

## BASF Analyst Conference Q1 2014



## Transcript - Q&A Session by Topic May 2, 2014

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## 1. Group and Regions

**Andreas Heine (Barclays Capital):** Very briefly on FX: You had an impact of 200 million in the first quarter. If you do not use what your guidance is – 1.3 for the U.S. dollar to euro – but the current rates of currencies, what do you expect the headwind from currencies will be for the full year?

**Manfredo Rübens:** To the guidance with 1.30 for US dollar versus euro: We look at the signals on the monetary policy in the U.S. and also the growth differential between euroland and the U.S. That is why we still look at a guidance of 1.30 of the dollar. The 200 million of EBIT impact compared to prior year compare basically to something that we told you for the full year 2013 of around 300 million. So here you have to see that the relevant currency devaluations occurred in the second half. With that in mind and without being more specific, last year's number is probably something to look at.

**Markus Mayer (Kepler Capital Markets):** Good morning! One question on the demand. Other competitors said that the demand momentum is less volatile this year than last year. Do you also see this?

**Dr. Hans-Ulrich Engel:** On demand and environment: If you look across our portfolio, I'd say, in general in our Chemicals businesses as reflected by the volume growth that we have in each and every – so that's in Chemicals, Performance Products, Functional Materials & Solutions – overall, as we stated, a nice development. But when you look in the underlying businesses, you see differences here and there. That's why it's just difficult to comment on a question that broad in light of our portfolio. But pick something like natural gas trading: I can only say that the demand that we have seen was very low, as a result of the winter. But I'd say: A fair statement would be: Overall, in the Chemicals segment we have seen a good volume development based on demand, we have seen strong volume development in our Agricultural Solutions segment based on demand. And we hope that this development will continue also going forward into Q2.

**Markus Mayer (Kepler Capital Markets):** Is the net working capital increase also due to the expected restocking and therefore together with this demand momentum then a more stable and forecastable environment?

**Dr. Hans-Ulrich Engel:** I'd say, this stocking, destocking, restocking is always very difficult to answer. What do we see? As already mentioned, we have seen good volume development. That's certainly reflected also in the case that our net working capital and there in particular the inventory increases. Then you see an effect in there which has to do with our precious metal business. As you are aware, the strikes in South Africa are continuing. As a result of that, we made a decision going into the year 2014 that we increase our precious metal – and this is physical – in order not to run into any supply issues.

**Andrew Benson (Citigroup):** Perhaps I can ask a question on the first quarter. You talked about start-up losses being about 200 million for the full year. Can you give an indication of how much there was in the first quarter?

**Dr. Hans-Ulrich Engel:** Regarding your start-up cost question. As we said, we have roughly 150 to 200 million in start-up cost in expecting that in the year 2014. These are the costs which will not be capitalized for projects such as the MDI and the TDI plant that we already talked about, the dispersion plant in Freeport in the U.S., the formic acid plant, the acrylic acid and super-absorbent complexes, both in China as well as in South America. That comes out to 150 to 200 million in the year 2014. For modelling purposes, I would say, relatively evenly distributed over the four quarters.

**Martin Evans (JP Morgan Cazenove):** On M&A, given what's been happening recently in equity markets and your cash flow, again, which is strong. How are you feeling about M&A potentially at the moment in terms of the availability of businesses and prices? Has your confidence to move forward with a significant deal increased or not? – Thanks.

**Dr. Hans-Ulrich Engel:** M&A: Martin, look at what we have done over the last two years, compare that to what we have done between 2006 and 2010 and then also look at the stronger focus on organic growth that we have in the BASF Group, supported by an increase in our capex programmes. I think that gives you a picture and that gives you the mindset that we are in. If you combine that then with the current very high multiples, if you look at transactions, that gives you an additional piece. I think I would just leave it at that.

**Lutz Grueten (Commerzbank):** Good morning! One question on regions: Could you give us a trading update on China? I am especially interested in the underlying demand and the short-term outlook.

**Dr. Hans-Ulrich Engel:** China: I think we all have seen the Q1 GDP figures, which came in, I would say, as expected – always keeping in mind that Q1 figures in China are obviously impacted by the Chinese New Year, which at least for me makes it a little difficult to get a really strong and thorough reading on these figures.

If I look at our business, we enjoyed a nice volume growth in China, in the order of magnitude of what you expect in an emerging economy. In other words, our volume growth in China was stronger than GDP growth. From that perspective, I would say: fully in line with our expectations. Also the start into the second quarter looks okay from our point of view.

**Lutz Grueten (Commerzbank):** A question on Russia: What is your latest news from the ground? Is your capex spending on budget? One word on the cooperation with Gazprom, please. – Thank you.

**Dr. Hans-Ulrich Engel:** On Russia, at this point in time we do not see any impact on our business, neither in the chemical business nor in the E&P business in Russia. We also do not see an impact on our raw material supplies that we are getting from Russia. In other words, the crisis there does not have an impact on the business. Where we certainly see an impact is to currency. You see the decrease in the ruble. That has an impact on our business.

I think the question that you asked related to the planned asset swap with Gazprom. There I can tell you that from our point of view everything is on track. We have the necessary approvals to do the transaction, both from the EU as well as from the German government. We are currently in the phase that you tend to be in roughly two months before closing a transaction: It is slashing out the last contract details there, making the necessary changes that are required in corporate setup. So everything is on track there. We are targeting closing that transaction mid-year, as we had announced it earlier.

**Andrew Benson (Citigroup):** Good morning, thanks very much. I think you have talked a little bit to investors about the government insurance against nationalization of assets. Can you give some detail about that? Obviously, the Russian government has been talking about energy interests if things deteriorate in Ukraine.

**Manfredo Rübens:** On the government insurance: This capital insurance from the German government is quite a customary instrument that we have been using already for decades. I believe it started probably in the 1970s and it is not only Russia, but also other countries like China or Libya where we use this capital insurance. Looking at Russia, we probably have more than 90% of our original capital investment in participations that we have or in participation-like loan structures, shareholder loan structures to joint ventures, partly also dividends, are covered by those insurances.

## 2. Capex projects

**Thomas Gilbert (UBS):** Good morning, Maggie, good morning, Hans! My question is on the on-purpose C3 facility in the United States. Coming back to the question we asked at the annual conference in Ludwigshafen, 13% of your capex budget through to 2020 was classified as being non-allocated or other. Is it fair to assume that the investments you make in ammonia and the one considered as of this morning, fall into that category, i.e. you will absorb some of that budget and re-allocate it into the Chemicals segment? Or does this announcement imply an increase in the capital expenditure guidance as per the Annual Report? If you can comment on that, that would be great.

**Dr. Hans-Ulrich Engel:** Thomas, if you look at the five-year capex plan of BASF, you can assume that the investment – if you look at the announcement, we clearly say that this is still very early stages –, but you can assume that most of the investment is included in the five-year capex plan.

**Tony Jones (Redburn):** Good morning everybody! I just wanted to go back to the on-purpose unit, actually. I am just thinking about the purpose of this. Clearly, this is to try and improve costs and will be positive for margins. But I was wondering whether, as part of this project, this will lead to additional downstream capacity, things like acrylics or alcohols or something? Or is this purely just to optimize costs? I suppose the question is: Will this be the start of the renewed emphasis on building up your production base in the U.S.?

**Dr. Hans-Ulrich Engel:** Tony, if you think about the fact that we are in a net buyer position for propylene in North America, that is the key driver for considering an investment in propylene in the U.S. We are currently building a dispersions plant, which also increases our propylene demand slightly. We have downstream capacities, which at this point in time are not 100% utilized. So there is a little bit of additional capacity there that could be supported.

Can I exclude that there will be further considerations for downstream activities in an attractive market like North America? No, I don't want to exclude that. But let's now, first of all, think about this exciting project. Then we will take it from there step by step. As I mentioned earlier with respect to Thomas' question, this is really very early stages where we are making this announcement. There is still a lot that needs to be considered.

Most probably you have seen our press release in which we said: Investment amount needs to be detailed, capacity needs to be detailed, location of the plant needs to be detailed. So let us do all of what we need to do there and I will take it from there.

**Jaideep Pandya (Berenberg Bank):** Just a small follow-up: Could you remind us how much of a net buyer position you have in the U.S. in propylene? – Thank you.

**Dr. Hans-Ulrich Engel:** The net buyer position: I tried to elegantly avoid answering that because we actually don't disclose, for obvious reasons, in what kind of position we are or give you a volume there. But I can clearly say that we are in a net buyer position.

**Pandya Jaideep (Berenberg Bank):** Can I ask it the other way: Would you be a merchant seller with this investment?

**Dr. Hans-Ulrich Engel:** This is not what we want to develop in with this investment.

**Laurent Favre (Bank of America):** My question is very quick, a way to rephrase Jaideep's question on the propylene project. Before the investments in Port Arthur towards lighter feedstock, were you a net buyer of propylene?

**Dr. Hans-Ulrich Engel:** The answer is a clear yes. We were a net buyer already prior to lightening the feed for the cracker in Port Arthur.

**Andreas Heine (Barclays Capital):** Very briefly only an update of the schedule of your TDI plant in Germany and the MDI plant in China: When will these two plants be on stream? – Thanks.

**Dr. Hans-Ulrich Engel:** We are moving forward with that as planned and targeting to start up the TDI plant in Ludwigshafen in the beginning of 2015.

**Andreas Heine (Barclays Capital):** And the MDI plant in China?

**Dr. Hans-Ulrich Engel:** On the MDI plant in China: You saw that there were changes in the gas price. That was set by the Chinese authorities. That led to re-considering part of the entire setup, which is not the MDI plant that we are building, but some of the precursor plants there.

We are currently in a situation that it looks like there is some delay, which would lead to a start-up of the MDI plant beginning in the second quarter of 2015, compared to what we have said so far, which is late 2014, early 2015.

### 3. Segments

#### 3.1 Chemicals

**Paul Walsh (Morgan Stanley):** Good morning, Maggie! One question from my side: Clearly, in Chemicals, divisional volumes are quite strong and accelerating. At what point, Hans, do you think pricing power will be brought back into that division? Can you give us a sense of where utilization rates are and at what point you could expect to see cash margins beginning to expand again? – Thank you.

**Dr. Hans-Ulrich Engel:** Paul, if you think about Chemicals, yes, you are right: We have a nice volume increase there to the tune of 8% across all three businesses, a nice volume development. On the margin side, that looks slightly different.

In petrochemicals we have a situation where margins in North America – thinking about cracker margins – are highly attractive, in Asia not so attractive, but in the process of improving. Can I give you a point in time where pricing power will be stronger than at this point in time? I would say that is very difficult. But what we certainly enjoy at this time is an increase in demand, which is clearly reflected in our volumes. I certainly hope that this will find its way then also into the margins.

**Paul Walsh (Morgan Stanley):** Are you seeing anything in the second quarter that is suggesting different trends from what you have seen in the first quarter?

**Dr. Hans-Ulrich Engel:** No. I would say, the dynamics that we have seen in Q1 continue into Q2. If you look at the upstream businesses: Turnaround season is starting in Q2. That could actually help the situation.

**James R. Knight (Exane BNP Paribas):** Good morning! Can I just gear from C3 to C2: You will be aware that a massive ethane export terminal has been announced recently in the U.S. I guess we will talk a lot more about these themes next month. But can I get an early BASF comment on this? Do you still think little ethane will end up in Europe in the longer term? How might this impact BASF, if at all?

**Dr. Hans-Ulrich Engel:** Ethane exports from the U.S.: This is a preview version with actually more coming at our Chemicals Investor Day in London and the U.S. end of May and early June. Our expectation is that there will be relatively little ethane that is exported to Europe – for two reasons, one being cost and there, in particular, logistic costs, which is in a similar order of magnitude as the LNG supply chain, the second being the European facilities which would need a significant amount of capital in order to convert them to be able to consume lighter feed. So far for the sneak preview.

### 3.2 Performance Products

**Michael Rae (Goldman Sachs):** Hi there! Thanks very much for taking the question. Is it possible to get a bit more detail on the fixed cost reduction measures in Performance Products? Can you quantify the savings in one quarter and provide a look for the remainder of the year? Thanks.

**Dr. Hans-Ulrich Engel:** Yes; I can certainly try to do this for you. As you know, we have announced over the last 18 months a number of restructuring activities in our Performance Products segment. They are covering all the divisions in the Performance Products segment. Based on what we have announced, we are looking at an earnings improvement in the order of magnitude of 450 to 500 million in the year 2016, roughly a reduction of 2,000 positions in the Performance Products segment and one-time cost in the order of magnitude of 250 to 300 million.

Impact so far: in Q1 2014, if I look at benefits from the programmes, compared to one-time cost, that is pretty much a wash, but over the next quarters we should start to see some impact, positive P&L effects from the restructuring measures.

**James R. Knight (Exane BNP Paribas):** On nutrition pricing pressure, are you indicating there that the announced rises haven't stuck?

**Dr. Hans-Ulrich Engel:** Your question on nutrition and in particular on vitamins and the price increases: What have we seen? We have seen overall that the – I would call them – relatively steep declines in vitamin E prices slowed down. But your assumption is correct with respect to vitamin E: The price increases did not stick.

That is different with respect to the other vitamins where we have seen that the price increases were accepted, which has also helped to improve the performance of our Nutrition & Health division.

**James R. Knight (Exane BNP Paribas):** A very quick follow-up: Are you seeing any change in that dynamic in the second quarter?

**Dr. Hans-Ulrich Engel:** Based on what I can see so far: No.

**Patrick Lambert (Nomura):** A very quick one: I don't see any citral impact at all in Q1. Why is that the case?

**Dr. Hans-Ulrich Engel:** On citral: Yes, as you know, we have an outage there. We had to declare force majeure. Let me put it this way: That had a small impact on the P&L of the Nutrition & Health division, but nothing major. The plant is back up and running. So I think we have that behind us and actually that should be it.

**Peter Clark (SocGen):** Good morning! It is drilling down into the Performance Products again. I know you review the businesses obviously and there has been some that were up for sale, then stayed in the portfolio.

Looking at businesses like paper chemicals: Clearly, you are fighting against a structural shift in the market. I am just wondering how regularly you review how they fit the portfolio. Quite clearly, a lot of positive work is going on across that division to improve the performance. But in some markets it might well be just holding water. So I am just wondering how the Board looks at businesses like this and how often they are reviewed.

**Dr. Hans-Ulrich Engel:** We review our portfolio, Peter, on a regular basis. This is part of the blocking and tackling that you do in each and every business. We positioned our paper chemicals business as a restructuring case from the point in time where we combined our paper chemicals business with the Ciba paper chemicals business.

We are addressing the performance issues that we have. Some of the first steps that we announced in the restructuring measures in Performance Products related to our paper chemicals business. Rest assured that we are working on it and working on increasing the profitability there.

### 3.3 Functional Materials and Solutions

**Laurence Alexander (Jefferies & Company):** I have just a question on the catalysts business. It's the comment on refinery catalysts, where you comment volumes were up, but I guess most of the other participants have had a very weak environment because of the timing of outages. So I was wondering if this a share shift or if it is just where your geographic footprint is.

**Dr. Hans-Ulrich Engel:** To be honest, Laurence, I can't answer that question. In refinery catalysts it always depends on what is the point in time where your customers reorder. A positive development in our business compared to the competitors that you are referring to based on one quarter would not lead me to say that there is a share shift or that we are gaining market share. I would have to see more than just one quarter. Let's see what Q2, Q3 and Q4 will bring us here. But so far, we had a good start into the year in our catalysts division overall.

**Christian Faltz (Macquarie Capital):** Good morning, thanks for taking my question. Construction chemicals: Can you share with us the regional performance of construction chemicals? If I remember correctly from my coverage of SKW Trostberg, this was strong in Japan. So any driver there?

**Dr. Hans-Ulrich Engel:** Christian, construction chemicals: positive development overall in Europe, if you compare that to Q1 of last year, benefiting clearly from the mild winter in Europe, which had a positive impact on construction activities.

North America: just the opposite. You can also see that in the U.S. GDP figures where construction is one of the culprits when it comes to explaining why GDP in Q1 2014 is so low. We experience exactly that due to a cold winter: hardly any activities.

Asia and rest of world are pretty much in line with what we have seen in the prior-year quarter. Overall in construction chemicals a nice earnings improvement as a result of the various restructuring measures that we have taken and implemented over the last 18 to 24 months.

**Laurent Favre (Bank of America):** Good morning! My question is on Brazil and paints. Are you specifically talking about volumes being up when your two key competitors have talked about volumes down in line with the market? I am just wondering: Is that market share gain – which, I guess, is the only explanation? Is it the result of specific actions? Or is it just a function of the dynamics for this quarter?

**Dr. Hans-Ulrich Engel:** If you go back to Q1 of the year 2013, I think we clearly said that we were not very happy with the development in our decorative paint business in Brazil. And I think we have done a better job in Q1 of 2014. Now, with respect to market share and market share gain, I'd like to answer that in a similar way as I did with one of the earlier questions: One quarter – at least for me – is not enough to say if we are gaining market share or if we are losing market share. We look at this over a longer period of time.

### 3.4 Agricultural Solutions

**Jaideep Pandya (Berenberg Bank):** Just a question on agri: You have another very strong quarter with 9% growth. Could you just tell us how much of this is really coming from the products that you have launched in the last two years? What should we expect? Last year was also a very strong year.

**Dr. Hans-Ulrich Engel:** Regarding your question on volumes Agricultural Solutions. Do we break this down and tell you exactly how much additional sales we generate through our new products? No, we don't. But I can clearly tell you that the market introductions that we did over the last two years – Kixor as well as Xemium – are contributing significantly to the very nice performance that we are seeing in our ag chem business in Q1 where, I'd say, we see a continuation of the very good performance that we have seen in the years 2012 and 2013. That is clearly driven by the fact that we are supporting our Agricultural Solutions business with significant R&D funds that help to position the portfolio the way we would like to see it. That generates volume growth for us, as we have seen it in Q1, with 9%. Not only that: We have also seen a positive development on prices to the tune of, if I recall that correctly, 3%. That led to the very nice performance of the Agricultural Solutions segment. Even despite the fact that we had strong currency headwinds the business delivers this performance.

**Patrick Lambert (Nomura):** Hi, good morning! A quick one on agri again: Is there any Monsanto contribution from your JV at this stage or when do you see it, now that we have some traits being developed, on your EBIT line?

**Manfredo Rübens:** On the Monsanto question: You know that we are just accessing the market with the first product, DroughtGard. It's in the market, it's starting. It has a good start, but the contributions to the bottom-line at this point in time are still small.

### 3.5 Oil & Gas

**Ronald Köhler (MainFirst):** Good morning! If I may, I'll ask for a slight outlook for the second quarter in Oil & Gas. Obviously, you informed us that you shifted this offshore lifting into the second quarter. Would that imply that I just can add 100 million on Q1 and that is roughly what I should expect for the second quarter in Oil & Gas, ex oil and gas exploration, excluding gas trading obviously?

**Dr. Hans-Ulrich Engel:** I like your question, but I don't want to fill your spreadsheet. As you know, we don't give specific guidance on quarters. We give full-year guidance and we don't give specific guidance on quarters in specific segments.

Oil & Gas: Indeed, we have a disappointing result there in Q1, for a number of reasons that I am happy to explain if that is of interest.

One of the key drivers is that in fact we expect the offshore lifting in Libya – by the way, offshore production in Libya continues, is unaffected by the strikes which led us to shutting in our onshore activities – we had in Q1 of the year 2013 and we expect now in Q2 of the year 2014.

Then, as I am sure you will do, you will factor in that in our gas trading business Q2 certainly does not seasonally benefit – let me put it that way.

**Ronald Köhler (MainFirst):** Okay. Could you highlight a bit what happened in Q1 and what was disappointing from your perspective beside Libya?

**Dr. Hans-Ulrich Engel:** Let's start with Libya. Onshore activities shut in, so no contribution in Q1 from Libya onshore, no earnings contribution from Libya offshore, as already explained.

Third, in euros, the oil price dropped from 85 in Q1 2013 to 79 euros in Q1 2014.

Fourth, in our natural gas trading business we have the impact from the warm winter in North Western Europe, meaning significantly less volume, but also a much weaker margin than what we had in Q1 of the year 2013.

Then also, with respect to earnings, on the negative side: As you know, we deconsolidated Gascade. As a result of that, we now only show the equity earnings of Gascade in Q1 2014. On the positive side, we have the contributions from the asset swap that we have done with Statoil last year. But that by far does not outweigh all the negative impacts that we experienced in Q1.

**Andreas Heine (Barclays Capital):** I'd like to come back to the Oil & Gas segment. After the consolidation of the Statoil fields, there were many moving parts in this segment. But basically, the Statoil earnings never showed up, at least in the reported numbers. Are these Statoil fields on track? If everything runs more normal in the coming quarters, do we see contributions here or is something worse than you expected at the beginning?

**Dr. Hans-Ulrich Engel:** No, absolutely not, Andreas. As you know, we acquired the activities on 1 July of last year. They deliver what they are supposed to deliver, which is in the range of 35,000 to 40,000 barrels per day. We are happy with the production, with the development there. The Statoil activities that we acquired are delivering perfectly in line with what our expectations were. And you should see the respective contribution.

I explained the distortions that we have in Q1. Look at the E&P business: If I get my numbers memorized correctly, I think we are down there by 36 million in EBIT before special items and this despite the fact that we don't have the offshore lifting from Libya in Q1 and despite the fact that the oil price dropped in euros from 85 to 79. You already see there that there is a nice contribution coming out of the acquired Statoil activities.