



We create chemistry

# **Analyst Conference Call Q3 2020**

## **Speech**

### **October 28, 2020**

**Martin Brudermüller**

Chairman of the Board of Executive Directors

**Hans-Ulrich Engel**

Chief Financial Officer

The spoken word applies.

## Martin Brudermüller

Good morning ladies and gentlemen,  
and thank you for joining us.

We hope you and your families are doing well. During the last couple of weeks, we have seen how difficult it is to contain the pandemic, as the spread of the virus is sharply increasing again in many countries worldwide. At BASF, we are doing everything we can to work safely in this environment. We have reintroduced stricter measures that were no longer necessary during the summer months, but now are advisable again.

On October 9, BASF released preliminary figures for the third quarter of 2020 and published an outlook for the full year 2020. Today, we will provide you with further details.

### **[Chart 3: Chemical production growth in China continues, recovery also visible in the U.S. and Europe]**

To begin with, let's turn to the macroeconomic environment. The indicators for Q3 2020 are estimates as most countries have not yet published their figures for the quarter. Overall, the macroeconomic indicators improved in Q3 2020 compared with Q2 2020. However, the future macroeconomic development remains very uncertain.

According to the preliminary data, global chemical production was slightly positive in Q3 2020 compared with the prior-year quarter. The resilience of chemical demand in some highly relevant customer industries is one reason for this. Another reason is China: The country continues its V-shaped recovery. Regarding the development in other regions, the bottom seems to have been reached and a gradual recovery is occurring.

Global GDP and global industrial production declined by 4.3 percent and 3.0 percent, respectively, compared with the prior-year quarter. Global automotive production was still around 2 percent below the prior-year quarter. For the full year 2020, we now expect light vehicle production to decline by around 20 percent, while we previously had assumed a decline of 27 percent.

**[Chart 4: BASF Group Q3 2020: Sales volumes in Greater China significantly above prior-year months]**

On this slide you can see how regional macroeconomic developments are reflected in our volume growth by region.

Overall, **BASF Group** sales volumes were 2 percent lower in Q3 2020 compared with Q3 2019. This was driven by lower volumes in July and August, while we achieved a 4 percent volume increase in September 2020 compared with September 2019.

In **Europe**, volume growth improved in the course of the quarter and turned positive in September. In the **U.S.**, volume growth compared with the prior-year months remained negative due to the outage of the steam cracker in Port Arthur, Texas. Excluding this effect, volumes in the U.S. would also have turned positive in September. In the meantime, the Port Arthur cracker is back on stream.

In contrast, we recorded double-digit volume growth in **Greater China** across almost all segments over all three months in Q3 2020. We continue to benefit from our strong position in China. The planned new Verbund site in Guangdong province will further increase our presence and customer proximity in the dynamically growing Chinese market.

**[Chart 5: The gap in BASF's average daily order entry is slowly closing, but visibility remains low]**

This graph shows that the gap between average daily order entries in April to September compared with the prior-year months is slowly narrowing. A look at the October month-to-date figures reveals that daily orders are still slightly below the prior-year month. The recent worsening of the infection situation worldwide is jeopardizing this development and might again negatively impact our order entry in the coming months.

As in the prior quarters, customers remain very cautious and are ordering lower volumes more frequently. About 50 percent of orders on hand – across BASF – are booked during the next month. Another 30 percent of all orders have a delivery date in the month after that. This means that 80 percent of all our orders on hand will be booked within the next two months. And we continue to have no clear view beyond that.

**[Chart 6: BASF Group Q3 2020: Volumes declined slightly, to a large extent due to lower demand as a result of the pandemic]**

Let us now turn to the volume development by segment.

Compared with the prior-year quarter, sales volumes declined by 2 percent on a BASF Group level. This volume decline was mainly driven by the Chemicals segment. Here, the cracker outage in Port Arthur burdened the volumes development. On a BASF Group level, the cracker outage had a negative volume effect of around 1 percent in Q3 2020. It thus accounted for half of the decline.

In the Materials and Industrial Solutions segments, we also recorded lower volumes, mainly due to lower demand from the automotive industry. In Other, volumes declined on account of lower raw material

trading activities. Volumes in Nutrition & Care were almost stable coming down from the elevated levels during the first half of 2020.

Volumes in Surface Technologies increased, and strongly so in Agricultural Solutions, which partially offset the overall volume decline.

**[Chart 7: BASF Group Q3 2020: Sales and EBIT before special items improved compared with Q2 2020, but are still below prior-year quarter]**

Let us move on to our sales and earnings development in Q3 2020 compared with the prior-year quarter. I will start with our sales development and the graph on the left:

- **Sales** decreased by 5 percent to 13.8 billion euros.
- **Currency** effects of minus 6 percent were the main driver for this. Currency headwinds were mainly caused by the devaluation of the Brazilian real and the US dollar.
- Lower **volumes** of minus 2 percent also contributed to the sales decline, as I already explained.
- **Prices** increased by 2 percent. Considerably higher prices in Surface Technologies, especially due to higher prices for precious metals, and slightly higher prices in Agricultural Solutions were the reasons for this.
- **Portfolio** effects contributed plus 1 percent, mainly from the acquisition of Solvay's polyamide business.

Moving on to the earnings development and the graph on the right.

**EBIT before special items** came in at 581 million euros, 45 percent below Q3 2019. All segments recorded lower earnings.

However, EBIT before special items rose by 355 million euros compared with 226 million euros in Q2 2020. This was mainly driven by good business development in September.

In the **Chemicals** segment, compared with the prior-year quarter, both divisions recorded considerably lower EBIT before special items due to lower margins and volumes. The decline was most pronounced in the Petrochemicals division. The cracker outage at the Port Arthur site had a negative earnings impact of around 100 million euros in Q3 2020. In the Intermediates division, lower fixed costs could partially offset the earnings decline.

In the **Materials** segment, EBIT before special items decreased considerably due to lower earnings in the Monomers division. Lower volumes and prices for polyamides were the main reasons for this decline. Higher isocyanate margins due to lower raw material prices and increased MDI volumes could only partially offset this. In Performance Materials, EBIT before special items increased slightly, mainly due to a positive contribution from the acquired businesses from Solvay. Compared with Q2 2020, EBIT before special items in the Monomers and the Performance Materials divisions improved significantly.

EBIT before special items in the **Industrial Solutions** segment came in slightly below the prior-year quarter due to considerably lower contributions from Performance Chemicals. This was mainly driven by lower volumes, for example in fuel and lubricants solutions as well as oilfield chemicals. In Dispersions & Pigments, EBIT before special items improved slightly, mainly due to lower fixed costs.

EBIT before special items in the **Surface Technologies** segment almost matched the level of the prior-year quarter. In the Catalysts division, earnings improved slightly, mainly due to lower fixed costs.

In the Coatings division, earnings decreased compared with Q3 2019 due to lower sales volumes, especially in the automotive industry. Compared with Q2 2020, EBIT before special items in the Catalysts and the Coatings divisions improved especially strongly.

In **Nutrition & Care**, EBIT before special items decreased considerably on account of lower contributions from both divisions. The Nutrition & Health division recorded lower EBIT before special items, primarily as a result of higher fixed costs. The prior-year quarter had benefited from an insurance payment. Earnings also declined considerably in the Care Chemicals division. This was due to lower volumes and higher fixed costs. The figure for the prior-year quarter included a contractual one-off payment in the personal care solutions business.

In **Agricultural Solutions**, EBIT before special items came in considerably below the prior-year quarter. While volumes significantly increased and prices were slightly up, sales and earnings were burdened by strongly negative currency effects. The currency impact was most pronounced in South America and here mainly driven by the depreciation of the Brazilian real.

In **Other**, EBIT before special items decreased significantly compared with the third quarter of 2019.

With that I will hand things over to Hans.

## Hans-Ulrich Engel

Good morning.

### **[Chart 8: The pandemic is impacting key customer industries differently]**

Let us have a look at how the pandemic impacted our key customer industries. Due to limited data availability, this external data represents the aggregate of EU, China and the U.S., and is preliminary for Q3.

China has quite a high weight in many of these industries, therefore the development is strongly impacted by the V-shaped recovery there. Nonetheless, these figures should give a good indication of global trends.

Besides the strong recovery in automotive, we are seeing a recovery of durable consumer goods and in construction activity. Information and communication technologies continue to show robust growth, owing to solid demand and the very high weight of China's production. Demand in health and nutrition is less volatile and shows tendencies towards normalization.

### **[Chart 9: Details on the impairments in the third quarter of 2020]**

After describing the development of our customer industries, I would now like to provide some further details regarding the non-cash-effective impairments in Q3 2020.

Our impairment tests identified asset impairments of 2.8 billion euros due to a considerably weaker macroeconomic environment and weaker demand outlook in certain industry segments as a consequence of the pandemic. The impairments were mainly booked in the following segments:



- In **Surface Technologies**, the weaker future demand from the automotive and aviation industries led to impairment charges of around 1.0 billion euros.
- In the **Chemicals** and **Materials** segments, the continued oversupply of basic chemicals and the associated margin pressure resulted in impairments of around 1.3 billion euros in total.
- In **Agricultural Solutions**, measures to streamline BASF's glufosinate-ammonium production resulted in impairments of around 300 million euros.

In the Industrial Solutions and Nutrition & Care segments, impairments added up to less than 200 million euros in total.

**[Chart 10: Excellence Program 2019 – 2021: On track to achieve the targeted annual EBITDA contribution]**

Let us move on to the measures we are implementing under the umbrella of our Excellence Program.

Overall, we are well on track to achieve the targeted 2 billion euro annual EBITDA contribution by the end of 2021. Regarding the personnel cost savings, we targeted to reduce 6,000 positions globally by the end of 2020. According to our current estimates, around 10 percent of this reduction will likely be delayed to 2021, mainly due to labor market effects caused by the pandemic.

Let me also specify the EBITDA contribution and associated one-time costs we expect by the end of 2020: We now expect an EBITDA contribution of around 1.4 billion euros by the end of December 2020. This is a run-rate. The associated one-time costs in 2020 are estimated to be around 300 million euros.

**[Chart 11: Realignment of BASF's Global Business Services unit – expected annual cost savings of >€200 million from 2023 onwards]**

At the end of September, we announced the realignment of BASF's Global Business Services unit. The division was established as of January 1, 2020. As of that date, around 8,400 employees worldwide transferred to Global Business Services without further changes in the organization. Since then, the unit has been providing services for BASF Group, ranging from financial and logistical processes to services in the areas of communications, human resources, and environment, health & safety, mainly following established processes.

By fundamentally simplifying and reorganizing processes with an end-to-end logic as well as utilizing digital solutions, the division wants to meet the needs of BASF business units flexibly and more competitively. As part of this, more services than before will be bundled in hubs, which will offer as many services as possible for the units in the BASF Group.

Following the bundling of services and resources and the implementation of a wide-ranging digitalization strategy, the number of employees in Global Business Services worldwide will be reduced by up to 2,000 by the end of 2022. This reduction is not part of the Excellence Program, which we will conclude at the end of 2021.

From 2023 onward, we expect to achieve annual cost savings of over 200 million euros from the realignment of the Global Business Services unit. Provisions of around 300 million euros for the necessary measures were recognized in Q3 2020.

**[Chart 12: Major portfolio measures in 2020 and 2021]**

Let me provide you with a short update on our portfolio measures.

We closed the sale of the **construction chemicals business** to an affiliate of Lone Star on September 30. The purchase price on a cash and debt-free basis is 3.17 billion euros. The construction chemicals business now forms the newly founded MBCC Group. The standalone business is very well positioned on the construction chemicals market. We wish the team much success for the future.

The sale of the assets and liabilities of the construction chemicals business and the related disposal gain – likely to be around 300 to 400 million euros – will only be reflected in BASF's reporting on the fourth quarter of 2020. Payments received until September 30 in connection with this divestiture are, however, included in the statement of cash flows for Q3 2020 under cash flows from investing activities.

The sale of our **pigments business** to DIC/Sun Chemical was expected to close in Q4 2020. We now expect the closing to be delayed to Q1 2021. The project teams are jointly preparing the closing and the integration to allow for a swift and seamless cutover once merger clearance from all relevant authorities has been granted.

With respect to **Wintershall Dea**, we are realizing the announced synergies. We are also working on IPO preparedness. We now assume an initial placement in 2021, again subject to market conditions.

**[Chart 13: BASF Group Q3 2020: Key financial figures]**

I will now focus on further details regarding the earnings and cash flow development of BASF Group in Q3 2020 compared with the prior-year quarter:

- EBITDA before special items decreased by 22 percent to 1.5 billion euros. EBITDA amounted to 1.0 billion euros compared with 2.3 billion euros in Q3 2019.
- EBIT before special items came in at 581 million euros, 45 percent lower than in Q3 2019.
- Special items in EBIT amounted to minus 3.2 billion euros compared with plus 280 million euros in Q3 2019. Around 2.8 billion euros are related to the non-cash-effective impairments. Around 300 million euros are related to the realignment of BASF's Global Business Services unit.
- EBIT thus decreased to minus 2.6 billion euros from 1.3 billion euros in Q3 2019.
- Net income amounted to minus 2.1 billion euros compared with 911 million euros in Q3 2019, mainly due to the non-cash-effective impairments, the lower EBIT before special items, and provisions for restructuring.
- In Q3 2020, cash flows from operating activities increased by 5 percent to 2.1 billion. The increase was mainly driven by lower miscellaneous items and cash released from net working capital. In Q3 2019, miscellaneous items comprised the reclassification of the gain on the sale of the Klybeck site in Basel, to cash flows from investing activities.

- Payments made for property, plant and equipment and intangible assets decreased by 190 million euros to 736 million euros. Free cash flow increased by 27 percent to 1.4 billion euros.

#### **[Chart 14: Cash flow development Q1 – Q3 2020]**

Let's now turn to our cash flow in the first nine months of 2020:

- **Cash flows from operating activities** amounted to 3.3 billion euros compared with 4.3 billion in the prior-year period. This was primarily due to the lower net income and the higher level of cash tied up in net working capital. Net working capital increased by 1.0 billion euros, mainly as a result of higher prices for precious metals affecting trade accounts receivable and the metal trading positions.
- **Cash flows from investing activities** amounted to minus 674 million euros in the first nine month of 2020, compared with plus 47 million euros in the prior-year period. The decrease was mainly driven by lower net cash inflows from acquisitions and divestitures. Payments made for property, plant and equipment and intangible assets decreased by 23 percent to 2.0 billion euros.
- **Financing activities** led to a cash inflow of 778 million euros in the first three quarters of 2020, compared with a cash outflow of 4.7 billion euros in the prior-year period.
- **Free cash flow** declined from 1.7 billion euros in the prior-year period to 1.3 billion euros, mainly due to the lower cash flows from operating activities. Lower payments made for property, plant and equipment and intangible assets could partially offset the decline.

**[Chart 15: Strong balance sheet]**

Turning to our balance sheet at the end of September 2020 compared with year-end 2019:

- Total assets were stable at 87 billion euros.
- Compared with the end of December 2019, noncurrent assets decreased by 4.0 billion euros to 51.9 billion euros, mainly driven by the non-cash-effective impairments. In addition, negative currency effects contributed to the decline.
- Current assets rose by 4.1 billion euros to 35.0 billion euros, mainly due to higher cash and cash equivalents, as well as higher other receivables.
- Compared with the year-end 2019, net debt increased by 196 million euros to 15.7 billion euros. Compared with the end of Q2 2020, net debt decreased by 4.8 billion euros.
- At the end of September 2020, the equity ratio amounted to 39.8 percent.

And now I will hand things back to Martin for the outlook.

**Martin Brudermüller****[Chart 16: Outlook 2020 for BASF Group]**

Ladies and Gentlemen,

As already announced on October 9, we now expect 2020 sales of 57 billion euros to 58 billion euros, mainly due to weaker demand because of the pandemic. We expect EBIT before special items of between 3.0 billion euros and 3.3 billion euros for 2020. As a result of the impairments in the third quarter of 2020, we anticipate a return on capital employed of between 0 percent and 1 percent.

For the fourth quarter of 2020, we expect a further improvement in EBIT before special items compared with the third quarter of 2020.

Our forecast assumes that severe restrictions on economic activity related to the pandemic, such as lockdowns, are not reintroduced.

As we have been asked several times, let me also touch on our dividend policy: BASF remains highly committed to its progressive dividend policy. We have based our dividend policy on BASF's midterm macroeconomic assumptions and the related earnings expectations. If the future macroeconomic environment reduces BASF's growth opportunities and significantly impacts BASF's profitability, we might have to adapt our dividend payout. However, I would like to make clear that we will only decide on this matter in February 2021 – based on our actual cash flow in 2020 and a more reliable medium-term forecast.

**[Chart 17: Measures to navigate BASF through the pandemic – well positioned to benefit from market recovery]**

Let me conclude with our measures to further navigate BASF safely through the pandemic and to mitigate its financial impacts.

With our customers in the center of all our activities, our corporate strategy is the right answer to successfully operate in this environment – even more so than before. We have significantly increased cooperation with many of our customers during the pandemic to immediately respond to changes in their demand patterns. Our teams now work hard to achieve profitable growth supported by strategic agreements with customers. In this context we are running our global production network with high flexibility, and we are well positioned to benefit from a market recovery.

We have a clear focus on further cost reduction and are fully on track to achieve the targeted earnings contribution from our Excellence Program. In addition, the realignment of BASF's Global Business Services unit will further support BASF's efficiency.

In these times, safeguarding cash is a top priority. In 2020, we will bring down capital expenditures by 600 million euros to 2.8 billion euros. Together with strict management of working capital, this will support a robust free cash flow, even in a year as difficult as 2020. Regarding our five-year capital expenditures budget, you can be sure that we will continue to strictly review our projects and focus our spending.

To support BASF's future profitable growth, we will continue to energetically pursue our investment project in Guangdong and our investments in the production of battery materials.

Let me conclude by saying that we are actively managing this crisis. Our diversified portfolio, a solid balance sheet, and a robust cash flow have proven to be strong assets in these times.

Ladies and gentlemen,

And now, we are happy to take your questions.