Conference Call Q1 2021
Transcript Q&A
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1 BASF Group

1.1 Q2 business environment

Christian Faitz (Kepler Cheuvreux): Will Q2 still see some skid marks from the Texas freeze? If so, can you give us an idea of the impact?

Dr. Hans-Ulrich Engel: Regarding the question on the outages and the impact of the freeze at the U.S. Gulf Coast.

Outages hit us, no question about that. But we were through the worst after about three to four weeks; so in the middle of March we were done, all of our plants were back up and running.

What we still see is that about 15 percent of the U.S. cracker capacity is out; chlorine plants of our competitors are still affected. There are still ongoing supply chain distortions, but at the BASF sites we were actually lucky compared to where our competitors are.

What we said in Q2 with respect to the expectation still stands. It's an impact in Q1 of upper double-digit million on EBIT. But that is it, and there shouldn't be any further impacts from the U.S. freeze in our Q2 earnings.

Christian Faitz (Kepler Cheuvreux): Would you see your sales into automotive being hampered in Q2 by the chronic semiconductor supply shortage in the automotive industry?

Dr. Martin Brudermüller: On semiconductors: I am certainly not a specialist, but you know that we sell some chemicals into this industry. I also tried to understand that by talking to a lot people in this industry.

Automotive production was up compared to the prior-year quarter. But it is also a little bit lower compared with the fourth quarter. There is, very obviously, if you follow the OEMs, some restriction in production volumes connected to semiconductors. It looks like, when the pandemic came last year, some of the tier suppliers have obviously given up some of their reservations for chips. These chips have now been taken or these capacities have now been taken over by others. I hear that China ordered a lot to get independent.

And what I also learned is that the automotive chips have lower margins than many other applications. So, also the producers now have dedicated their capacities to other, higher-margin production. And that means: It's most probably not so quickly coming back because they are sold out.

And that is also one of the reasons when we say "uncertainty" for the year. There are some indications that production in cars could come back in the second half. But it could also be that this whole semiconductor issue is a bit of a longer one that reaches into 2021. This is one of the question marks where we say, we do not know how production levels in the car industry will be in the second half.

It doesn't look like people have to really stop production now. But there is uncertainty and it is more a structural topic and it is a very strong demand in the semiconductor industry in various applications.

Thomas Wrigglesworth (Citi): Just to draw you a little further onto Q2, if we take out the Ag seasonality, looking at the rest of the chemicals upstream and downstream business, where is the reason to be thinking that actually the run-rate profitability seen in Q1 will not persist into Q2?

Dr. Hans-Ulrich Engel: You already alluded to a seasonality that we have in the business. If we leave this aside and based on what we are currently seeing in our order books, the expectation is that the momentum that we had in Q1 carries on in Q2. Looking at the daily sales also that we have in the month of April, they continue to be strong. So the expectation is that we will see a very solid Q2, obviously much, much stronger than the extremely weak Q2 of last year.

Gunther Zechmann (Bernstein): If you could just comment on stocking levels across the value chain, please, particularly in China, with the strong volume growth you have seen in Q1.

Dr. Hans-Ulrich Engel: As always, we can try to assess, but we don't have really firm data. But if you see what happened in Q4 around the globe, a significant pickup in demand. If you think about the fact that China has in our business a double-digit volume growth since April of last year, month after month, it looks to us like the inventory levels across the various chains at our customers continue to be relatively low.

End consumer demand is so strong, obviously also fueled by a number of stimulus packages, that there is just no time to rebuild inventories. Inventories, in particular end of Q2 around the globe, but in China end of Q1, were very, very low. I think this is exactly what we're seeing. To a certain extent, this reminds me of the situation that we had in the second half of 2009 and then going into 2010.

There's another reason for us to believe that inventory levels continue to be on what I would call a moderate level, and that is the significant increase, in the meantime, in prices. These are situations where customers tend to be careful with putting in their orders and with buying. So actually, I would think, overall that's good news also for the remainder of the year.

Laurent Favre (Exane BNP Paribas): You've alluded to the margin squeeze downstream in Performance Chemicals, Nutrition & Care, maybe Coatings as well. All your peers are thinking that there will be more pressure in Q2/Q3 than in Q1. I guess you've got the Verbund integration which is not helping. Should we expect more margin squeeze in Q2 and Q3?

Dr. Hans-Ulrich Engel: On margin squeeze in downstreams and what's going to happen there in Q2? The situation that we have is: In Q1 compared to Q4 of last year, our raw material portfolio shows a price increase of 14 percent. We are in a situation where the downstream businesses, as a result of the demand, have pricing power. But whether or not they will be able to fully pass on the kind of raw material price increases that we've seen in Q1 remains to be seen.

As a result, yes, there is a risk for further margin squeeze that we need to factor in. At the same point in time, our businesses have clearly understood the message that they got, and they need to go for further price increases.

Robert Hales (Morningstar): Just a very quick one on raw material inflation: I'm just wondering, can you quantify your inflation expectations for the year and maybe versus last quarter?

Dr. Hans-Ulrich Engel: On the raw material side, we have a price increase of 14 percent in Q1 compared to Q4. We are expecting a further price increase, but on a more moderate level than in Q2, and overall, most probably raw material prices peaking in Q2. This is, I want to say, highly speculative.

Q1, as I said, 14 percent, going into Q2 further raw material price increases, but on a more moderate level.

1.2 Outlook 2021

Gunther Zechmann (Bernstein): On the outlook for the year: You increased the sales outlook by €7 billion, but you kept the CO_2 emission target flat. The Accelerator sales target goes up by €1 billion. So what's the message here? That your Accelerator products are seven times more ESG-friendly or that that increase in guidance is mainly driven by pricing rather than volume? Or a combination of the two?

Dr. Martin Brudermüller: It is certainly a combination of all the effects. There is a strong price push which increases our sales, and which then also carries onto margins. We think this is also going on in Q2 and further into the year.

You are right: CO_2, that was a very clear commitment that we keep that on the level of 2018. So we also progress on all the measures we have here, that is both on buying in green energy from outside and we have concluded some contracts in the U.S., for example. We have also intensified our opex measures. You know that, by a wide range of measures, we also collect every year a quite significant share just to bring down our CO_2 over here. So that is roughly how we overall, with all the measures, get it in line. And that is a very clear target.

You know that this is also related to the LTI program. All the people are very eager to not release more CO_2 than on the level of 2018. But it is a stretch.

Anthony Jones (Redburn): A question on the guidance from a different angle: You've guided for sales of about €6 billion above consensus, but the midpoint on EBIT is broadly in line. Earlier in the call, you've already been calling out a very strong Q2, at least at the start, good pricing, margin trends. Do you expect something else to go wrong or something we don't see? Or does this also include a much bigger STI/LTI accrual than we normally would expect?

Dr. Martin Brudermüller: As I mentioned, in my speech: Overall, we are positive. And this was also what we, I think, radiated when we gave the guidance in February. We moved the span a little bit higher because of what I told you. Q1 was great and Q2, so far, is running on a very, very high level. We will certainly have a strong base effect from last year.

But I think there are also some question marks in what's going on. So, first of all, is the vaccination campaign all over the world going in the direction that people return to normal life? Then there is also the question: With people in the lockdown today, is there advanced sales, so that they consume certain things, that they buy now, goods which they use in the house? Then later, in the second half, when they have, their freedom to move again, they might spend more of their discretionary earnings or disposable income on leisure, on traveling, on entertainment, maybe investing less in goods. I told you about the semiconductors in the car industry.

We are not negative about that. But we also say, it could be that one or the other thing is retarding and taking a little bit away from the dynamics in the second half. This is why we have the span like it is.

But, I think, as we told you in February: We are expecting – base assumption – that we are at the higher end of the span. This is also true for what we will tell you today: that we are positive about what we are seeing going forward. But there is still uncertainty out there. We should not be carried away now by this very dynamic environment, that everything with this pandemic is done. That is the reason we have these little bit wider numbers out there. But you see that we are positive and at the moment can only tell you: The strong business is carrying on also in Q2.

Matthew Yates (Bank of America): Can you say anything about your maintenance plans in Ludwigshafen this year and how we perhaps need to factor that into our forecast over the coming quarters?

Dr. Martin Brudermüller: There is not very much I can tell you. First of all, this is nothing you basically switch on and off. If you want to have your assets in shape and with reliability, you also have to invest. Certainly, the factories are a little bit older and some of the Ludwigshafen plants are older and depreciated. So you have to spend a little bit more, but you have to do that continuously. So there's nothing spectacular. But as you know, we keep our hands on cost. That means we certainly look that there is only stuff done that is reasonable and is needed.

We also connect that to the opex push we have. We are very much pushing on opex. That's always a super opportunity to get relatively cheap smaller debottlenecks. Specifically, they are very interesting and attractive. You can partially combine that also with EHS and maintenance needs. So, I think, with this we are in an ordinary, normal year.

Maybe one remark here on the turnarounds: They are on the plant side slightly lower than last year, also nothing spectacular here. Some of the plants in Ludwigshafen will also go into turnaround. That is the season coming up now, which is always towards the summer. So I would say, a relatively ordinary, normal year in terms of maintenance spending.

Laurent Favre (Exane BNP Paribas): Phrasing a question that has been asked a lot, but a bit differently. When you look at the H1 comments you have just made, even at the top end of your new full-year range, you seem to be assuming quite a bit of normalization in the second half in the upstream. I was wondering, in-between TDI, MDI, crackers, polyamides, where do you see the risk of a sharper normalization and where do you see actually the strong demand, maybe carrying the strong numbers for a bit longer in terms of product chain as opposed to end markets?

Dr. Martin Brudermüller: A very strong and good, favorable environment for most of the commodity lines, that is carried by the strong demand, first of all, but also supply/demand; we talked about the freeze, but also the one or the other problem in production lines over there.

This is always something where you cannot expect that it is staying like this forever; it can very quickly change, first of all, when it's easing on the supply situation.

But then also if there would be negative parts coming in Q2, which is not our base assumption, but if the demand would lose a little bit of dynamic and the supply is really good, then you know how quickly some of the margins react.

If you look at acrylic acid today, or MDI, BDO: Currently, in China, very good and high pricing, also good margins, those went up very, very quickly. But these could also in the same way quickly come down. Now to make a pledge for an assumption here how many months this will carry on is simply very difficult.

But all the indications we have, and we intensively talk with the businesses and the customers to get an outlook: So far, it is stable. That's why we said, Q2 will be stable. I think also, it's carrying on, but I doubt that this is the basic assumption for the rest of the year. Hans mentioned ethylene prices. Are these now the new normal for the rest of the year? I am not so sure. I think we should take what we get here, but also not think that this is now carrying on forever.

Markus Mayer (Baader Bank): On the outlook: If I remember correctly, in the full-year conference call you said you have baked in a security buffer for potential logistical and supply issues in the guidance. Now I have not heard anything about that. So I guess this buffer is completely out of the guidance or is there still a small buffer included in the guidance?

Dr. Martin Brudermüller: We don't expect anything on the supply chain which is significant here. I would leave it at that.

1.3 Corporate topics (incl. Other)

Thomas Wrigglesworth (Citi): Obviously, the excellence program is coming to its last year. What in these results do you pull from this about the success of that program? How do you see that influence in the set of results?

Dr. Martin Brudermüller: Just a few remarks on the excellence program in general: First of all, we delivered on our target at the end of last year. The composition of components was a little bit different for one or the other reason. We pushed more on cost reduction during the pandemic. From others, e.g., from opex, we got a little bit less. But we are on track.

Believe me, Hans and myself, we keep the pressure on the organization that now we are not carried away by growth and by nice margins and do not look at the cost. We want to clearly deliver the €2 billion at the very end of the year. You know that that has also to do with the reduction of people. We told you, we are a little bit delayed here because certainly in times when the economy is not so nice, people don't sign contracts to leave. But the rough number I can give you: At the end of the first quarter, about 5,750 of the 6,000 left. So I think we are very well on track here.

And also in terms of one-time cost, I think we are totally in line with what we said, that this might cost €100 million to €150 million this year.

Peter Clark (Société Générale): Around the cash flow and the capex. I presume Covid is impacting the capex spend in Q1, which was down year-on-year. I think you gave guidance for €3.6 billion or so for the full year. I'm assuming this is going to step up quite sharply as we move through the year and potentially beyond that with the target you gave for the five years. So it's just on the capex and the cash flow implications around that.

Dr. Hans-Ulrich Engel: Compared to the €3.6 billion that we have in the budget for capex, Q1 is very low. That is not out of the ordinary. We typically see spending ramping up. It also depends on the time that the invoices are sent for the work that is done. We'll see capex increase during the course of this year, no question about it. But that's clearly factored in.

You were asking the question with a look on cash flow. I think that the following is important to keep in mind: Number one, we have a seasonally extremely strong business in Q1. This is a key season for our Agricultural Solutions business. We have a significant increase in our accounts receivable in addition to that, due to the general pickup of the business. All of that needed to be digested in the Q1 cash flow.

Nevertheless, our operating cash flow is €500 million stronger than in Q1 of last year, and our free cash flow is €600 million stronger than in Q1 of last year. What you also want to keep in mind is that with this seasonally very strong Q1, most probably on the accounts receivable side, we are seeing a peak at the end of Q1. So depending on how the rest of the year will go, whether prices will go up significantly etc., I'd say most probably there is a bit of a cushion in our cash flow as a result of this very strong business that we have in Q1.

Sebastian Bray (Berenberg): Firstly, is there a rule of thumb for tracking the percentage increase or decrease in BASF share price and somehow translating this into another number for the Other segment? The share price is up about 10 percent over Q1. The Other segment had a result which is, by and large, about €300 million more negative than consensus was expecting. Is this something that can be used as a rule of thumb? And secondly, could you just remind us of the activities located in this business aside from corporate and commodity trading?

Dr. Hans-Ulrich Engel: First of all, we've tried many, many times, also for our own forecasting purposes, to come up with a meaningful formula on the Long-Term Incentive Program, on the provisions that we have there and how they will develop depending on the share price. We weren't able to come up with anything. And the reason is: There is a relative component in there. There's an absolute component in there. With the relative component, it's always the question: How does our share price and share price development compare to the indices? And as a result of that, unfortunately, even though I tried many times, we didn't come up with anything that is meaningful. So sorry, I can't help there.

In Other, we have a number of things, what I call a hodgepodge of various businesses. They range from our raw material trading business to services that we are providing. These services range from maintenance services that we are providing to third parties. We have rent in there, so tons of what I would call smaller things.

The main driver actually on the sales side is the raw material trading. That represents roughly 60 percent of the sales in Other.

2 Segments

2.1 Chemicals

Jaideep Pandya (Onfield Research): If we go back to 2019 and compare current volume levels to 2019, it seems like volumes are up maybe 4 to 5 percent. But product spreads upstream are up more like 25, 30, in certain cases even 50 percent. Would you say that this trend in the spreads that you're seeing currently is pretty much all outage-related and Texas-related? Or is there something fundamental here, you know, with China not performing as well as it used to back in the day?

Dr. Hans-Ulrich Engel: With respect to your 2019 and 2021 comparison in Q1, where do we stand when we look at in particular upstream? It was quite amazing to see after the steep fall that we had in basically all commodities and then at the trough point some time at the end of Q2, the type of increase that we've seen from there and the level of margins that we reached. If I think about our key commodities, we are currently in an environment that is very similar to where we were end of 2017, early 2018.

We think that the key driver for that is really the strong demand. Yes, outages, problems such as the U.S. freeze are certainly playing a role. And if you think about the fact that ethylene prices in the U.S. are higher than ethylene prices in Asia, that's something that we haven't seen for years. And, yes, 70 to 75 percent of U.S. cracker capacity being out for, let's say, roughly a month, as I mentioned earlier, today still 10 to 15 percent of cracker capacity being out, the same being true for some other commodities, such as, for example, also the isocyanates, then that is contributing. But we think that the underlying very strong demand is the key driver.

2.2 Materials

– no specific questions –

2.3 Industrial Solutions

– no specific questions –

2.4 Surface Technologies

Georgina Iwamoto (Goldman Sachs): On Catalysts: It looks like in recent years the volumes there are actually outgrowing auto production a bit faster than we've seen historically. I was just wondering if maybe you could comment on why that might be the case and if it's something that you'd expect to continue at a similar rate.

Dr. Hans-Ulrich Engel: Automotive catalyst business: actually a very good development since end of Q3, early Q4, in particular in our Asian business, driven there by China 6.

Yes, I can confirm your observation: The growth rates that we have in the automotive catalyst business are stronger than the production growth in automotive which, I think, is a very good message. But then hearing what competitors say with respect to their respective business, I always come to the same conclusion: This market must have more than 100 percent.

2.5 Nutrition & Care

Matthew Yates (Bank of America): Can you just elaborate a little bit more on the Nutrition division? To what extent, in some of the areas you've highlighted as having lower prices or lower production, is it just quarterly issues and not necessarily telling us anything about demand to be extrapolated?

Dr. Hans-Ulrich Engel: What do we see in Nutrition & Health? Yes, compared to the very strong Q1 that we had in 2020 where we mentioned that, towards the end of the quarter, we saw some pre-buying going on, the results in Nutrition are weaker.

There are a number of factors in addition to this, what I call the comp problem that we have when we compare the quarters: We have the cost of bringing the vitamin A plant in Ludwigshafen on stream. That will start up around the middle of the year. That's my expectation based on everything that I see.

We have a bit of a technical issue with certain grades of vitamins at this point in time. That's also reflected in our pricing.

And then there's an element that benefits upstream and that's very typical for situations like this. Upstream is showing very strong results due to strong demand. And what you see then in the beginning is some margin pressure in our downstream segments. And that's hitting the Nutrition & Care segment because, while upstream you price more or less on the basis of the spot raw material prices, downstream you price with formula pricing, averages of raw material prices over a certain period of time. There is a certain time lag and that then typically in these kind of situations results in some margin pressure.

I think these are the reasons for the decline in earnings that we had in Nutrition & Care in the first quarter of this year.

2.6 Agricultural Solutions

Andrew Stott (UBS): If you look at Q1, the balance between price and currency was minus 6. Obviously, I get the fact that quite a lot of your competitors are dollar-based, so that doesn't really help you. But the simple question: Do you think you can improve upon that balance as you go through this year? In other words, currencies in any case, I guess, will naturally get a bit better for you. But do you think you can push on pricing in crop protection through the year?

Dr. Hans-Ulrich Engel: Let's not forget about the 7 percent volume increase that we had in the business. And yes, you're right, prices are at 2 percent, which have to do a little bit with mix.

Currency: As a company that reports in euros, that works against us. This is a strong business in Q1 in the U.S., where in Q1 of last year, the U.S. dollar to the euro was at 1.10. Now it's around 1.20. It remains to be seen what's happening on the currency side.

There's certainly an environment there, with soft commodity prices that have increased significantly, that supports a good, strong business. And also, in light of what we're seeing on the raw material side, it's a clear target for Agricultural Solutions to also bring prices up.

Jaideep Pandya (Onfield Research): If you look at the mix in Q1 with very strong fungicides and canola coming back, how much of FX headwind did you have on EBIT? I'm just trying to understand: Excluding the FX, would EBIT have been significantly better year-on-year?

Dr. Hans-Ulrich Engel: Yes, EBIT would have been significantly stronger in Q1 without the FX impact. I don't have the exact figure for you, but if I recall that correctly, FX on a top-line level is minus 8 percent in Agricultural Solutions. So you can imagine what that does overall then also on the earnings level.

Andreas Heine (Stifel): In Agricultural Solutions, I was expecting the volume to be not as strong as it really was due to the weather. In North America and in Europe, it was quite cold for much longer than last year. Have you seen any of this impact or was weather not an issue at all in the first quarter? Which basically translates to Q2: Last year was very strong in Q1, less so in Q2. I would expect it the other way around this year. But given the volume you have posted in Q1, I'm not sure whether this is right.

Dr. Hans-Ulrich Engel: A good, strong business, as you are pointing out, with 7 percent volume increase. Order book for Q2 in the Agricultural Solutions business looks very good, in particular on the fungicides, where last year, as a result of the drought in Europe, we saw a relatively weak business. It had a very good start and continues to look good.

What may also play a role here are the much stronger soft commodity prices. There is higher interest in more yield. And that typically then leads to a situation where the farmers are willing to also spend more for the input because their expectation is that for their output it will clearly be beneficial.

So that's what I can say at this point in time. But weather is always a factor. Let's see what's going to happen now during the season. It's too early to tell, but in any case, we have a strong, very strong, from my point of view, Q1 in the back.

Chetan Udeshi (J.P. Morgan): We all know about the seasonality in Ag, which typically comes down in Q2 in terms of earnings versus Q1. Looking at the current trends which, as you said, are strong, maybe you could shed some light on how the LTI provision will proceed through the year, is it possible that Q2 may be similar to Q1 in terms of EBIT, or is that too optimistic an assumption?

Dr. Hans-Ulrich Engel: That is probably too optimistic. We also have seasonality differences between Q1 and Q2, which is driven by the fact that the seeds business for the row crops has its clear strength in Q1 and not in Q2. And I think we'll see this reflected in this year.