Transcript
Q4/FY 2021 Earnings Call

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PRESENTATION

Operator

Ladies and Gentlemen, thank you for standing by. Welcome to the Covestro Earnings Call on the fourth quarter and full year 2021 results. The company is represented by Markus Steilemann, CEO, Thomas Toepfer, CFO, and Ronald Koehler, Investor Relations. [Operator Instructions] I would now like to turn the conference over to Ronald Köhler. Please, go ahead, Sir.

Ronald Köhler

Yes. Good afternoon to all European participants and good morning to all Americans. I'm happy that you're joining our full year 2021 conference call and I know it's a busy day and it might be one of several conference calls that you have; therefore, I'm even more happy that you are here. We have posted the annual report and earnings call presentation at our IR website and if you haven't seen it, you can always download it. And there, you will also find our Safe Harbour statement and I assume you have read it. And with that, I turn it over to Markus.

Markus Steilemann

Thanks a lot, Ronald, and a very good afternoon and/or good morning to everybody on the call. In the full year 2021, our earnings performance was well above previous year level as the 2020 results - as you are well aware - were heavily impacted by the coronavirus pandemic. The demand rebound resulted in a 10% core volume growth in last year and earnings remained on a high level throughout the entire year 2021. We delivered € 3.1 billion EBITDA and a free operating cashflow of € 1.4 billion. I think that qualifies 2021 as a strong financial year for Covestro. We want our shareholders to participate in our financial success and, therefore, we announced a new share buyback programme of € 500 million over the next two years. We also continue our ambition to pay out an attractive dividend and propose a dividend of €3.40 per share. How do our 2021 results compare to our past promises? Let's turn to the next page.

We achieved all our financial targets set for the year 2021. As I said, core volume growth of 10% included the volumes from the acquired RFM business and came in at the lower end of the guided range. We also saw strong demand and also limited product availability accompanied us and our customers throughout the year. Free operating cashflow of exactly € 1 billion 429 million came in at the lower end of the latest guided range yet above the upper end of the initial range. While earnings and cashflow outlook improved during the course of the year, cash was increasingly absorbed by working capital reflecting the outstanding price inflation, especially during the second half. We generated € 3 billion 85 million of EBITDA and 19.5% return on capital employed, well above our initial guidance and close to the centre of the latest guidance corridors. While delivering on target on the financial side, I am excited to announce today new targets on the non-financial, climate related side. Covestro has a tradition and a track record of pioneering sustainability in the polymer industry. I am convinced, shareholders of Covestro will also in future benefit from both leadership in sustainability and profitable growth. Let's take a look at our new targets in more detail.

Covestro aims for climate neutrality and has set for itself bold and ambitious targets: Net zero for scope one and scope two greenhouse gas emissions by 2035. This target is another major milestone toward our corporate vision of becoming fully circular. As a key milestone, we plan to cut greenhouse gas emissions from our own production, referred to as scope one, and from external energy sources, referred to as scope two, by 60%, by 2030. A key aspect for our 2035 reduction target is meeting the goal of the Paris Climate Agreement under which the world community aims to limit global warming to 1.5° C. Sustainability and, more specifically, climate related targets are not new to Covestro. As a matter of fact, in 2021, we achieved our previous specific greenhouse gas emission reduction target for 2025 ahead of time. We more than halved specific emissions, again scope one and scope two compared to the base year 2005, while production volume doubled. As a consequence, Covestro has achieved climate neutral growth since 2005. Reducing our own emissions, however, will not be the end. We plan to further reduce indirect greenhouse gas emissions from upstream and downstream processes in the value chain, referred to as scope three. This part of the transformation will be largely linked to our transition to a circular economy.

More importantly, we strongly believe that transition opportunities will outweigh transition costs. We aim to shift all our production processes and products completely to circular principles in the long term and we intend to support meeting our and customers' climate objectives at the same time. Covestro is continuously expanding its portfolio of climate neutral products as customers, already today, demand sustainable products and, we believe, are also willing to pay for the added value. This is vital to align our transitions to net zero emissions with profitable growth prospects. To achieve net zero emissions, Covestro anticipates dedicated investments of accumulated €250 million to €600 million by 2030. These investments will tackle our direct greenhouse gas emissions, but also increase our overall energy efficiency. This is expected to result in lower operating expenses of between €50 and €100 million annually during the same time. We currently also expect an increase in operating expenses in a magnitude of a low three-digit million Euro amount annually. These cost assumptions base on the historic circumstance that prices for fossil-derived energies are lower than prices for renewable energies. The upside here is that this historic price order is being turned around as it can be observed in many places today.

If you now turn to the next page, we have identified three main levers that make a vital contribution to achieving our climate targets: more sustainable manufacturing, renewable electricity and renewable steam. The waterfall graph on the chart shows our detailed path and expected contribution of each of the measures to reach our interim target of 60% emission reductions in 2030 and 100% reduction in 2035. It is needless to say that business growth without any climate related measures leads to higher emissions; in our case +1 million metric tons until 2030. Thereafter, we expect no negative impact on emissions from business growth as future growth investments are required to support climate neutral growth from 2030 onwards. Also, there are external factors that influence our scope 1 and scope 2 emissions. These factors comprise the energy mix of public grids, for example the announced nuclear exit in Germany and Belgium, as well as public energy allocation schemes, for example determined by the German renewable energies law, short EEG. The net effect of all changes as known today amounts to minus 0.7 million metric tons. To look at the identified lighthouse projects from the area of manufacturing excellence and renewable energy, let's turn to the next page number 7.

We have identified numerous measures to effectively reduce our greenhouse gas emissions. In the area of more sustainable manufacturing, production processes will be further improved and energy efficiency enhanced. One focus is to reduce nitrous oxide emissions by installing highly efficient catalysts. Secondly, in the area of renewable electricity, our production sites worldwide will be gradually converted from fossil based to renewable electricity. We have already entered a number of power purchase agreements for renewable energy and further agreements are being planned. Thirdly, steam is an important energy source for chemical production processes. Converting steam generation from fossil to renewable energy sources is a challenge that Covestro intends to solve by various routes. Those routes are ranging from electrifying steam generation based on renewable energies to using biogas or green hydrogen as an energy source for steam generation. In a nutshell, we are very excited to have set ourselves this bold emission targets and have worked relentlessly out our road map towards climate neutrality. Covestro continues as a pioneer toward a circular economy and to successfully deliver both leadership in sustainability and profitable growth. With this, I would like to hand over to Thomas for the financial review.

Thomas Toepfer

Yes, thank you, Markus and also a very warm welcome from my side to our call. So, if you go to page 8 of the presentation, you can see our core volume growth of 10% in the financial year 2021 and that reflects the volume rebound and consolidation of RFM. Just to remind you, RFM contributed 6 percentage points, but I would also like to remind you that at the same time we were constrained by product availability. And you can see the volume development by our key industries in the box on the righthand-side in the order of kilotons sold. So, first of all, wood and furniture came in at -4%. We saw solid demand, however, we were constrained in terms of TDI and polyols availability. Construction, we came in at +1%, again solid demand, however, constrained MDI and polycarbonate availability. And number three, the auto and transportation industry +10%, so very strong year-on-year growth globally. And I would like to remind you that the global auto industry grew by only 2% year-on-year. So, we outgrew the industry by 8 percentage points and that, for me, is another indication that we are delivering to the high-growth part of that industry, specifically electric vehicles. Last but not least, electro came in at +9 % with growth in all regions and I would like to remind you that all industries are excluding RFM and the RFM business is fully consolidated in diverse and this is why you find the +33% in the box on the right-hand side of the page.

So with that, let's turn to page 9 of the presentation where you have the sales bridge. You can see full year sales increased by 48.5% pushed by 35% higher prices. That is the 3.7 billion that you see in the bridge. And it's just another proof point that Covestro successfully passed through the unprecedented inflation of raw material prices to our customers. The net volume effect in sales and that excludes RFM was 6.5% year-on-year mainly driven by Solutions and Specialties as this segment compared itself to a relatively weak prior year. The volume growth, especially in Performance Materials, was limited by constrained product availability as I mentioned earlier. FX is only a small negative number with -0.8% mainly driven by the weak US dollar and I would like to draw your attention to the portfolio bucket which is the €863 million that is essentially the entire sales of RFM which have been consolidated as of April 1st. And that's an 8.1% effect for the full year, if you put it to the Covestro numbers.

So with that, let us turn to the EBITDA bridge on page 10, you can see that the full year EBITDA doubled compared to prior year driven by the highly positive pricing delta. That is the €1,866 million and the vast majority of that was contributed by all key product groups within Performance Materials. However, also the volume effect in EBITDA contributed positively with an attractive volume leverage of 49% and FX was virtually neutral on a year-on-year basis. So I would just like to comment on the other items bucket which includes, essentially, three main effects. First of all, there is a negative €443 million in there and that is the impact from the higher bonus provisions for variable compensation. Secondly, there is a negative €60 million one-time effect, which is related to the acquired RFM business and that compares to a negative €33 million in 2020 and number 3 there's a negative €39 million one-time effect included in that bucket which is related to the LEAP transformation program and we had no such effect in 2020.

So with that, let us go to page 11 which shows you the free operating cashflow and as Markus said earlier, we generated a free operating cashflow of €1.4 billion which is a strong number, well above the previous year and we achieved this despite the significant higher working capital. You can see in the bullets on the righthand side that in Q4, the free operating cashflow was somewhat below previous year as the positive contributions for working capital and the higher earnings were eaten up by significantly higher income taxes paid and also higher capex. And talking about working capital, that ratio in terms of working capital to sales ratio stood at 18.6%, so it's just slightly above the 18.2% that we had a year earlier. Again, that reflects higher feedstock and also product prices which push up the Euro values, especially of our inventories. You can also see in the table below the graph that we spent €764 million on capex so slightly below the budget number of €800 million. That is due to two effects: one is that some projects were shifted into 2022, but also some projects came in at a lower spend than we had expected so that is a positive news in terms of capex. And you can also see that year-on-year, we spent a much higher number on income tax paid, but that reflects our cash tax rate of 25%, absolutely within the guidance range and also below the P&L tax rate of 29.5%. My last comment is the last item in the little table, the other effects. That, of course, reflects the higher provisions for variable compensation because the cash out for the bonus will only occur in the second quarter of 2022.

So with that, let us turn to the balance sheet on page 12. I can truly make the statement that our balance sheet remains strong. Our pension provisions decreased by €924 million. That is partly due to the higher discount rate, specifically in Germany. But the other reason is that we transferred €500 million of funds in one of our pension trusts and the effect you can see, essentially, shown twice in the bridge: One time on the financial debt side and the other time on the pension provision reduction side. In terms of the balance sheet ratios, you can see that the ratios are strong. So the ratio of total net debt to EBITDA stands at 0.8 times at the year end of 2021 versus 1.7 times a year before. And essentially, you can also see that after €1.5 billion cash outflow for RFM and the 0.5 billion Eurobond repayment and also the €0.5 billion fund transfer, we still have €1.1 billion available in cash, cash equivalents and also current financial assets. So with that, I would like to hand it back to Markus for the segment review.

Markus Steilemann
Yes, thanks a lot Thomas and please allow me to begin with the full year review of our Performance Materials segment: the segment delivered a highly positive pricing delta in 2021. We were able to pass through increasingly higher feedstock as well as energy prices and – on top – expanded our margin. First and foremost, this performance was based on solid underlying demand. However, simultaneously, our growth potential was limited by a continued constrained product availability. Looking forward into full year 2022: We expect our sales volumes to grow strongly based on improving product availability. At the same time, we expect the segment EBITDA to significantly decrease year-on-year due to intensified competition, mainly in standard polycarbonates. I will talk a bit more about polycarbonates in a short moment. Positively, we anticipate that the supply-demand balance for our product groups MDI and TDI will further improve as announced supply additions are below expected demand growth. Let's turn to the next page.

Turning to Solutions & Specialties: we defended absolute EBITDA and managed earnings to remain virtually unchanged year-on-year, despite unprecedented inflation. Positively, the segment recorded strong sales volume growth of 12% year-on-year, reflecting a rebound in demand from a pandemic-impacted prior year. The acquired RFM business, consolidated since April 2021, also contributed positively. EBITDA margin, however, was down year-on-year by nearly 5 percentage points. This is due to mainly three reasons: Significantly higher price-driven sales comparing to unchanged absolute EBITDA, resulting in a mathematically lower margin. Earnings significantly burdened by higher feedstock prices and longer-term sales contracts yet prevented to fully pass through prices, reflecting the typical nature of a specialty business. Looking forward into 2022: We expect sales volumes to continue strong growth versus 2021. We also expect segment EBITDA to significantly increase year-on-year. How we anticipate reaching our segment margin target of 17% is what I will present to you on the next page.

I just presented the unsatisfactory 2021 margin of 9.9% as a reference point to the target of a segment EBITDA margin of 17% in 2024. In order to reach 17 %, our EBITDA margin will be driven by the four key elements that are shown in light orange on the chart: Firstly, continued execution of our LEAP transformation and cost containment program as well as continued strong growth are expected to further dilute fixed cost. Secondly, we are going to further progress with the RFM integration and realize the anticipated synergies. Thirdly, we will focus on value-based pricing, especially for newly launched, innovative products. Lastly, the margin target is based on mid-cycle inter-segment charges by Performance Materials, therefore are anticipated to be lower than in 2021. In 2022, as already mentioned, we expect a significant increase in EBITDA. On the following two charts I am going to share some further details on our targeted path of margin improvement, beginning with RFM. So, let's turn to the next page. Regarding the integration of the acquired RFM business: all planned synergies are fully confirmed and realization is ahead of plan. As a recap: at the time of acquisition, we identified a total EBITDA contribution from synergies of €120 million or about 12% of RFM full year sales, thereof €80 million synergies from lower cost and €40 million from additional revenues. We could pull forward the realization of synergies and delivered €26 million in 2021 compared to originally expected €10 million in the same year. We achieved this above-plan realization at €6 million lower cost compared to earlier planning and we now expect total implementation cost of €115 million, €40 million less than originally expected. The main reason is lower than expected severance needs. In a nutshell, the integration of the acquired RFM business – about one and a half years after the announcement – is a success and we are absolutely satisfied with the delivered results. Let's now turn to the next page: polycarbonates.

As a second deep-dive, let me elaborate a little bit more on our polycarbonates strategy. Overall, we continue the strategic portfolio shift from standard polycarbonates to differentiated polycarbonates. I, myself, accelerated this shift from 2013 onwards when I headed the former business unit Polycarbonates. The graph on the left side shows the development of the volume split: while the grey bars continuously shrinks, depicting the standard polycarbonates business within our Performance Materials segment, the light pink bars continuously rises, depicting the differentiated polycarbonates business. Refining standard polycarbonate resins, produced at our fully integrated, large-scale and cost-driven plants within Performance Materials into differentiated grades – that is the job of the Business Entity Engineering Plastics within the Solutions & Specialties segment. In order to allow this shift, we are continuously investing in downstream capacity referred to as 'polycarbonate compounding'. Between 2020 and 2025, we will add 230,000 tons of additional compounding capacity. Importantly to note is this addition is neutral to the overall industry supply demand balance. Yet it exclusively allows Covestro to cater even more for the attractive, differentiated customer segments of this industry. This portfolio shift is supported by the expected 7% industry demand CAGR for engineering plastics across several customer industries. A detailed list of growth drivers is shown on the right side of this chart. With that, allow me to turn to the next page.

Looking ahead into 2022, we expect solid demand recovery to continue globally. This applies to the products we just talked about in more detail, but also to our entire product portfolio. The figures on this chart show full year demand estimates for our key industries and respective important sub-industries. The expected 2022 demand growth in global automotive and global construction shows growth estimates above the full year 2021 values. The recovery in those industries is expected to continue after the strong demand hit by the corona virus pandemic in 2020. The expected 2022 demand growth in global furniture and global electro, in contrast, show values below full year 2021 but on continuously attractive levels. Key reason is the strong demand recovery seen in these industries already last year. Now, I would like to hand over to Thomas.

Thomas Toepfer

Yes, thank you. I'm on page 19 of the presentation where we talk about our fixed cost development. Remember: last year we committed to keep our fixed costs unchanged until 2023 relative to the 2020 level. It's fair to say that we qualified this target as being challenging from the beginning. Now, if you look at the chart you can see that in the financial year 2021, the cost development was in line with the expectation and our guidance, so we saw a rebound from the 2020 level which at the time was marked by the lockdown and the short-term cost savings. And the rebound was absolutely in line with our guidance and expectations, as I said. So also in 2022 and 2023, we do continue to execute cost reductions of between € 50 and €100 million per year through the LEAP program and I can tell you that all the costs that we can control are on track. However, what we also see now, of course, is that there are counter-effects resulting from high inflation, for example logistics and labour costs, and also potential projects that we will decide like the MDI project. Last but not least, also the new climate related investments that are necessary in order to reduce our greenhouse gas emissions as Markus just elaborated on. So, as the graph indicates, with that, we will have to face some counter-effects in the years 2022/2023, but we remain fully committed to tightly manage our fixed costs. Just one example of that counter-effect, you find on page 20, because this just shows the unprecedented challenge with the global energy costs more than doubling within two years. So as you can see, the global energy costs are significantly increasing in 2021, mainly driven by the European energy prices. And you can see this in the blue columns in the upper part of the chart. So global energy costs for Covestro in 2021 were €1.0 billion and thereof €0.6 billion were driven by electricity and €0.4 billion were driven by natural gas. And if you break that down on a region by region basis, I can tell you that 70% of that is in the EU, 20% is in Asia and 10% is in the United States. So the lower part of the chart depicts per some key countries the specific price development for electricity and natural gas. As you can see, first of all the significant increases, but also the regional differences, so that based on our actual breakdown, our global energy bill in 2022 is expected to be at €1.5 billion and again you see this in the light blue bar on the upper half of the chart.

So if you put it all together and you go to page 21, we are expecting an EBITDA in 2022 again above the mid-cycle earnings level. The market-to-market estimate stands at about €3.3 billion based on the January data and that is above the upper end of our EBITDA guidance corridor. And that EBITDA guidance is €2.5 to €3.0 billion reflecting expectations of an increasing competitive pressure during the course of 2022. I would also like to say that the mid-cycle EBITDA level, we now see it at €2.5 billion after a step-up compared to 2021, which is attributable to the RFM acquisition, should increase to €2.8 billion until 2024 driven by the business growth and also the realisation of the RFM synergies. What I would also say is that, based on the industry's supply and demand forecast that we see for the next years, the EBITDA is expected to remain above the mid-cycle levels for the next years.

And with that, I would like to come to the concrete outlook for 2022 on page 22. As you can see, it contains two new KPIs. So first of all, EBITDA is replacing core volume growth and that reflects our ongoing shift away from volume growth towards value driven growth. Secondly, there is an ESG KPI measuring the greenhouse gas emissions measured in metric million tons for absolute CO2 equivalents in scope one and two. The free operating cashflow outlook is in line with our EBITDA outlook as I explained a minute ago and the number stands at €1.0 – 1.5 billion and in terms of ROCE above WACC, the outlook is that we have a WACC of 7 percentage points in 2022 after 6.6% in 2021, and we expect an over-achievement, so a ROCE over WACC between 5 and 9 percentage points. Greenhouse gas emissions we expect between 5.6 million and 6.1 million metric tons. The increase is mainly attributable firstly to the composition of the externally procured power which is less favourable for us and secondly, to the growth of the business. And last, but not least, I would like to mention our guidance for the EBITDA in Q1. We are expecting between €750 and €850 million. And even with the lower end of this guidance range, we would be above the previous year level of €743 million.

So, let's turn to the next page, which shows our capex development. So unchanged and with the highest priority is the investment into profitable organic growth, because we do think that we are delivering attractive returns based on our industry and cost leadership. So, for 2022, we have an expected total planned capex of €1 billion and that includes €0.6 billion expansion capex and €400 million of maintenance capex and this planned year-on-year step up, especially in expansion capex includes our single largest capex project which is our Annilin expansion in Antwerp in Belgium. And, of course, we will continue to maintain an adequate level of maintenance capex to secure safe and reliable and efficient operations.

So, with that, let me come to the topic of the dividend on page 24. We are proposing €3.40 per share. That is the highest dividend in the Covestro history. We had communicated our new pay-out corridor, between 35% and 55%, and we said that in strong years, we will probably be in the lower half of the corridor and in weaker years in the upper half of the corridor and as we consider 2021 to be a strong but not a peak year, the pay-out ratio of 41% is pretty much in the middle of the lower half, so that explains the context and of course, the upcoming AGM on April 21 should then ratify the proposal that we are making.

So on the next page, you can see the details on the share buyback program which we announced yesterday. We announced to buy back shares of €500 million over the next two years. We do see a share buyback as an additional option to create value for our shareholders because it optimises the capital structure for the group and, of course, it increases the earnings and the dividends per share. And with this decision, I would like to reiterate and explain also, and you can see this in the right hand side in the box, our priority in terms of capital allocations. So, what is unchanged, our number one priority is profitable growth through capital expenditures and I was talking about the capex standing for next year on one of the previous pages. Secondly, we do want to maintain an attractive dividend pay-out and I think that the proposal we are making for 2021 is underlining that. However, what we currently see is that large acquisitions currently for us have a lower priority. This is also driven by the fact that we see that the multiples that are currently paid in the market make it very difficult for us to find value creating M&A activities for us, at least on a larger scale and you know that we are very much value driven and selective here. Therefore, the priority for large acquisitions currently is lower. That then leads me to our share buyback because we do think that currently, the investment into our own shares is a very attractive investment opportunity that we have. And just to conclude it, we do remain committed to a solid investment grade rating and with that, I would like to hand it back to Markus.

Markus Steilemann

Yes, thanks a lot Thomas and before we enter into the Q&A session, please allow me to quickly summarize. Our EBITDA increase in full year 2021 was driven by positive pricing delta and we were able to pass through the unprecedented raw material inflation. Secondly, we suggest to the annual general meeting a record dividend of €3.40 per share for full year 2021, with a dividend yield of 6.3% based on year-end share price. Thomas just alluded to our share buyback program of half a billion Euros that has been launched, using the opportunity to create value for our shareholders. The full year 2022 earnings outlook is again above mid-cycle level based on solid sales growth and a strong start into the first quarter of 2022. And, we also announced our climate neutrality in 2035 ambitions and an important intermediate milestone: a 60% reduction of greenhouse emissions referring to scope 1 and scope 2 in 2030. So, all in, looking ahead means expecting profitable growth into a climate neutral future. Thanks a lot and now we are looking very much forward to your questions and I'm handing back to the operator. Thanks a lot.

Questions & Answers

Operator

Thank you. Ladies and Gentlemen, at this time, we will begin the Question and Answer session. [Operator instructions]. The first question for today comes from Mr. Christian Faitz, who's calling from Kepler Cheuvreux, over to you.

Christian Faitz, Kepler Cheuvreux

Good afternoon, everybody. Good afternoon Markus, Thomas and Ronald. Two questions if I may. First one, I know your sales exposure into Russia and the Ukraine is rather limited, yet looking at some of your major customers, there are exposures in these regions. I am thinking of IKEA and furniture or Henkel and adhesives. Would you see those sales into these major customers as being impacted and can you give us an idea of how impacted those would be? And then, the second question, is it still your plan to come to a decision where to build the new MDI plant by the middle of this year? Thank you.

Markus Steilemann

Yes, Christian. It's great to hear from you and let me answer the following way. For sure, we are looking into individual customers that have exposure to Russia and for sure, we are also looking into specific industries that have exposure into Russia. But, currently, it is way too early to really speculate about how that from a macro perspective and also from an overall industry perspective would impact our own sales, because there are so many influencing factors that it are really currently difficult to predict. One thing that I would like to make sure is that we understand: we have numerous assumptions from a macro perspective but also numerous assumptions from an individual industry perspective and so even if some of those aspects are maybe not exactly in the order of magnitude as we currently expect it today, we do see very limited to maybe even no impact on our, for example, current guidance for the year. For sure, if there was massive influence, for example, global GDP would go massively down, maybe even half or even go below that would have an impact, but it is way too early to say that and that is why we are also factoring in what we currently can see and that is also what you see reflected in the current guidance. So I hope that answers the first part of your questions. And, in that context, you also have to see that Russia is only representing 2% of global GDP, therefore a spillover effect should be, at least from today's perspective, limited. I know there are different scenarios out there, but we're closely monitoring the situation. But, today, honestly speaking, this is the position we have and this is what we today can say to this. On MDI, we have always been clear that we will come to a decision at the end of the third quarter, beginning of the fourth quarter. So that means, after the summer holiday you will hear more about that.

Christian Faitz, Kepler Cheuvreux

Okay, thanks, Markus. Thank you very much.

Operator

The next question comes from Mubasher Chaudhry, who's calling from City. Over to you.

Mubasher Chaudhry, Citigroup

Hi, thank you for taking my questions. First of all, on the guidance: could you please talk about the new spreads that get you from the bottom end of the guidance, up to the €500 million to the €3 billion range around there. And then, second one on industry utilizations, can you provide some thoughts on the MDI/TDI utilizations in 2021 and where you see them going for 2022, please? Thank you.

Thomas Toepfer

So, the sound quality was a little bit poor, so I'm trying to answer the first question. If it's not spot on, please let me know and I will try to repeat it. So, what I understood in your question is "what will bring us to the bottom end and the top end of the guidance?". There's two major factors, one is you should know, of course, we are assuming a growth factor for 2022, so a mid-to-high-single-digit number growth. That is factoring in the assumption that we will have lower unplanned shutdowns than we had in 2021 and that we will simply have a higher up time for our own plans. And secondly, on the negative side, it is assuming essentially, a negative pricing delta of €1 billion, because we do see that there is, especially in Asia new capacity for polycarbonates coming to the market and we are, already now seeing some pricing pressure for polycarbonates in that region. So, how exactly that will play out, is of course, the big question. There for the lower end of the guidance, simply assumes that we will again have some unplanned shutdowns and therefore not deliver the full growth potential, so rather in the mid-single digit range and the other factor, every percentage point of growth is from €80 million of EDITBA, just to give you the order of magnitude and the other is, of course, the pricing delta. We do think that €1 billion is a reasonable number. You can see that the pricing, the mark to market today stands at €3.3 so that also shows you the order of magnitude that we factored in, but of course, things can move quickly. However, I would also like to be a little bit more confident here. We currently do see that Q1 is on a very good track and the fact that we are guiding between €750 and €850 million, so above previous year, is maybe another proof point to that. So I think those are the swing factors between the lower and the upper end of the guidance for EBITDA.

Markus Steilemann

Yes, and thanks Thomas also here, if you would like to have a bit more flavour on the individual product groups MDI/TDI, polycarbonate as well as our standard polyols. Let's take a look at MDI first. We actually assume that based on nameplate capacity last year, we had an industry utilization of around 90% for the full year and we expect given the continued demand, but also the continued supply editions that we should see, that we should move above 90% in full year 2022. The maybe well-known Wanhua ramp up last year in early 2021: expansion should, more or less, already been absorbed by the market and at the same time, I believe that we are currently in a situation, where things can turn north and south. That means, we are in a situation where we can have a balanced MDI market, but I would lean more towards a market that's, let's say, that would change to be a little bit undersupplied, if there are not major disruptions happening in, maybe one or the other direction and TDI margins, you know, it's a slightly different story. Because nameplate capacity, we are operating at rates in the full year 2021 at around 73%. That would indicate that there would have been little pricing power, but we have seen actually opposite in the overall market and also, given that the available capacity based on planned or un-planned shutdowns is actually much lower than a nameplate capacity also expected overall. Structurally this situation improves, but we also may benefit a little bit from this current lack of availability of some TDI plants around the world. So long story short, if you look at the overall mid-term development, the announcement until 2026, the supply growth and on the other hand demand growth in TDI, we expect that we will see a further improving industry utilization rate and especially in 2022 and 2023, the announced capacity editions would only sum up 1% by each year. So that also gives you flavour on TDI. Standard polyols in the really relevant markets for Covestro, which is Europe and North America, you could see that the industry margin levels are assumed to be extraordinarily high. That means more than twice as high as historic average and the reason for that margin peak was that we had several production limitations at the same time of larger producers (and I'm not going down the entire list now). We have seen a recovery of the supply in Europe and North America and that would indicate further margin normalisation during this year. That might be, on the other hand, potentially cushioned by planned turnarounds in the second quarter by, for example, Dow and Shell in Europe, but also Lyondell and Dow in North America. So overall, we have seen that in China already some margins declined happened to normal levels and with the rest of Asia Pacific to follow and it remains to be seen how that spill over effect will look like for Europe and the US. Because currently, that is limited. Particularly by the significant increase of supply chain cost that we talked already about in a different context and reliability of the assets. So last point, and Thomas has alluded to that already quite a bit, on the polycarbonate and here in particular, I'm referring to the commodity part in our Performance Materials segments, so that standard polycarbonate types. We assume that we will see a further decline of the nameplate capacity utilisation from 69% last year to around 65% in the full year 2022. And we also see that there is additional capacity until 2026 coming in. So we have a supply growth of 5 – 6 %, which is above the average annual demand growth of 4%. That would also then indicate, that it would lead to a further decline in industry utilization rate so, long story short: supply editions expected to peak this year and so on and so forth. Long term supply growth is expected to further decline. Nonetheless, we are in a rather challenging situation with regards to standard polycarbonates. However, and I think we have made that very clear, we are moving away from the commodity and standard polycarbonates for Covestro. The volume share of standard polycarbonates now in the segment performance materials versus the total polycarbonates declined from 65% in 2010 to only 32% in 2020 and we saw 27% in 2021 and we expect that share to further decline in 2025 to 20% and that shows you very clearly that our exposure to that segment is decreasing by the day. And our exposure to the high value segment is increasing by the day. And that should give you also some comfort on how we are cushioning this. Nonetheless, Thomas has alluded to that, what that overall could mean, for all four product groups in terms of our pricing effect in 2022. It was a long answer, however, I think it is important to get the full picture, so that you have a better flavour of how to look at our guidance and also the year ahead.

Mubasher Chaudhry, Citigroup

Thank you very much.

Operator

The next question comes from Geoff Haire, who's calling from UBS. Please, go ahead.

Geoffrey Haire, UBS

Thank you very much for the presentation and the opportunity to have some questions, I have two related to energy. So, if I look at slide 20, if I'm reading it right, I think you're saying that there's a €500 million increase in the energy bill in 2020, but if I look at it from a market to market basis, at the graphs and the information we can see, it would imply that this could be significantly higher than €500 million. So is there offsets with hedging or long term energy pricing contracts that you have or that you could discuss. And then also connected with this, do you expect energy costs to continue to be high relative to where we were last year in 2023 or do you assume some normalisation?

Thomas Toepfer

Well Geoff, this is Thomas. Your last question certainly is the $100 million question, so let me start with the first one. Exactly, the numbers in the light blue columns that you see is yes, we had €0.6 billion energy costs in 2020, €1 billion last year and we were expecting €1.5 billion for 2022 in our plans. If you mark that to market with yesterday's levels, you're right. It would be slightly higher, roughly €1.7 billion. But again, I would say in the overall context, we have shown that we were able to pass through energy cost rises quite successfully in 2021 and therefore, the daily mark-to-market, which really had quite an amplitude over the last number of days, would not lead us to change our guidance. But you're right. The €1.5 would be €1.7 as of yesterday. What are we expecting for 2023? It's really more the volatility that is a challenge and not the absolute level, because we have seen this specifically in our Solutions and Specialities segment where we are somewhat slow to adjust contracts to price changes, simply because they are longer running. However, if it is a longer plateau on a higher level, our view is that also the Solutions and Specialties segment should be able to pass this on to the customers and therefore, we are not so much concerned with the absolute level, but more with the volatility in the energy prices.

Geoffrey Haire, UBS

Can I just ask a follow up? Within your multi-year contracts that you have for MDI or polycarbonate, do you have energy pass clauses in these?

Thomas Toepfer

Essentially, we do not have longer term contracts for MDI and TDI, so those are one-month rolling contracts, if you like. I mean, there might be a frame contract with minimum and maximum quantities, but the prices are essentially adjusted on a monthly level. Therefore, there is no automatism. So there is no automatic price adjustment clause, but there is a monthly re-negotiation of the prices, which is the standard in the industry.

Geoffrey Haire, UBS

Okay, thanks.

Operator

The next question comes from Thomas Swoboda, who's calling from Société Générale. Please go ahead.

Thomas Swoboda, Société Générale

Yes. Good afternoon, everybody. I have two questions left, please. Firstly, on capex. Can you give us a sneak preview on the next couple of years in the light of the investment in sustainability and the MDI plant, wherever it will be built? So when do you see the peak? What is the peak capex roughly? Whatever you can say. And the second question is on your emission targets. An important driver is the renewable energy. My question is: How much of the renewable energy you have in your planning, you are going to require yourself, meaning how much is under your control and how much do you do rely that basically, the governments will provide enough green energy so that you can reach your target? Thank you.

Thomas Toepfer

Yes, Thomas. This is Thomas. Let me take the first question on capex. Of course, the sneak preview is somewhat dependent on the decision we take after the summer break as Markus said. But let's assume that just for a minute that we were to decide to build MDI, irrespective of what region in it it is. Then, I think you should expect another step up in 2023 of between €100 and €200 million and you should expect the peak to occur roughly in 2025, with up to €1.5 billion for capex. You also put this in context with our investments for carbon neutrality. We said that we would spend €1 billion over the next 10 years. I think that shows you the absolute capex number that we need to achieve that target is not the big swing factor here, simply because we have no stranded assets, we can fully operate our assets as they are, with drop-in solutions, so renewable input factors. We have to switch the energy to a green energy supply. We have to switch them to green steam. But we don't have to invest big ticket items for completely new installations, because, as I've said, the ones we have do work with drop-in solutions and are not stranded assets and I think that puts into context that the ticket for our carbon neutrality path is not the big swing factor in our capex planning.

Markus Steilemann

Yes and Thomas, this is Markus speaking, that plan has, as Thomas alluded, three big ticket items. Not in terms of cost, but in terms of where we want to focus on in terms of leavers. Where we want to make our scope 1 and scope 2 emissions climate neutral by 2035. Parts of it is, for sure, that we have expectations on how the overall electricity production will look like in a specific country; however, we are not entirely, or even to a large extent relying on that. And proof of that is, for example, how we have so far managed that. We actually closed a big deal at the time, the largest ever made, private deal between two companies on renewable energy was Ørsted where we expect about 10% of the electric demand of our production facility by 2025, being supported by a wind farm of Ørsted in the North Sea. We have actually done a similar deal with the company Engie for a production plant in Antwerp covering already since last year, 1st April, 45% of the electrical energy demand. And then we have, sun powered electricity that covers around 10% of the electrical demand of our Caojing site. So you see that regardless of what the state is doing and the state grid energy mix looks like, we are also pursuing own options to buy our own electricity to make sure that we achieve that target and we will, for sure, adopt this, depending on how, the overall development will look like. So that flexibility is built in. For sure, at one point in time, you have to jump and you have to make a decision for example the Ørsted contract was actually signed in 2019. It takes 6 years to build the wind park and therefore, at one point in time we have to say, "No matter what the state does, we secure our own energy." But on the other hand, that is not different from what we are currently doing, with fossil-based energy. Also here, we have our own supply agreements with individual companies and also here, we already had the chance to say how much green electricity we want to have and so on and so forth. So, long story short, that is not carved in stone and that is relying on any individual governmental decisions, but rather the flexible approach that we have within the three major levers that we have described in the presentation.

Thomas Swoboda, Société Générale

Very clear, thank you both.

Operator

Thank you. The next question comes from Matthew Yates, calling from Bank of America. Please go ahead.

Matthew Yates, Bank of America

Hi, good afternoon. Just a couple of questions please. Just to clarify on the market-to-market calculation, are you assuming mid- to high single digit volume growth within that That's the first question. The second question is for Markus, maybe going back to slide 17 on your Polycarbonate Mix, thanks for the detail there. When you've talked in this call about intensified competition, can I just check, is that specifically on these more standard products? Or are you seeing competition creep into the more sophisticated areas? And if I could ask a third one around the buyback. Just out of curiosity, the decision to do this over two years rather than one year, can you just explain the thought process there? I'm guessing that it's not really just a question of approvals, but more living within a financial framework. If that was the case, then was there any debate about adopting a more modular approach over a shorter time period that you could revisit and update over time, depending on how things evolve. Thank you.

Thomas Toepfer

Let me maybe start with the first question on the market-to-market. So, yes. That essentially takes into account the current pricing level or current margin level, I should say, as of January. And if you multiply this then out with our volume assumptions for 2022, so the mid- to high single digit growth rate, that we see. So that is, essentially, the product that gives you then the €3.3 billion. And, as I said, 1 percentage point of growth essentially translates into €80 million of EBITDA as an effect. I could also directly cover the share buyback question. So, we always said that we would do this in an opportunistic and anti-cyclical way. So we do feel that the two year horizon gives us the flexibility to do exactly this. There was not a big debate, because secondly, we also see this as market standard. Therefore, we do feel that both from a company, but more specifically from a shareholder perspective, this is the right approach to give us the time to really act flexibly and, as I said, opportunistically with respect to the share buyback.

Markus Steilemann

Yes, and on the third question, as you alluded to, more the sophisticated or the non-sophisticated part. If I assume that you mean with non-sophisticated part, the standard polycarbonates. That is where the competition is really in full swing. That is where we also expect the market to really heavily compete. And that is exactly why we, long time ago already have moved away and doing that with increasing speed over the next years from that particular segment. Nonetheless, we are very competitive in this market, to be absolutely clear. We have large assets. We use high economy of scales continuously and particular now in the new structure focussing on cost leading positions in all regions with all assets where we produce to make sure that we always get the best out of our investments here and compete as tough as possible and as dedicated as possible in that. Do we see similar trends in the sophisticated grades? Honestly speaking, no. Why? We have some local competitors here and there, who try to do the same trick that we do. But, we have to consider that this a more a technology platform approach for the sophisticated grades of polycarbonates. What do I mean with that? You have to understand how all the technologies work together. You have to have the ability to invest. You have to have the ability to have critical mass also to have this research and technology platform really having leading edge technology. And the newest trend here, for example, is the digitalisation, simulation kicks in with all the new calculation capacity, supercomputing, high performance computing, even quantum computing and by that you could even further accelerate, your development speed towards customers with regards to that technology platform. That makes it more and more difficult for smaller, local competitors to really step in. And that means that you need to have global reach, global scale and access to those technology platform levers, otherwise you will not be able to really compete in that market. Therefore, that is a market for the big ones. That is a market for the fast ones and that is a market for the innovative ones. Therefore, we feel very well positioned in that segment, no matter how the competition looks like.

Matthew Yates, Bank of America

Very clear, thank you for taking the time.

Operator

Thank you. The next question comes from Georgina Fraser, who's calling from Goldman Sachs. Please go ahead.

Georgina Fraser, Goldman Sachs

Thank you. Good afternoon, Markus and Thomas. Thanks for taking my questions. I have two. The first one is: just looking a bit further up the supply chain, in Russia. I understand that it's quite difficult to predict how demand might be impacted, but are there any key raw materials in either your own supply chains or competing chemical product supply chains that you think will be affected? And then, my second question is: Do the recent geo-political tensions raise the importance of delivering your circularity targets and how would you characterise the opportunities or benefits for a chemical company that is switching to more diversified feedstocks?

Markus Steilemann

Yes, Georgina. Thanks for the questions. While the Russian supply chain petro-chemicals are limited in that sense. If you look at the benzene prices in Europe, they are just settled only slightly up. And if you look into specific raw materials that we have versus competing products, we have done so far only our own analysis and we do not see currently any short, not even in most of the cases any midterm, physical supply risks of any of the raw materials that we need for our production. And on the long term, we anyhow, and we have stated that in a different context in earlier conference calls, however due to different reasons that we want to broaden our supply base to make sure that we also have here more competition with regard to our supplier base. So long story short, we currently do not see any large effects on our own supply chains, but currently, I have to say, we are not yet aware of any supply chain disruptions of immediately competing products or drop-in products for our solutions, so that analysis has not yet been performed. On the second bit, the second question: we do see clear demand on the markets for products that are having a higher share of circular carbon, in our context. The challenge we are currently facing is that we want to build the raw material markets for circular carbon and that is a key challenge, because we would have more demand from our customer side for those products. We are able to also create value and extract value from those products and we get, by the day, more and more requests from customers and consumers whether they can have the respective products. That is why we have very boldly moved forward on renewable MDI, on renewable TDI, on renewable polycarbonate, exactly to address those markets. The key challenge is that we have to grow and to develop the respective markets from the supplier side. Just to give you a few numbers: last year, we roughly bought 20 thousand tons of renewable certified respective raw materials that go into our large products. This year, we aim to roughly 70 thousand tons to 100 thousand tons. That would mean factor three to five. However, that still, at the upper end, would only represent 2.5% of the total amount of petrol chemical feedstock that we are currently buying. So, long story short, we see great opportunities. We also believe in a first mover advantage to also extract value. But we also see the challenges to now rapidly scale up and we are far, I have to say, far from the situation where this is a major share of our portfolio. However, I see mid of the century, that the industry will be able to supply maybe millions of tons of carbon feedstock. Not necessarily for our own products, but in terms of the overall industry supply and I think that also from the mid of the century, those investments will fully kick in, so that we can make major progress here in that regard. But I truly believe that there is a first mover advantage and that is exactly what we currently try to establish and we'll also try to log-in business with our customers.

Georgina Fraser, Goldman Sachs

That's great, thank you.

Operator

Thank you. The next question comes from Chris Counihan, who's calling from Jefferies. Please go ahead.

Chris Counihan, Jefferies

Thanks guys. You mentioned the mid-to-high-single-digit volume price assumptions for 2022. But I was just trying to tie it back to your 10 year growth in greenhouse gas emission that's on slide 6. In which the orange bar implies average Covestro growth closer to 1.5% per annum, before the described abatement measures. And I noted that the top end of your guidance, as well, you've already potentially used or admitted at least half of that bar in 2022. So are there already some net offsets in this orange bar over the coming years, or can you help me reconcile that to the gross expectations on the volume side longer term?

Thomas Toepfer

Once again, the sound quality was a little bit poor, so I hope that I can answer your question correctly. If I understand correctly, your question is: how to reconcile the mid-to-high-single-digit core volume growth assumptions, especially if you compare this to the historic development. And I would say, what you have to keep in mind is, in 2022, first point, 2021 was a poor year in terms of operational uptime that we delivered, for various reasons. Some of them external, like the winter storm, some of them internal. We had a major standstill in our newly built MDI facility in Brunsbüttel. We had standstills in our facilities in Leverkusen and also in Dormagen. So it was not a great year and we were actually, operationally, below the numbers in terms of core volumes of 2019. And therefore, the big effect that we are expecting for 2022 and it's a Covestro specific effect is that those things will not reoccur. And if you take those things together. Together with some core volume growth, that should come from GDP growth and a catch-up in automotive and you've seen the double-digit number that we are projecting. That brings us then to the mixed number of a mid-to-high-single-digit number. So there is quite a bit of catch-up effect in there and there is, of course, some support from RFM in there.

Chris Counihan, Jefferies

Sorry, Thomas, but I was more referring to slide 6 and the mixed single digits for 2022 and in slide 6 the greenhouse gas emissions rise of, I think, 1 million metric tons over the next decade and I'm asking if there are already abatement issues within that timeframe on slide 6, because that would be implying an average Covestro growth of 1.5% per annum, when historically, core volume had been ahead of that.

Thomas Toepfer

Now, I get it. So, of course, the new volumes are growing with lower CO_2 emissions than the historic numbers, because everything that we invest into growth will be on newer technology. Markus was mentioning things like abatement for NOx. We have the high temperature phosgenation et cetera, et cetera. So all the new technologies that we are building have a lower CO_2 footprint, plus of course, the majority of growth, as we have also shown in one of our earlier investor relations presentation takes place in the Solutions and Specialties segment which, by nature, has a lower CO_2 footprint than the upstream business. And that, I think is, for you, the explanation is not a 1:1 relationship and sorry, if I misunderstood your question the first time.

Chris Counihan, Jefferies

Thank you.

Operator

Thank you. The next question comes from Markus Mayer who's calling from Baader Bank. Please go ahead.

Markus Mayer, Baader Bank

Good afternoon, gentlemen. Three questions from my side as well. The first one is on the RFM synergies. Are there any specific reasons for the fast, unexpected synergies? Or are these faster synergies coming from somewhere specific? Or was it just that you were more conservative for the timing all over amount of synergy and also the cost? That was my first question.

Thomas Toepfer:

And directly to that, Markus. First of all, all of the operational synergies came in exactly as expected. Where we were faster than expected is the cancellation of the service agreement that we still have with DSM for a transitionary period and we were able to take over those services in terms of IT and accounting and controlling and some other administrative functions earlier than what we had put in our plans and that led to the over-achievement. However, that is not to say, just to be very clear, that the more operational things in terms of headcount consolidation and also sales synergies through the joint formation of laboratories and research programs is not above track. It's also on track, but the over-achievement specifically in 2021 came through the early cancellation of transitionary service agreements, mainly with DSM.

Markus Mayer, Baader Bank

Okay. Thank you. My second question would be on the potential fall away of the EEG in Germany, which could be the case in 2022. What kind of affect can we expect for Covestro?

Markus Steilemann

That's currently really, I would say, a little bit challenging to say, because the currently intended stop of the EEG and also the respective potential impact would mean that we would only see about one year later a visible impact and if that would be cancelled, we would at least see a positive impact of about 1.2 million tons of less accounted, if you want to say so, carbon dioxide equivalent emissions, simply due to the fact that we are currently falling under this and therefore, we get the, if I may say so, dirty part of the German energy mix fully into our books, once the EEG exemption is falling away, we would also get the German complete energy mix in our books and that would lead to, as I said, 1.2 million tons positive development in terms of lowering our carbon dioxide emission footprint. Does that answer your question?

Markus Mayer, Baader Bank

Yes. Absolutely. My third question would be then on this 230 thousand tons of polycarbonate compounding capacities until 2025. Can you quantify how much capex will be needed for these kinds of capacities? Also, how fast is the best edition and what kind of regions?

Markus Steilemann

I think two things are very important. Number one is the same like carbon dioxide intensity, the capital intensity for those businesses is happily and, let's say, that's good that actually it's much lower than the intensity for the upstream businesses in terms of capital. So, normally, we would expect, for 230 kT a capex in the lower triple-digit million number and also the complexity to really install it is much lower than building, for example, a fully fledged polycarbonate plant in that order of magnitude. So from that perspective, I would expect that those capex costs are much lower than you would expect for an upstream polycarbonate. I would also expect that we would swiftly execute and we will definitely execute this where the key markets are. The key markets are, for that growth, to the largest extent in relative as well as absolute terms of growth in Asia pacific. However, I do not want to indicate something that we only invest in Asia-pacific, or give you a share, because it is way too early to talk about specific investments but that is just a general order of magnitude to give you some indication. Asia Pacific is the market to be. We also see good growth for those high value products in the United States as well as in Europe.

Markus Mayer, Baader Bank

And regarding the ramp-up pace, specifically, these 230 thousand tons. Should we expect a linear trend for the ramp-up?

Markus Steilemann

Yes, it's difficult to say, because we really look into individual markets and there we go for local permits. We need to see where's the exact place where we do that. And, we also did just finish one line in 2021, the ramp-up is currently happening. That means, specifying with customers then fully loading the plant with all the flexibility that those plants have and so and so forth. So I would not expect a linear ramp-up, but it's more like bits and pieces from smaller and larger lines as we call for extrusion. I mean, that is the name of the technology, how you do it. That compounding is basically an extrusion process and therefore, there might be here 5 thousand tons, then there might be 20 thousand tons, then there might be another 6 thousand tons. So it's really a big network of smaller plants here and there at sites that are close to customers within an already existing site and that is exactly why I cannot say it will be linear topic. But once again, as a reminder, that is not additional capacity in terms of polycarbonate capacity. It's just that we take more of our own production of standard polycarbonate and route it through the additional capacity of highly specialised polycarbonate. So no additional overall capacity, we are just moving from highly cyclical standard polycarbonates now to the value adding products in our portfolio, to achieve, let's say 80% of our portfolio by 2025 to be in that space.

Markus Mayer, Baader Bank

Okay, thank you for this clarification and the answers.

Operator

Mr. Köhler, there are no further questions at this time. Please continue with any points that you wish to raise.

Ronald Köhler

Thank you all for your interesting questions and your interest in Covestro. I think we arealready slightly overdue on time. So, happy to close it right now. If you have any additional questions, just come back to the IR team. Thanks, bye.

Operator

Ladies and Gentlemen, this concludes the Covestro Earnings call. Thank you for participating. You may now disconnect.