusted earnings per diluted share was $1.85. Our earnings were negatively impacted by about $20 million of unfavorable foreign currency translation. On a constant currency basis, our adjusted EPS is modestly higher than the prior year.

Our effective tax rate was about 24 percent in the second quarter, which is higher than the 22 percent rate in the second quarter of 2018. The increase mostly relates to recognizing non-recurring favorable discrete items in the second quarter of 2018. We are still anticipating a tax rate between 23 percent and 25 percent for the full-year 2019.

Our EPS results were supported by the increase in our selling prices, improved manufacturing performance, aggressive cost management, and excellent progress on our cost-savings programs, which delivered about $20 million in cost savings during the quarter, in line with our targets.

As we look ahead, we expect global economic activity to remain sluggish in the third quarter. We expect global automotive production and general industrial demand to remain unfavorable year-over-year and roughly comparable to what we experienced in the second quarter. Positive developments around regional and country trade disputes could provide a spark to industrial demand as inventory levels in many of our end-use markets remain low.

Specific to our businesses, we believe that the potential for lower U.S. interest rates could aid growth in the U.S. housing market and also favorably impact automotive OEM in U.S. architectural sales.

In Latin America, we anticipate economic activity to be similar to that experience in the second quarter, and we will continue to add new PPG Comex concessionary locations and expand our customer reach. Also, we have a new manufacturing facility under construction in Panama to localize production and support our sales growth in Central America.

In Asia, demand rates are expected to remain consistent in comparison to the second quarter. As we move back into the back half of 2019, sales comparisons to last year will become easier, given the weakness in Asian demand that began to occur late last year. This will result in easier comparisons and relative performance improvement year-over-year.

We intend to remain laser focused on our cost structure. We remain confident that demand growth will eventually return in China. Economic growth in Europe is expected to remain tepid. In our automotive OEM business, year-over-year growth will be difficult in the third quarter as last year benefited from inflated sales from purchases brought forward ahead of the WLTP implementation.

Later in the year, the year-over-year comparison should improve into positive territory. We expect our architectural business to continue to grow, driven by higher selling prices and strong cost management. Brexit uncertainty is not yet impacting our business trends. However, we expect to closely monitor the situation and prepare contingency plans to best address the potential impacts to overall demand and relating inventory needs. With ongoing uncertainty over global industrial production, we have intensified our cost management and costs, including working with our supplier base to ensure that our input costs are reflective of current industry demand conditions.

In addition, our focus on our cost structure remains elevated as evidenced by our recently announced approval of a new cost savings program, which is a result of a comprehensive internal operational assessment to identify further opportunities to improve our profitability. We have begun implementation of this program which--we expect to have a full run rate savings of $125 million upon completion of the program.

In addition, we're in the final stages of the execution of the cost-savings programs announced in 2016 and 2018. We expect the total benefit from all of these programs to be about $20 million of additional incremental savings to be realized in the third quarter.

Earlier today, we provided EPS guidance specific to the third quarter of 2019. This guidance is $1.57 to $1.67 and includes an unfavorable impact from foreign currency translation of $0.01 to $0.02 per share. We are also reaffirming our full year 2019 adjusted earnings per share growth of 7 to 10 percent, excluding currency translation impacts.

In the second quarter, we generated operating cash flow of about $550 million, nearly $200 more than last year, and through the first six months of the year have generated about $350 million more operating cash flow in the same period last year. Our focus on cash flow generation will continue, and our goal remains to reduce working capital as a percent of sales compared to 2018.

We completed the Hemmelrath acquisition early in the second quarter. I'm happy with the early progress and performance of these three recently completed acquisitions, Hemmelrath, SEM, and Whitford, which will add about $400 million in annual revenue, of which approximately $100 million is in the Asia-Pacific region.

Acquisitions remain one of our preferred cash deployment options, given the value that these have driven for our shareholders over the years. And currently our pipeline remains solid. In addition to acquisitions, we have progressed our key capital expenditures during the second quarter, and we expect total spending to be about 3 percent of sales in 2019.

Also, earlier today our Board of Directors approved a $0.03 per share dividend increase. We have paid uninterrupted annual dividends since 1899, and 2019 will mark 48 years of increased dividend payout. And we are pleased to continue to reward our shareholders in this manner. We ended the second quarter with more than $1 billion of cash and short-term investments, which continues to provide us with significant financial flexibility.

Finally, I'd like to thank and recognize PPG's 47,000 employees all over the world for the continued support in strengthening our position as a leading paint coatings and specialty materials company. Every day our employees are driving our cultural initiative the PPG way to provide innovative solutions for our customers' most pressing challenges and to deliver value to all our stakeholders.

This concludes our prepared remarks. Once again, we appreciate your interest in PPG. And now Jaime, would you please open the line for questions.

QUESTION AND ANSWER

Operator
Ladies and gentlemen, we will now begin the question and answer session. To ask a question, you may press "*" and then "1" using a touch-tone telephone. If you are using a speaker phone, we do ask that you please pick up your hand set before pressing the keys to ensure the best sound quality.

To withdraw your questions, you may press "*" and "2." In addition, we do ask that you please limit yourselves to one question and a single followup for the interest of time.

And our first question today comes from David Begleiter from Deutsche Bank. Please go ahead with your question.

David Begleiter
Thank you. Michael, just on raws, how are you looking at raws in the back half of the year, and what do you expect to happen with the Ti02 prices in the back half of the year? Thank you.

Michael McGarry
David, there has been a lot of focus on raw materials in-house, but when you think about it, we have some of our commodities--most of our commodities are flat. Maybe one of them is still up. And we have a couple that are trending down. But overall, between that and overall inflation with salaries and everything else, we're still in a marginally inflationary environment. And we still have not recovered all the margin from our pre-inflationary peak. So, as you heard in my opening comments, we are still progressing with price increases, and we anticipate having further price, moving forward.

In regards to Ti02, what I would say is the same answer I gave at the very beginning of the year, is that Ti02 is really a non-event this year. And we're going to continue to focus on using Ti02 very efficiently. And our program, as you know, has been to optimize our formulations to minimize Ti02 usage. And this year, we're on track again to take an additional 1 percent out of our Ti02 consumption. So, I don't see the trends really changing. You know there's excess capacity on the sulfate side, and later in the back half of the year you have a chloride plant coming on. So, that's why we remain confident that Ti02 will be a non-event.

David Begleiter
And, Vince, just on buybacks, what were buybacks in Q2? How should we think about buybacks in the back half of the year? Thank you.

Vince Morales
Thanks, David, for the question. In Q2, our share count was relatively neutral year-over-year. We did minimal, if any, buybacks through the first six months of the year, except to offset some dilution we did with an acquisition. The--for the full year, our focus remained on not building our cash position. We have--on a year-over-year basis we have an active acquisition pipeline, which Michael alluded to in the opening remarks. That remains an important part of our cash deployment strategy for properties at the right price, create value for our shareholders. Absent that, if we can't execute on those, we would look to share repurchase.

David Begleiter
Thank you.

Vince Morales
Thank you, David.

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

John Roberts
Thank you. There's a Bloomberg report about PPG being among others looking at Axalta. I don't expect you to comment on the speculation, but could you just remind us how concentrated the auto OEM and auto refinish markets are, maybe just in general terms?

Michael McGarry
Well, I think the way to think about that is that the different numbers vary by region and by automakers. So, it's probably inappropriate for us to comment on not just the speculation but actually the market share because we could overestimate or underestimate the various people's shares. And I wouldn't want to put incorrect information out there. So, I probably would prefer to pass on it.

John Roberts
That's all right. Sorry, I didn't mean to put you on the spot. In the U.S. DIY retail channels, we've had some share shifts, first at Lowe's then at Home Depot, now Ace. If you looked in aggregate at the U.S. DIY retail channels, have market shares in aggregate changed much over the past year, or has it just been a lot of shuffling around between different channels?

Michael McGarry

Well, if you go back and look at this space over 20 years, you'll always see some movement as the various retailers try different strategies. By and large--I would say that market shares have stayed relatively constant by and large. There has been a little bit of shift here and there but not that much, more of a rounding there is what I would call it.

John Roberts
Okay, thank you.

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

Bob Koort
Thank you. Michael, I noticed in your heat map that refinish seemed to be in the marketplace a little bit weaker. Is that--you mentioned accident rates. But, is there any function of price hikes and buying patterns of your customer base or the market that has shifted from one year to the next? And then secondly, you mentioned--I guess you're lapping some very robust trends in the packaging market that sort of stalled out, but you indicated getting back to growth later in the year. Could you give us some more specifics on why that happens? Thanks.

Michael McGarry
Sure, Bob. So, let's start with refinish. We had a very strong 2Q last year with refinish. There's a couple of very large what we call multiline, or people who buy refinish from multiple suppliers. We had a pretty robust 2Q last year with those guys. Then they elected to not purchase in the third quarter. A lot of this is what I would call trying to take advantage of the pricing cycle in refinish.

So, from a demand standpoint, though, we're still picking up share. Our net gains on shops is a nice positive, and pricing has been very good in that sector. Claims are down about 2 percent, and totals are up 1 to 2 percent, so that puts that negative overall at about minus 3 percent.

So, our team has just rolled out new technology in Europe on precision metering of refinish products. It has gotten excellent traction so far. So, we're looking forward to seeing how that--since we're very early--we just rolled it out a month ago. We're very early in that. But, we anticipate that we'll continue to gain share in refinish, given our strong water-based technology and the fact that we've converted more shops of water than anybody else--everybody else in the industry combined.

For the packaging side, we still have very good technology, and we are trialing some additional new technology for the packaging space. That--those pack tests are going on right now. Once those pack tests are completed, we anticipate that the customers will be shifting some additional business our way, which will be a net positive for us. So, that's what we're looking at. Obviously, we have to wait until the conclusion of the pack tests, but we're feeling pretty good so far.

Bob Koort
Great. Thank you for the help.

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

John McNulty
Yeah. Thanks for taking my question. Look, there's a lot of noise between the weather and home sales and I guess the contract that you lost last year. Can you give us your thoughts going forward now that you have anniversaried that? How we should be thinking about the architectural--the health of the U.S. architectural market--and how you're thinking about kind of the next 12 months overall volume growth in that market?

Michael McGarry
Yeah, John, we see that market as growing, this year we would have said 2 to 3 percent, given the challenging weather that we have had. They will try to pick up as much of that as they can, so we might finish 1 to 2 percent for the year. But overall, our customers still have very good backlogs, and they feel very confident. They still are challenged to find enough labor to get all their projects done, but they have been able to successfully continue to win business as that trend again--from DIY to do it for me. That's going to continue.

So overall, we feel like we're in a good position plus, as you heard in my opening remarks, we have committed and we are on pace to out-earn in the third quarter what we were making pre-customer assortment loss. So, the business has been focused on that, and they are going to be in a position to start delivering that in the third quarter.

John McNulty.
Great, thanks. And then--and then just a question on the architectural EMEA market. It sounds like you're expecting kind of the usual seasonal dip. It did sound like the second quarter was a little bit washed with bad weather. Is there a way if we have a normal seasonal kind of weather pattern, if there is such a thing these days, that that--you could sequentially see kind of a stable to maybe even up scenario for EMEA architectural, or is that too aggressive?

Michael McGarry
Well, first of all, we have--we're going to have positive sales growth because of pricing. And right now, through the first, whatever you want to call it, 17 days, volume have been more consistent with prior patterns. But as you know, Europe takes August off, and so we're always hesitant to predict the third quarter until we see how much vacation time all our big painters take and then how they come back.

So, I would be--if I were sitting in front of your model right now, I would use the same predictions you've used for years past, but knowing that we are getting nice price gains in that business in Europe.

John McNulty
Got it. Thanks very much for the color.

Michael McGarry
Thank you.

Operator
And our next question comes from Ghansham Panjabi. Please go ahead with your question.

Ghansham Panjabi
Thank you. Good afternoon, everyone. In your slide deck, you basically commented on additional pricing actions for the performance coatings segment in the third quarter. Is that

specific to any region or business? And I didn't really see the same comment as it relates to industrial coatings. I guess, are you where you need to be in that business at this point as it relates to pricing?

Michael McGarry
We have positive price in every business and every region of the world. And it has been a positive story. Now, we've had positive price for nine consecutive quarters. We're still not where we want to be. We've had 11 quarters in a row of inflation, so we still have some catch-up to do. But, when I look at our industrial coatings segment and our industrial business within that, they are doing pretty well.

And so, I'm not concerned. Obviously, the biggest gap is in the automotive piece. And that's where we're working the hardest to get prices up. But, we still have more traction in all our industrial businesses.

Ghansham Panjabi
That's helpful. And then, just in terms of the outlook, you commented on 3Q volumes basically mirroring 2Q. How should we think, Michael, about the fourth quarter? The comparisons are quite a bit easier. You commented on auto dealer inventories in China, for example, as a potential positive. Just as we cycle into 2020, how are you sort of thinking about the world at this point?

Vince Morales
Hey, Ghansham, Vince--a little early to call Q4. We got to make our way through Q3. But, in the back half of--really in the back half of 2018, we had several key issues that make the 2019 period--make it a little easier from a comparable basis. We did have the refinish destocking Michael alluded to earlier.

We did just start the customer assortment changes. We will anniversary very shortly the China automotive downturn. And just from a top-line perspective, our currency has been a negative in the first part of this year, and it mutes out in the back half of the year. So, we have several things specific to PPG that we think gives us some comfort in our forecast.

Ghansham Panjabi
Thanks so much, Vince.

Vince Morales
Thanks.

Operator
And our next question comes from Michael Sison from KeyBanc Capital Markets. Please go ahead with your question.

Michael Sison
Hey, guys, nice quarter there. In terms of the outlook for the second half of the year, it certainly seems that demand is weaker. Volumes are going to come in a little bit weaker, I guess, than prior expectations. When you think about what has been--what you have been able to do to offset that--can you maybe frame up--was it mostly the cost savings--the new cost savings program? Are you getting a little bit better price for raws--and any other factors that might help you stay on track with your earnings guidance?

Michael McGarry
Yeah. So, Mike, I'd say it's everything. With 2.3 percent price, $20 million of costs down, better manufacturing, we pretty much have hit on all cylinders. Everything within our control the team has executed very well on, so we're going to continue to look at that. Volume in a lot of our businesses have been pretty good. Aerospace has had a very good volume quarter. PMC has had a good volume quarter. So, there are pockets of success. Unfortunately, when you look at OEM-type businesses, they have been a little struggling.

Michael Sison
Okay. And then, a quick followup on architectural Americas and Asia-Pacific, your outlook is low single digits for third quarter. Are you seeing--do you need to see that now, and is it kind of a fluid on a month-to-month basis as the year unfolds? Or is there any lumpiness in that outlook for the third quarter?

Vince Morales
No, just picking up on what Michael said earlier, we--there's growth in this market in the U.S. It has been tempered by the weather patterns. Anytime we see decent weather, we see good pickup in sales. So, we think there's some pent-up demand there. And we do expect growth in Q3 and a seasonally lighter quarter in Q4--but continued growth--so there's definitely a backlog of demand here.

Michael Sison
Great. Thank you.

Vince Morales
Thanks, Mike.

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

Frank Mitsch
Yes. Good afternoon, guys. Hey, you had a difficult comp on auto refinish in 2Q. You are suggesting that 3Q is going to be an easier comp due to the vagaries of the year-ago period, so just curious as to--how should we think about the underlying volume growth and sales growth that you can get in the refinish business?

Michael McGarry
Frank, I still see refinish as a flat long-term market. We are going to get positive price, we are going to work through our water. More people are going to convert to water which uses less product and solvent. At some point in time, China will start to put in regulations. We are the number one guy in China, so when you factor in the solvent to water conversions, you will see some negative volume over a longer period of time. But, we don't see collisions changing materially in the near-term.

Collision rates in Asia continue to happen, so--and, of course, there is still a growing car park around the world. So, this is a great business for us, as you know, and we're one of the global leaders. And we're still very excited about this business.

Vince Morales

And just to expand on that, Frank, our customers pay for technology, and we are part of the leadership in terms of technology in the industry. So, Michael refers to price. We really talk about price mix. The whole mix of the industry is moving up, reflective of the technology that everybody is bringing to the table. So, even though the absolute volume might be down a little bit, the cost per unit or cost per liter is up because of the mix component.

Frank Mitsch
That's very helpful. And I guess my followup would be, it has been about two months since you did your strategic review and decided to keep the portfolio as is. I'm just curious in terms of the feedback that you have received from your shareholder base. Is there any color you can provide in terms of the positive or negative feedback that resulted from that decision?

Vince Morales
Yeah, Frank, we talked to obviously a lot of shareholders. Those are conversations we have individually with them. The feedback we look at is what happens to the stock every day in the marketplace. That's what I would reference you to.

Michael McGarry
Yeah. And, Frank, one other thing I might add back on the refinish question I should have pointed out. We do have a light industrial piece of that business and a commercial transport. And both of those segments are growing. Of course, they are much smaller than the base refinish business, but those are a help offsetting some of the trends we talked about earlier.

Frank Mitsch
Great. Thanks so much.

Operator
Our next question comes from Jeff Zekauskas from JPMorgan. Please go ahead with your question.

Jeff Zekauskas
Thanks very much. I was looking at corporate expense. I think for the first half it's $90 million versus $66 million a year ago. And I think for the third quarter, you said your corporate expense would be $45 million, and maybe last year it was $26 million. So, it looks like that through the first three quarters, your corporate expense will be up, I don't know, $40 million or $45 million. What is going on there? What is behind that? Or is it a timing issue and corporate expense in the fourth quarter comes down a lot?

John Bruno
Hey, Jeff. This is John. I think there's two key drivers. One is last year we made some adjustments to our incentive compensation accruals in the second and third quarter. And last year, we had a little bit more favorable pension expense based on the different items like the discount rate and consensus data that we have. So, the former is the bigger driver, but a couple of things there, Jeff, that are driving the upswing this year.

Jeff Zekauskas
Okay. And then, for my followup, the--your SG&A costs year-over-year were down a little bit both in the first quarter and the second quarter. But last year, your SG&A really fell pretty sharply in the third quarter. It went from I think something like 9.41 to 8.67 from the second to the third quarter. Is your SG&A going to be lower year-over-year or roughly lower year-over-

year in the third quarter? Or does it rise maybe because of the compensation expenses you are talking about? How does the SG&A look year-over-year in the third quarter?

Vince Morales
Yeah, Jeff, those two questions--I think your first and second questions are interlinked. Some of the numbers John mentioned are located in our SG&A cost pool, so there's variability there. Currencies--if you're looking on an absolute number basis, currency is a big impact to just absolute numbers. So, we did have weaker foreign currencies last year, so that has an impact as well. We're--our steady run rate--we're adding Q2 of 2019. We expect to be comparable as a percent of sales in Q3. We do have lighter seasonality in Q3 versus Q2 as well, so that's not--
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Jeff Zekauskas
--Sure. Yeah. Okay, great. Thank you so much.

Vince Morales
Thanks, Jeff.

Operator
And our next question comes from P.J. Juvekar from Citi. Please go ahead with your question.

P.J. Juvekar
Yeah. Thank you. So, Michael, you talked about China auto inventories coming down, and that's a good thing. When you talk to your customers in the OEM market, what signals do you get when you look at their production schedules for 2020? Do you think market can grow--come back to growth again in 2020 for Chinese auto OEM?

Michael McGarry
Well, I do believe it will be up in 2020. I think it's a little early to call that, though. I don't think the trends that we're seeing right now are going to continue, but the single biggest factor in this is the trade war, if that's what you want to call it. People have money in their pocket in China. People are employed. It's a lack of consumer confidence. These--our Chinese employees themselves--they are also looking at the same thing. I was just over there six weeks ago, and the fact of the matter is for major purchases, they are sitting on the sidelines to see how this turns out.

So, the first thing that I'm looking for is a settlement where everybody can move on from the current positions that everybody has staked out. Consumer confidence will flow very quickly because it's not like they have to get people re-employed over there. They are already employed, and are saving money right now in this environment.

And so, they have a lot of fire power to put to work. So, I think whenever this does settle, we will see a pop, not too much different than we saw, what quarter was it? It was the third quarter last year when they changed the tariffs--or the VAT. So, I think there will be a--there will be a pretty good movement in that.

P.J. Juvekar
Okay. Thank you. And for my second question, recently there was a market share change at Ace Hardware, and you talked about that a little bit. Was PPG involved in any of those discussions? And then, when you lost some volumes at one of your retail customers, are those volumes still available if you get an order, or do you shut that capacity down?

Michael McGarry
P.J., I don't think it's appropriate for us to discuss specific customers. You should assume that any place there's somebody buying paint that we're actively talking to those customers. From a paint plant standpoint, we did shut down some plants in response to the customer assortment change, but we still have capacity in the marketplace. And as you know, ramping up a paint plant sometimes is as simple as adding another shift or running overtime. So, we are definitely flexible enough to respond to the market.

P.J. Juvekar
Great. Thank you.

Michael McGarry
Thanks, P.J.

Operator
Our next question comes from Arun Viswanathan from RBC Capital Markets. Please go ahead with your question.

Arun Viswanathan
Thanks a lot. Good afternoon. Just a question on the guidance. Last quarter, you had mentioned that embedded within your guidance, there was a little bit of a recovery in China. And obviously production rates have continued to lag on the auto side, potentially seeing some continued slowing due to the trade skirmishes. So, I guess, where do you stand on China? Is that part of what pushed you to the upper end of the 7 to 10 percent recovery there? Maybe you can just give us your comments there. Thanks.

Vince Morales
Yeah, Arun, if you noticed, we did talk about the sales guidance being low single digits. I'd see a stretch to get to the bottom end of our prior range on sales. So, that's really where we saw the downtake we--or the updraft we didn't experience during Q2. We do have, as we walk into every quarter, three, four, five, six weeks of order book in hand for most of our OEM customers, not just our auto customers.

So, we typically have at least an early read on what each quarter is going to look like. We don't--as Michael mentioned in the opening comments, we don't see a significant uptick in Q3 in Asia or China specifically. So, again, we lowered our sales guidance for the year. As you would expect from us, we're compensating on the cost side to account for the lower sales.

Arun Viswanathan
And just as another followup, on the raw material side obviously there was some deflation in Q2. When do you see that kind of flowing through your system? And maybe you can just relate that to the inventories of raws that you have. Thanks.

Vince Morales
Yeah, a couple points, Arun. One, we're still seeing pockets of inflation. And secondly, we have to--we have to recognize there are still two years of inflation we absorbed. So, we still have a lot of catch-up to do on the pricing side. We're going to work through that. Furthermore, if we do see changes in our raw material basket, they have to flow through inventory. We're getting to a period of the year where--obviously sales season, they are going to be lower. So, we typically have a hold on our inventory a little longer.

Arun Viswanathan
Thanks.

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

Christopher Parkinson
Great. Thanks, guys. When you think about your progression back towards prior peak margins just generally, how shall we think about your expectations for industrial and performance--just towards the end of this year and 2020, just very broadly? I mean, what additional levers can you even pull now, given the volume environment? Or could you even just pull harder to get back to this level? Just any key moving parts would be appreciated. Thank you.

Michael McGarry
Chris, this is Michael. The levers are going to still be the same. We talked about having more than 2 percent price in Q3, so that's going to be a positive. Moderation and the inflation, that's going to be a positive. We're going to have additional cost savings. That's going to be a positive. The teams are working really hard on the manufacturing side, so that's going to be a positive.

So, I think that trend lines that you've seen will continue in that regard. The big challenge we have is obviously we need a lot more price in our automotive business and a little bit more price in our industrial business to get back to where we need to be. And so, that's front and center.

Christopher Parkinson
Got it. And can you just talk a little bit more about your performance in aero and how sustainable that is just in the intermediate to long term? I understand you're obviously doing a lot more than paint in the end market, including obviously a growing presence in services. So, how should we just generally think about your long-term strategy versus, let's say, the core growth on the coatings side? Thank you.

Michael McGarry
Well, we expect to outperform industry for quite a number of years in this business. If you look at the segments that we're in, we're leading in coatings, so we're going to be slightly better than market there. If you look at our transparencies, we've been--our customer pull on new programs has been quite significant. And so, we have customers that are asking us to bring them new technology, which they are more than willing to pay for. And that has been a significant win.

And then, of course, on the sealant side, our new technology on lighter weight sealants and cure-on-demand is going to be trend lines that our customers all value highly, and it drives tremendous productivity in their businesses. So, they are going to stay on top of that.

And then, for a lot of our customers, because we're so important to them, we provide chemical management services or unique packaging to help their productivity on their lines. And so we have consistently--so, you look at this past quarter, the industry grew about 5 percent, and we almost grew double digits. We grew double digits the prior quarter. And we're going to grow somewhere in that double digit range in the third quarter. So, even though this has historically

been a lumpy capital intensive business, this is a market that we're super excited about, and we continue to outperform in all the major segments.

Christopher Parkinson
Thank you.

Michael McGarry
Thanks, Chris.

Operator
Our next question comes from Kevin McCarthy from VRP. Please go ahead with your question.

Kevin McCarthy
Good afternoon. Vince, on slide 9, I think you indicate anticipated cost savings of $17 million to $20 million in the third quarter from your restructuring efforts. My question is, what does the glide path look like in 4Q and beyond as the new program ramps and the older ones are executed upon? Is that a relatively steady pace we can extrapolate?

Vince Morales
Yeah, we said 80--70 to 80 for the year, Kevin, for 2019. We're pacing slightly ahead of that right now, and that's the basis of the old programs we have. We'll pick up a few million dollars in the fourth quarter on our new program, but the new program won't really kick in in earnest until early 2020. And there are some longer lead items in there. So, by the end of 2021, we'll be at the $125 million run rate. So, I would assume a linear progression as we go through 2020 into 2021.

Kevin McCarthy
Great. And then shifting gears, the text of your prepared remarks indicated that you had some customer wins in Latin America. Can you comment on which businesses those were in and how large they are? I'm not sure if they are material or not.

Vince Morales
Yeah. These are mostly in our industrial segment, Kevin. We have some benefit in our auto business. We--it's really customer mix. We underperformed in the U.S., we overperformed in Latin America, really serving the same market. But, given we give regional outlooks in addition to business outlooks, we had to flip between those two regions.

John Bruno
And, Kevin, just on top of that--this is John--packaging has been doing very well in South America.

Kevin McCarthy
Did you win business in packaging there?

John Bruno
Correct, in South America packaging has been winning business.

Kevin McCarthy
Thank you very much.

Michael McGarry

And, of course, Comex continues to win on a daily basis.

Operator
Our next question comes from Stephen Byrne from Bank of America Securities. Please go ahead with your question.

Stephen Byrne
Yes, thank you. That sealant and adhesive technology that you have in your aerospace business, is that suitable to be transferred to one of your other businesses such as autos end markets or construction?

Michael McGarry
So, we have sealant and adhesive businesses in our aerospace, our automotive, our architectural, and a teeny, tiny bit in our industrial business. We share technology across segments. So, when we launched the most recent liquid nails product, it used some of the technology that we had in our aerospace business, and that was a win. We currently have also launched some new products for the U.S. military, and that technology can also be shared across the various platforms. So, we routinely share technology across our various business segments.

Stephen Byrne
And then, on this most recent cost management program, this $125 million program, it reads basically three buckets, some manufacturing consolidation, some trimming of low margin businesses, and then head count cuts. Can you allocate that program into those three buckets? And were these readily identifiable? Do you see another round after this one?

John Bruno
Steve, this is John. So, we're not going to get to that specific level of detail. But, these are opportunities we've identified both in continuing to improve our cost structure and inflection of the demand environment that we have today.

Stephen Byrne
Thank you.

Operator
Our next question comes from Michael Harrison from Seaport Global. Please go ahead with your question.

Michael Harrison
Hi. Good afternoon.

Vince Morales
Hi, Michael.

Michael Harrison
Just a question on the regional pricing dynamics in auto OEM and on the sustainability of pricing there. You said that pricing had increased in all regions. I believe that was the comment last quarter as well. How much was pricing up, and if there were any differences from region to region, what was driving it?

Michael McGarry

No, Mike, we have pretty much similar pricing across the regions. You can well imagine we deal with global customers, and you're dealing with people that are very sophisticated in how they deal with you. So, we're getting it across the regions and across the platforms. And we are getting it with the local Chinese in case that was your next question as well.

Michael Harrison
Okay. And then, my other question is related to the refinish business and these lower collision claims in the U.S. I mean, is that accident rates coming down? Are we starting to see the impact of collision avoidance systems? Any thoughts on what is behind that?

Michael McGarry
Well, really what you have is a plateauing. Collision is driven by congestion, which is driven by employment, which is driven by miles driven. And right now, unemployment has plateaued at, let's call it, 3.8, 3.7, whatever you want to call it. And so, that leads to less collisions when it plateaus. And there has been some impact from lane departure and smart cruise control. But, you had the negative impact of distracted driving, which I hope you're not doing, Michael. But overall, I would say you should assume a minus one is kind of what you should probably think about in the long term.

Vince Morales
And, again, as we said earlier, Michael, that's total volume. There's a value uplift in this business, as there has been for many years. All the participants add new technology, and the technology is definitely desired by the body shops for productivity purposes.

Michael Harrison
All right. Thank you very much.

Operator
And our next question comes from Duffy Fischer from Barclays. Please go ahead with your question.

Duffy Fischer
Yeah, good afternoon. First question is just around the delta between inventory--not inventory--between volume being down 4 percent and GDP being positive 1 or 2, a pretty big gap. Anecdotally, when you talk to your customers, are they destocking where maybe their real consumption is running at higher levels than that and so we'll get a bounce back sometime in the next couple quarters?

Vince Morales
Yeah, Duffy, we really look at industrial production, not GDP. GDP includes services. So, industrial production has certainly not been strong in the first half of the year. But, really, to the heart of your question, we see most of our customers running lean on inventory, leaner than we've seen in the past. Michael, again, alluded to that in the opening comments. If there is any surge in demand, there might be a little bit of a two stack here, not only the demand surge but also inventory replenishment. So, that's certainly plausible.

John Bruno
Yeah, and Duffy, I would say, think about the volume more at a two level, not a four level because of the customer assortment changes.

Duffy Fischer

That's fair, okay. And then, just last quick one, Vince, the billion in cash you have now, if you found a place to use that, how much cash do you need to run the business? How low can you take that cash balance?

Vince Morales
Well, it's a seasonal question. We obviously are building inventory in the beginning of the year. We run that down in the back half of the year, so we need a little less cash on a daily basis, somewhere between $400 million and $700 million, depending on the season.

Duffy Fischer
Great. Thanks, guys.

Michael McGarry
Thanks, Duffy.

Operator
Our next question comes from Garik Shmois from Longbow Research. Please go ahead with your question.

Garik Shmois
Thank you. I know it's early, but if we're looking out to 2020 and thinking about pricing, and you've been very committed to getting price over the last several years, but in a slower volume environment, just wondering, how long can you keep pushing this 2 percent or so price cadence?

Vince Morales
I'll start. Michael can finish the question here. But, we saw our suppliers push price for two and a half years, and we had an amiable demand environment when that occurred. Again, we're just trying to catch up, maintain the value chain. So, that's--again, we saw it on our--coming into our front door for two and a half years.

Michael McGarry
And I would add innovation. Our customers are always very willing to pay for innovation. If you think about the cost of the paint versus the cost of their final product, if we can get one more car through the body shop or one more heavy duty equipment out, we can make the packaging line run a little quicker. Anything like that, they are more than willing to pay for. So, that's why we're so focused on innovation. And sometimes innovation leads to slightly lower volumes, but it leads to a richer mix with higher pricing, so that's also something you should factor in.

Vince Morales
And if I could just pick up on that because what we typically do see when demand is a little choppy like it is today, customers are looking for ways for cost savings, and that plays right into that kind of innovation center that we have.

Garik Shmois
I was just wondering if you could update us just on paint store openings in the U.S., how that has tracked year-to-date and what the outlook is for the second half.

Michael McGarry
Yeah, I try to always get people off this question. It's--for the U.S., it's not the key driver for our business. We're focused on servicing our customer needs. We have an authorized dealer

network, we have our own paint stores, we have our own DIY customers. So, for us we're doing different things in different markets, so we add stores in places that are growing like Texas and Florida. And we might be subtracting stores from contracting markets. So, for us our store count was relatively flat overall. And that's not a metric that we're a driver of in the U.S. If you want to look at Mexico where we have 50 percent market--more than--a significant share down there, we are driving additional store growth down there, and we are continuing to take share.

Garik Shmois
Thank you.

Operator
Our next question comes from Jim Sheehan from SunTrust Robinson Humphrey. Please go ahead with your question.

Jim Sheehan
Thanks. Regarding China, you mentioned the unexpected early implementation of China 6 emission standards in large cities. Did you see that impact retail buying patterns at all, or was that just an impact on OEM production schedules?

Michael McGarry
Well, you do see a little bit of it because the dealers are trying to get those vehicles off their--off their lots in Shanghai, so they don't have to then move them to a tier three-type city. So, you did have--sales were up I think 6 percent in June. And sales in July appear to be trending positively as well. But, I would tell you that it's hard to parse between how much of that is a change in emission standards versus the actual demand.

Jim Sheehan
Terrific. And then, on--there are some deals in the coatings space announced recently, including aerospace coatings. Are you seeing a lot of competition for M&A, given the attractiveness of the aerospace market?

Michael McGarry
Well, what I would say is that any asset that comes up for sale in the coatings space always attracts interest. There are some natural buyers, there are people who are consolidators on a continuous basis, and you should assume that when any asset comes up for sale that unless there's an issue with it, it's going to trade at a pretty reasonable multiple.

Jim Sheehan
Thank you.

Operator
And our last question today comes from Dmitry Silversteyn from Buckingham Research. Please go ahead with your question.

Dmitry Silversteyn
Good morning. Thanks for squeezing me in there. A lot of my questions have been answered, but I'd just like to go back to Vince's response to Garik's question on pricing. You mentioned that you have taken price for 11 quarters when the demand conditions were amenable. And we've had strong economic conditions. We're seeing a pretty meaningful slowdown across the globe when it comes to industrial economy. And if you kind of read the early signs, it may actually get worse before it gets better. How does this environment--given that, yes, you are

adding technology, but you're competing against other very competent players out there with technologies of their own--are you--am I fair in saying that you may be sacrificing a little bit of volume growth to make sure you get the pricing, and that is the most important part of your strategy in a short term is to restore your margins through price and then worry about volumes later?

Michael McGarry
Dmitry, that's 100 percent accurate. We're--we are expecting to get paid appropriately for the technology we deliver. If we haven't been able to get that, we have been willing to walk away from volume. We--as you saw, our volumes in 2018 in architectural Europe--we're down as we were the only ones out there leading price. Now that the other parties are up there leading price along with us, volume is flowing back our way. We've always said that we might get short-term penalized for raising the price, but ultimately most of our customers want to do business with PPG. And as soon as our other friendly competitors--if they decide to raise price independently, some of that volume could flow back to us, and we do see that happening sometimes.

Dmitry Silversteyn
Okay, that's very helpful. And as a followup, just a couple of bookkeeping items. In your general industrial business, you talked about your revenue being down. What was--there has got to be a price component in there. So, what were the volumes in GI down? And then, a similar question on European paint--what was the foreign exchange impact on the European paint business?

Vince Morales
Those are granularities we typically wouldn't give, Dmitry. We did say that the segment volumes I think were down about 5 percent, general industrial--auto is more than that--or excuse me, in our industrial segment. Auto is more than that. General industrial was less than that. The proxy for currency in our architecture EMEA business would be just euro to the dollar. That would get you pretty close.

Dmitry Silversteyn
Got you. Thank you. That's all I have.

Vince Morales
Thank you. We appreciate it.

Operator
And ladies and gentlemen, that will conclude today's question and answer session. I'd like to turn the conference call back over to management for any closing remarks

CLOSING REMARKS

John Bruno
Thanks, Jamie. I'd like to thank everyone for their time and interest in PPG. If you have any further questions, please contact our Investor Relations Department. This concludes our second quarter earnings call.