



We create chemistry

Presentation Coatings

Transcript Speech

September 27, 2024

Anup Kothari

Member of the Board of Executive Directors

[Title slide: Coatings]

Now I will cover the Surface Technologies segment. As you know, it has three businesses: Coatings, Battery Materials and ECMS. Markus mentioned the direction of travel for these three businesses, which gives us the most strategic and operational flexibility. What I will focus on is how we will unlock value in these businesses while being in BASF.

I will start with Coatings and then I will go to Battery Materials and then to ECMS. The upside for you is: You are able to get a little bit more visibility and transparency on some of the numbers for these businesses, which we generally don't provide. But you will also have to wait through the three presentations before the Q&As.

[Slide 2: Coatings: Leading surface solution provider in mobility applications]

Let me start with Coatings. Coatings is a business very focused on automotive: roughly €4.4 billion in sales, almost €2 billion in automotive OEM coatings; this is our main business here. Then we have a surface treatment business that we acquired some time back, Chemetall. This is close to €1 billion in sales. It's also a fantastic business. A big part of this is also automotive, but it also works in aerospace and other industrial applications. Then, we also do roughly €750 million in refinish coatings.

Then we have the deco business, which is number one in Brazil, a fantastic brand. Here the direction is very clear: We will go for a structured divestment process.

I think some of you went to our agro stations yesterday and got a behind the scenes glimpse into the business. And if you think about the paint on your car, the color on the car, what is underlying this is the surface treatment layer. It's a pre-treatment layer. This is what we do.

There are typically four coatings for protection and creating this color and this effect. The thickness of these four or five layers combined is the thickness of a hair. When I first saw it in Münster in our application lab, I thought this is also pretty cool. A lot of technology, a lot of know-how, application expertise. And our people are also very passionate about this business. This is also how we create value with our customers. Because it's our teams, our expertise, going to customers and solving their problems. They call us if they need a special color. I would say, this is what all the standalone businesses have in common: The people in these businesses are very passionate about their businesses, not just about being pure-play. For them, this is the business they are in. Sometimes they stay lifelong.

[Slide 3: Coatings has outgrown the market and generated strong earnings]

The role of this business is strong earnings and cash. You can see it: It is also showing up in the P&L. Over the last five years, if you look at the gray line, which is the sales line, you see good growth. The market has grown by roughly two points, and we have grown above market: 4% sales growth.

The blue bars are the EBITDA. Here you see that 2023 was a record year for us. And this was not just one year. It was a result of the work that we did over the past years in terms of gaining share, doing many things on our cost efficiencies and operational work, and strong margin management.

This momentum has continued in the first-half results. As you can see: Our margin continues to be strong. So, a lot of good performance in the last years.

[Slide 4: We will further unlock the value of our Coatings business]

And our ambition now is to look forward, the next four years: How do we sustain these margins, continue to outgrow the market? And we have visibility. I will share why we have confidence that we can continue these growth rates.

You also see: Our cash conversion is going up much higher because we also invested in the last years. Now we can benefit from that, and we can have much more cash conversion going forward. You see this targeted EBITDA increase; this increase is in comparison to the average of the four years from 2019 to 2023, not against 2023 alone. Even compared with 2023, it's an increase. But since it was a peak, we're giving you an idea of the baseline over the last few years and then how it will grow.

[Slide 5: Our strategic priorities for 2024 – 2028]

What's underpinning this value creation? There are four strategic priorities that we will focus on to unlock this value. Number one is outgrowing the market with our leading positions in all the three segments: auto OEM, surface treatment and refinish.

This accounts for roughly 70% of this value creation – it's not an exact number, but just to indicate to you – and is the biggest lever where we will drive value.

Then, we will drive operational cost efficiency, which is roughly 15%. And then structural optimization of our asset base is another 15%. That's our focus.

And finally, for the deco business, which we will also talk about later, the aim now is unlocking the implied multiple.

I'll start with our right to win and then give you a feeling of what we are doing now in the market, which gives us confidence and visibility that we can deliver on this.

[Slide 6: We have a focused portfolio with strong brands and leading market positions]

Our right to win really starts from our strong brands, our strong positions where we play. Here, you see the brands we have. They are very well-established longstanding brands, premium brands: number one position in auto, number two in surface treatment, number three in refinish and number one in Brazil.

These automotive markets are not growing as fast, but they are still very attractive markets because of their big size. They have high barriers to entry. There's only a small group of peers that we compete with. It's a market we like and know and in which we are well positioned.

[Slide 7: Key market trends are shaping customer needs]

The trends that are driving these markets – other than the build rates and what's happening in the automotive market – are also very much driven by sustainability trends. For example, in surface treatment, you're always looking at how to use chemistry that is more environmentally friendly, more sustainable, free of certain metals, etc. So, there's always a need for innovation to advance our chemistry.

For the refinish side, you're also always looking at more sustainable solutions and more digital solutions. And because this is much closer to retail in terms of body shops, we're looking at how we can help our customers drive efficiencies and provide good customer service.

[Slide 8: We win by providing solutions for our customers]

This fits quite well with our business model. Our business model is the big brands that we have, which are very trusted in the market. If people have problems, they're looking to come to us. We have this deep expertise in customers' processes.

I'll give you an example here, from the surface treatment side. Just imagine a big turbine in an airplane which has to come to a repair shop. There are so many parts in this turbine which have to be taken out. They have to be cleaned. They have to be treated. They have to be tested without risking damage.

To do that, you really need to understand not just the chemistry but also the processes that our customers are using. That's happening in many industries, such as the steel industry or coil industry. So we go in and our people understand the processes, and then they're able to provide the right product and explain the right way to use it.

So, it's also a game of being local: local application, local assets, people in the region. And the supply chain is, of course, very important.

One area we are building on and where we are also having success is digital offerings, especially in refinish. You can imagine a body shop: People come in with a damaged car and they have to match colors. We have this Refinity Software digital offering where more than a million formulations are available on the platform, and this allows them to quickly match the color. At the same time, we are getting data regarding the trends and what's happening – who's using, how much material is being used, where it's not being used. It's also a fantastic way for us to get access to information which then continuously improves the offering.

We launched it a few years ago, and we are having a good ramp-up in terms of conversion here.

That's our right to win. The right to win doesn't mean that we will win. So, what's important now is how we are playing on the field.

[Slide 9: Growth lever: Our strong positioning and supply share with NEV OEMs in China enables high growth]

Here I give you a view of the growth levers and the visibility we have in terms of how we are playing in the market.

For our automotive OEM business, we are well positioned with all the global OEMs. We have a long history. We are working with all of them. But I want to highlight one group of customers, in China. All the new EV OEMs that are emerging there and launching many cars: Here, we are number one with them. We have been with them now for a few years. For these companies, color is very important. For them, this is a differentiator how they brand and how they sell. There are some OEMs who actually charge you more if you buy a white or black car because they want you to buy a car with a color because it fits their brand.

They come to us because they know we have the knowledge, the application know-how. We can support them. We can be fast. We are locally present in China with production, labs, people and assets. And here we are having fantastic success. This is also one of the reasons why we are gaining share. This is what gives us confidence that we will continue this momentum in this market.

[Slide 10: Growth lever: Winning in aerospace to leverage above-market growth]

I'll now go to surface treatment, which is a different kind of game. Here I use an example of aerospace because that's a market which is growing much more than automotive. We have also been there for many years.

You see an example from Airbus here. This is an award that we have got multiple times as a supplier. We've been with them for 30 years. This also shows you the stickiness of this business – how much qualification, trust and everything you have to build. And then once you are in, you are able to benefit. This market is growing as these customers grow and you can see the growth rate here. We are also growing.

We not only provide different cleaners and coatings, we also provide the sealants. If you can imagine a plane and how much environmental stress, temperature stress, everything a plane endures, it requires sealants everywhere: outside and inside. It's our sealants you will find there.

It's also a fantastic business and gives us growth rates which are above the normal-grade sales that we have.

This is another lever that we are pushing. And we are, of course, expanding our customer base and qualifications and other things here as well.

[Slide 11: Growth lever: Increase market share by winning with the right customers and in growing segments]

For refinish, we have done our homework in the last three years. Now we will benefit going forward. This is where we will also see higher growth rates.

What's happening in this market is: You have what we call multi-shop operators. These are consolidators. They buy small body shops. We have an example here of Crash Champions, one of our customers in the United States. Six years ago, they owned maybe 10 or 11 body shops. Now they own close to 600. And we have been with them, investing with them, helping them setting up their business. This is how we grow. As they consolidate, we grow. This is why I feel very good going forward. We have the visibility of where they are going.

Historically, we have had a very strong premium brand. Now we have also established these value-for-money brands. You see the two brands baslac and Norbin. Norbin is in China, baslac is in our Western regions. This also positions us to play in a bigger volume segment. So, the work has been done. The brands are getting recognized, and we also see good growth there.

Our refinish business is also now well positioned, compared to where we were, to benefit as we go forward.

[Slide 12: Growth lever: Our unique sustainable portfolio positioning enables growth and drives industry transformation]

Another common lever that we have for all of these businesses is sustainability. A cool example here in terms of sustainability: In 2020, we introduced the Glasurit 100 line. First of all, it is 40% below the E.U. solvent limit. So, it's really benchmark for what is possible in terms of VOC emissions. At the same time, it uses less material and requires less process time. So, the total cost of ownership for customers is lower. This allows us to price it for performance. We are also substituting our portfolio with these products because it's a win-win. You get a lower cost of ownership and it's better for sustainability. In our portfolio you can see: 18% is already switched over to sustainable products and we plan to switch even more.

This is an example from refinish. But we are also working on these kinds of things in our labs for the entire portfolio. This gives us confidence that it will continue to help us win with technology, also in the different segments.

So, hopefully you can see: This is why this growth lever is something we are very confident about. We are growing above market. We have already shown it and now we can continue this momentum and outgrow the market with the right customers, right segments, right technologies and our teams.

[Slide 13: We drive cost efficiencies and operational excellence along the entire value chain to reduce inflation impacts]

Now, at the same time, we need to work on cost efficiencies. This business is fantastic. It is also very complex. We have close to 50,000 customers in Coatings. Just to give you a sense: This is half the number of customers of the entire BASF. If you think of our number of products we produce here, it's also roughly half of all the products in BASF.

But it's a perfect place for automation, digitalization and driving efficiencies. We can put these at the center of all our different steps here: in procurement, production, supply chain, labs and sales.

We have had a lot of successes, and we continuously work on this because it enables us to continuously unlock more operational efficiencies as we go forward.

[Slide 14: We are disciplined in capital steering with investments focused on growth in Asia and optimization in Europe and South America]

We are also looking at structural efficiencies. Some of this we have already announced. For example, there are assets and plants where we were not as profitable, or we thought we can consolidate. So, we have announced some exits in Brazil and Argentina – where we exited the OEM coatings business – as well as in Europe. We have consolidated some assets from some of our sites into one place in Münster, where we can have a much more efficient setup. This allows us, again, to drive structural efficiencies; this is what we have done. And this is why this capex has been spent. And now we will see the benefits going forward.

At the same time, we continue to invest in our growth markets, which are in Asia. Our investments are now shifting, as you see on the right-hand side, among the three segments, much more toward surface treatment and refinish. These are also businesses with higher margins. This is why you also see this boost in the margins that we are aiming for. The capital allocation also goes in this direction.

[Slide 15: Our decorative paints business is #1 in Brazil]

Now, I'll take a minute to make a pitch for our fantastic deco business. The Suvinil brand is really a well-known brand. It's a very renowned brand in Brazil. It's a B2C business. We are number one in the premium segment. We also have a very strong brand Glasu!, number two in Brazil.

[Slide 16: Divestment of decorative paints to unlock value from implied market valuation]

This business is also a good-sized business. It's roughly €500 million net sales and 1,000 employees. It's a fairly standalone business even today because it has limited synergies with the rest of the automotive segment and industrial segment.

We are very confident that this business, with the right ownership, can even grow more or extract more value and can also be value-accretive for us. This is the process we will kick off now.

[Slide 17: We are creating value in Coatings by focusing on growth and efficiencies]

I come to my last slide to wrap it up. Our focus with this business now truly is on unlocking the value while we run within BASF. We have a direction of travel which could take us to a different place. But no matter what, it's a no-regret move for us to focus on improving our absolute EBITDA, EBITDA margin and cash conversion. And that's what the team is focused on.

We communicated this direction of travel to the team in recent days and I can tell you: We have a fantastic team. Many of them love coatings. For them, it is about: How can we win in the market, how can we grow? We are very proud of the know-how we have and the brands we have, and the team is staying focused on this.

That's the value creation playbook for Coatings.