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1 BASF Group

1.1 Upstream business environment

Laurent Favre (Exane BNP Paribas): On that normalization in the upstream: You still assume that conditions will normalize which is less than before. I was wondering if you could give us a bit more color on the various moving parts of your assumptions.

In particular, do you see now the risk of further normalization into the first half of 2022, or do you think that that scenario is off the table? If you could separate, I guess, Chemicals and Materials in your comments, that would be great.

Dr. Martin Brudermüller: First of all, let me say that the conditions for the Chemicals and the Materials segments in the second quarter overall were better than in the first quarter. That was coming on the one hand from very strong demand because in all the different businesses, there is solid demand globally. I think the world has been a little bit surprised by low inventories and then big business.

And then we have also the supply chain topics. In some of the markets – because of the supply chain issues and the shortage of containers – there is not in every business an arbitrage opportunity from one region to the other. So partly they are a little bit more segregated markets. And that's also why everything reacted quite sensibly in a pattern and also where some of players in the major commodities had supply problems, even coming back to the big freeze in the US, which took weeks and partly until today to normalize and to work down the backlog.

If we look at a lot of the margins, I have to say: We really have super margins at the moment, being on a very high level. It's just not right to assume that this is going to stay forever. I mean, if you look at products like acrylic acid, but also BDO, MDI, and TDI, this is on a high level, simply with the effect that in some areas the supply normalizes and even if the demand stays strong, you just have a certain relaxation of margins.

I expect, however, that even in the second half, there still is a solid margin level. It's not record margins anymore, but still very good margins. For that reason, we have to figure into our numbers that there is a certain normalization. You know how sensitive that is. I mean, in the MDI case, one of the competitors has a force majeure and then immediately prices react. So that is always, some ace up one's sleeve, that there could be some unfortunate or unplanned outages which would change the situation. But overall, I mean, margin levels are so high compared to the last five, six years that they have to go down to a certain extent. But that should not signal that they are now totally collapsing. It's just a normalization.

Laurent Favre (Exane BNP Paribas): And past the level of H2? The risk beyond that H2 normalization you are factoring in in your guidance. You would still say that they are at normal in your new guidance, in your new scenario for H2 for this year?

Dr. Martin Brudermüller: Yes. This is what I said. We have factored in a high level of margins, but not as high as in the first half of the year.

Andreas Heine (Stifel): In Q3 in Chemicals, if I look to the prices, I would say, on average prices might be even higher than in the second quarter. Is there anything I miss if you look at what you see for that particular segment in the current quarter?

Dr. Martin Brudermüller: A short answer on the Chemicals margins: If you look at some of the margins, they already at the end of Q2 turned down a little bit. If you see MDI and TDI in Asia, caprolactam more flat and some others also, let's say, started to normalize already a little bit. That's why we expect simply with the higher availability that this is going to continue. If I then do the math, I would say, in Q3 on average margins are a little bit lower than they had been in Q2.

Chetan Udeshi (J.P. Morgan): It seems you are alluding to maybe a slight reduction in margins in the upstream businesses. So should we take that as a sort of guide for what Q3 could be in terms of earnings, maybe a slight reduction from Q2 levels of around €2.4 billion? Or do you think that there are some other factors we need to take into consideration when thinking about Q3 versus Q2?

Dr. Martin Brudermüller: We alluded to it already, it is a certain normalization. If you look at some of the margins, they are just not healthy at the moment. They are so high that you cannot expect that customers overall stay with those. With a better supply, it is just immediately reacting to go down.

But, as I said, it is still a margin in most of the chains which is far above their normal average. It is still a very attractive margin.

There is one element coming in, seasonality, in some areas and that is always factored in. The BASF pattern has that as well that in summer months sometimes they draw a little bit less because some of the companies also shut down or reduce production rates, or go down with the number of shifts or something like that.

I think that is also now going in the same direction that it is simply normalizing. But consider that these are still very attractive margins in the commodity area.

1.2 Guidance and capex

Jaideep Pandya (Onfield Research): Going back to the CMD you did in 2018 where you gave the 3% to 5% EBITDA, sort of CAGR target and obviously at that time flagged that this is not going to be easy.

As of today, you're probably going to do almost all the CAGR in 2021 if EBITDA is close to roughly €12 billion, based on a €9 billion base of 2018. So I just want to understand, as we think about life ahead for BASF, how sustainable is this earnings level today? Do you think that, basically, if you add all the sort of overearning you're doing in certain upstream areas versus some of the investments/underearning that is in the downstream areas, there's still room to grow from the current profitability level of roughly €12 billion, or is it really an exceptional year this year and, therefore, we should actually be thinking about some moderation in the outer years and therefore go back to this more like a 3% growth rate level rather than the 5% growth rate level in terms of the range?

Dr. Hans-Ulrich Engel: With the new corporate strategy that we launched at the end of 2018, we announced a number of measures. These measures included the divestitures that I talked about briefly, so in other words: changes in the portfolio, upgrading the portfolio overall. It included certain cost measures which we have put into what we call the Excellence Program, on which we will deliver, as you will see, by the end of this year, I have no doubt.

We have put a strong focus on the customer where some of you have asked me over time: Well, Hans, shouldn't an organization like BASF be always focused on customers? And how I said the same. – Yes, absolutely. But at times it may make sense to put even more focus on customers and with that also fuel more growth in BASF.

As Martin has explained, as it looks both in Q1 and in Q2, our growth – and this is measured in volume – is stronger than volume growth overall of the chemical industry. We've implemented a number of other measures in the meantime. That should all help us to increase profitability of the BASF Group.

Let's see whether this one year will be the catch-up year and form then the new baseline for the 3% to 5%. But as Martin and I sit here, we are firmly convinced that the BASF Group is able to deliver that and we will do everything to actually also fulfill the promises that we made there.

Andrew Stott (UBS): On capex. I wonder if you could give us an update now on capex for 2021, 2022 and 2023 on the basis of Vattenfall coming in. So I assume you have got to take about half of that 1.3 billion of capex, but I just don't know the phasing on that.

Dr. Martin Brudermüller: I would say we are so far very well on track and I think also the €3.6 billion for this year, we will most probably spend that amount.

Going forward with capex: In 2022, 2023, capex is stepping up. That is what we always said because then the big investment in China, in Guangdong province, will come in.

I cannot give you detailed numbers now. We will do that with the next five-year numbers where we can then also provide a little bit more outlook on how that will develop and how steeply it will increase. By then we will also show you a bit more on what we intend to do in battery materials.

These are both drivers. But at the same time, we are very stringent and very disciplined in the allocation for all the other businesses. So I would say, it doesn't bear any surprises. But give us some more time to provide more detailed numbers.

Tony Jones (Redburn): With EBIT this year, the new guidance, it's going to be well over €7 billion. How are you thinking about returning any excess cash to shareholders in a peak earnings year or are you favoring growth investments and strategic M&A?

Dr. Hans-Ulrich Engel: So, first of all, let's bring the year home, number one. Number two, you know what our priorities are for the use of cash and they have not changed.

1.3 Further corporate topics

Andrew Stott (UBS): What are your thoughts on the proposals from the "Fit for 55" program? Where do you think Chemicals ends up being within the EU carbon border adjustment mechanism (CBAM)? And if so, what are the implications for BASF's decarbonization strategy, if any?

Dr. Martin Brudermüller: The "Fit for 55" package is a package which you have to digest first. It is more than 3,000 pages of regulation; quite amazing, I have to say, not so many surprises.

We have also been able, in the dialogue before to change the one or the other thing to a minor heavy impact. But it is still a heavy package. It is a 55% reduction, which I think was clear to everyone that this will come. It has also translated in the meantime into a stricter climate law in Germany, which is also accelerating this path and into even more reduction in a shorter period of time.

So, actually, there are no big surprises and that is all factored in into our plan, which we have shown you at our Capital Markets Day in March.

I am personally very critical of CBAM. I think it is just not going to work. It is not only the WTO compliance, it is a very bureaucratic piece, because if you apply that to chemistry and you just think about how value chains are branching out, you have to know for each and every product that is imported and exported what actually the fair CO_2 carry is. I think it is almost impossible.

That's why we in the CEFIC, which is the European association for the chemical industry, have actually decided not to hunt for participation in the CBAM, but rather let that first be tested in other big commodities.

So, there are now five commodities and there is only one from the chemical industry in, which is ammonia, which is a relatively easy-to-understand commodity, and with that also the fertilizers. So, it will affect us, not dramatically , but certainly we are also a large ammonia producer.

You also know that with CBAM, the free allocation of CO_2 certificates will be reduced starting in 2026 to go down to zero by 2035 [corrected]; that is a major burden on cost. But that really hits the whole industry.

I think it is a good example to now learn how that actually impacts export and import and also certain value chains. It is a starting point of a long, long journey with a lot of question marks.

I can only repeat myself here: If you really want to manage that and convert that into an advantage, what I think we can do, we need a lot of dialogue that overall regulation is positive. So far, "Fit for 55" is actually a wish list what they want to do. But it is not a list of regulation to help us realize those targets.

So, maybe we have some more time in future; then I will talk more in detail about that.

Matthew Yates (Bank of America): I wanted to ask you what the strategic options are for the Wintershall Dea asset and how we can avoid this becoming somewhat of a stranded asset if the market continues to be resistant to valuations in the oil and gas sector. Other than an IPO, are you also exploring options for a trade sale or could you even contemplate some sort of spin-off to shareholders, if given the improvement in the rest of the business? You are making good progress on deleveraging anyway. So could you simply just spin the asset off?

Dr. Hans-Ulrich Engel: Wintershall Dea, a stranded asset? I would say, definitely not. We made a conscious decision here, seeing where the broker prices were. When it comes to valuation and when it comes to valuation for an IPO, what is at this point in time in particular of relevance are the years 2022, 2023, 2024. We saw the strong move on the front end of the curve, but 2023 and 2024 were clearly lagging behind. It's slightly improving, as we had expected. It also looks like the multiples are improving. So from that point of view, I think we made economically here the right decision.

Are there alternatives? I can tell you that between the shareholders we have agreed on a path for an exit, which is the IPO, and we'll continue on that path. Let me also reiterate what I said during my brief speech earlier: The strategic decision for BASF is absolutely clear. As we have implemented on the divestitures of the water and paper treatment chemicals business, the construction chemicals business, the pigments business, we will also implement in this case.

2 Segments

2.1 Chemicals

– no specific questions –

2.2 Materials

– no specific questions –

2.3 Industrial Solutions

Christian Faitz (Kepler Cheuvreux): On Performance Chemicals: The price momentum is relatively weak compared to any other traditional chemicals segment. Is that because of the late cyclicality of your customer industries, i.e. oil and gas, etc.?

Dr. Hans-Ulrich Engel: If you look at the Industrial Solutions segment, we have an overall price increase there of 9% in Q2. That does not fully compensate for the kind of raw material price increase that we have.

But again, the general explanation that I gave earlier is true here. If you are moving a step downstream from our two upstream segments, i.e. Chemicals and Materials, it just takes a little longer to pass on the prices.

But I'd say, overall a nice, strong performance that we have seen there.

2.4 Surface Technologies

Jaideep Pandya (Onfield Research): Around your battery business: Obviously, you've announced a big joint venture in Shanshan. How do you actually unlock value in this business from a capital markets point of view? In the longer term, do you plan to sort of separate this business with a focused strategy or do you intend to just keep it in BASF? Is this going to be an important part of your strategy? But it is always going to be for the capital markets to assert a value to it?

Dr. Martin Brudermüller: Regarding your question about the battery materials business and our acquisition in China. You know that we have a footprint which includes North America, Japan and now with the investment also Europe. But we have no capacity in China so far. And this is the largest market at the moment.

This chain is moving fast, I would say. Over all the different steps of the value chain, there are new alliances, there is a lot of investment coming up, giga factories, material factories, also investments in mining.

It is very important to also have a position in China because the Chinese suppliers are currently delivering a major part of the material for the value chains globally. It allows us to also link in very quickly via Shanshan's position into some of these opportunities.

On the other hand, you see that when we bought ourselves into this enterprise, also Shanshan was interested because the world is not only China anymore. They also want to get more access to the European markets. I think, with this investment, we have a good opportunity to really exploit all the different constellations and setups you have in this value chain worldwide.

And don't forget that we also gain very quick access to additional capacities, because now we will be really a big animal, the only one, by the way, to have a global footprint. We have 160,000 tons of capacity coming at the end of 2022. That gives us the opportunity to grow very quickly and to build up these new alliances and customer bases and react very flexibly to the demands of the customers.

As I said, this is all very dynamic. With Shanshan, I think, we can accelerate growth, we can build on our position and we can enlarge our customer base. We should be able to also unlock value quickly in this business.

Charlie Webb (Morgan Stanley): As we look at the auto sector, maybe you can just provide us a bit more detail in terms of what you're seeing into the second half and in particular how that relates to Surface Technologies.

Clearly, it seems registrations are still very positive on the automotive catalyst side, as well as precious metals, obviously helping out in Q2. How do you see Surface Technologies through the second half of the year?

Dr. Martin Brudermüller: I think I said already in February that the semiconductor issue is not an issue and a blip for one or two quarters, but it is a longer-term problem. I think it turned out that I was right.

We clearly reduced our assumption for cars produced. We are currently thinking about 83 million units to be produced this year. So that is definitely lower. We have, however, been surprised that Q1 was stronger than anticipated, with about 800,000 units. But that means for the other three quarters it is actually a minus of ~1.3 million units.

The second half will be a little bit weaker respective the opportunities. And that has nothing to do with demand because the demand is strong. You see, also in the U.S., the inventory of cars is really low. You see that the delivery times of OEMs increased.

So it is really a semiconductor shortage that is the root cause not to produce more cars.

This overall move into e-mobility is very exciting because now more and more of the players are accelerating their plans to change from combustion engines to e-mobility. I think it's a very clear commitment. It's a proof point that we have been right with our assumptions for battery materials. That develops very dynamically.

But let me also say: We have a lot of other projects that are connected with e-mobility because a lot of things are differently constructed in a car that has an electric powertrain. Overall, there's much more chemistry in terms of value in a car that is electrically driven than by combustion. So overall, that is really good news for a supplier like BASF.

Let me give you one example: If you think about the different fluids you need in a car, you think if you don't have a combustion engine, you don't have to cool it anymore, that you actually need less fluids. It's exactly the opposite. You need about three to four times more fluids to also cool the battery. So there's a lot of opportunity and a lot of the projects we pursue gain higher attention and faster execution than we thought. So overall, a quite challenging, but also a very interesting and dynamic development.

Charlie Webb (Morgan Stanley): Just on Surface Technologies in terms of the automotive catalyst business, the strong first half. I am just wondering how that looks into the second half, how far are we along in that kind of regulation upgrades in Asia, in China?

Dr. Martin Brudermüller: Overall, still for the years to come, the combustion engines have the big market shares here. There is also Euro 7 and China 7 coming up further intensifying regulation. That still drives innovation. We need new catalyst systems. We have to adapt. So I would say, over the next years, that is still a good business.

Peter Clark (Société Générale): I think you have alluded to this, but it is the flip side of the super profitability upstream. I am looking at the lag effect you are talking about downstream, passing some of this stuff on. I know there are different inputs.

Take Coatings for an example: Some of your peers are talking about peak impact of the inflation, probably in terms of Q3 and stabilization from the winter and then perhaps gentle moderation, the supply disruptions easing.

I am just thinking if your thoughts are similar to that and how it might impact some of the businesses being squeezed at the moment as well.

Dr. Hans-Ulrich Engel: I'd say, in general, we have a similar view. Martin described what our expectations are for Q3, second half of the year for prices in upstream.

The Coatings business is typically a business where it also takes definitely longer than upstream to pass on the price increases.

Despite the semiconductor issues that we have, demand overall is good and strong, which is also reflected in the results of Q2 and the first half of the year. But there is definitely some work to be done on the price front.

Dr. Martin Brudermüller: Just to add: Let's not get depressive now if we are at the peak. We enjoy it as long as we can.

As I said, if you talk about normalization, this is not collapsing margins. As long as the demand stays healthy – that is what we can see also from the order entry levels, I think there is no reason for too much concern.

Chetan Udeshi (J.P. Morgan): Can you remind us what is the existing sales and profitability of your cathode active materials business right now?

Dr. Hans-Ulrich Engel: On the battery materials business: As you know, we don't provide the financials for our strategic business units. But what I can tell you is that this is a nicely growing business and it certainly grows in line with the overall growth that you see in electro-mobility.

Sebastian Bray (Berenberg): What exactly was the purchase price that BASF paid for the 51% stake in the Shanshan materials business? Was it about US$650 million? Why was this not disclosed?

What is the total organic capex investment that BASF will make in battery materials to reach the 160 kilotons by the end of 2022? The company has previously disclosed €400 million in Europe. How much on top of that will come to reach the 160 in total?

Dr. Martin Brudermüller: On the second part with the battery materials investment: We have currently our European battery materials investment, which is in execution, which will then be finalized next year.

All the other parts that are actually coming in now are coming in via China. So, there is no other capacity expansion at the moment in the numbers from our side.

Dr. Hans-Ulrich Engel: With respect to the price, we have given you what we can give you, following the agreements that we entered into. So I can't tell you more than that it is a mid-triple-digit million-euro figure.

Sebastian Bray (Berenberg): Was it a condition of the agreement that you signed with the shareholders of Shanshan that the price not be disclosed?

Dr. Hans-Ulrich Engel: These are the usual confidentiality rules that are in place and, as a result of that, we haven't disclosed more than what we just said.

2.5 Nutrition & Care

Markus Mayer (Baader Bank): What was the magnitude of the start-up cost in Nutrition & Care and this vitamin A plant?

Dr. Hans-Ulrich Engel: On the start-up cost that we have in Q2 in Nutrition & Care for vitamin A: I give you a rough figure; that's between €20 and €30 million. Keep in mind, though, that this is the start-up effect that I am talking about. We also had a number of turnarounds on which we typically don't specify the respective cost. But that's also something that plays a role when you look at the results of Nutrition & Care.

Christian Faitz (Kepler Cheuvreux): Can you please elucidate the price pressure, particularly in Nutrition & Health, which is consistent since Q2 last year? Is that mainly coming from the vitamin side?

Dr. Hans-Ulrich Engel: Yes, there is some price pressure. There is also something else and that is raw material cost pressure that we need to keep in mind here.

You know how this works. Our upstream segments pass on any type of price increases on the raw material side relatively quickly; I tend to say, within 30 days. The further you go downstream in the portfolio, the longer it actually takes and that is something we typically see. You know how it is when prices go up; you see the kind of margin pressure that we have. When raw materials prices come down, you'd see typically the margin expansion, and that is exactly what we have here.

Maybe one more word to put things in perspective. For Nutrition & Health, please also keep the comparable figure in mind, which is extremely strong. You may recall that last Q2 we talked about the resilience of the business, the very high demand that we had seen, particularly in the months of April and May 2020, the pre-buying that took place there. I think all that needs to be factored in to put overall Nutrition & Health in the right light with what we consider and admit is a weak quarter.

2.6 Agricultural Solutions

Markus Mayer (Baader Bank): Regarding the product mix effect you experienced in your Ag division, can you maybe also shed some light on this effect as well?

Dr. Hans-Ulrich Engel: The product mix in Ag, what do we have there? In Q2 of last year, which had to do with weather development, we actually had still higher sales, in particular in seeds and traits than we had in Q2 of this year. The seeds and traits business is a higher margin business than the crop protection business. That plays a major role in the product mix and the resulting outcome.

Let me say in addition to that: If you look at the earnings – this is on the EBIT before special items level – of Agricultural Solutions and if you look at the currency effect that we have in there, somewhere between €40 million and €50 million, that is actually the key explanation of the decline in results that you see. If you add that back, you have a quarter at the same level where we were last year.

Matthew Yates (Bank of America): You are making substantially less profits in the quarter than you did a few years ago, before you acquired the Bayer assets.

So, when we think about the moving parts you've talked about, is it really foreign exchange that's the big problem? When you talk about higher fixed costs, is that specifically relating to freight or is that something more of an investment in the business that maybe we see some return on going forward?

Dr. Hans-Ulrich Engel: We talked about the significant FX effect that we have, that burdens the earnings of Ag. I mentioned already: Without that, we would have been at the same level as in Q2.

There is one very simple explanation for that, which is the U.S. dollar which was sort of locked in at 1.10 in Q1 and Q2 of last year and we have it slightly above 1.20 in Q2 of this year. This is also something to be kept in mind when you compare then later on, once our competitors report and report their figures in U.S. dollars. At this point in time, it's simply the disadvantage of showing the numbers in euro terms.

Yes, we have increased fixed cost, as Martin has explained already. Pulling through higher volumes means also that your fixed manufacturing cost increase. We have, in line with the higher volumes, also higher selling cost and, as part of that, also higher freight cost.

And then we have something that is also true; I mentioned this already. It isn't in the fixed cost, it's in the variable cost, but significant increases in raw material prices, in part in situations where prices for the products are fixed at the beginning of the season. And these raw material prices then hit you during the course of the season.

Laurent Favre (Exane BNP Paribas): On the Ag side: Compared to February, when you issued the guidance for slight EBIT growth, there are new moving parts on higher costs and better soft commodities, I guess, currency finishing now slightly better. If you net all of those new incremental things, do you still think you can grow EBIT slightly in Ag for the full year?

Dr. Hans-Ulrich Engel: Yes, we had expected to be slightly ahead of half one last year. We are in fact down by an order of magnitude of €45 to €50 million. Things have actually, from raw material cost to currency, not gone in our favor.

It remains to be seen how the second half will develop. You know that this is seasonally weaker than the first half of the year. It is predominantly the business in South America. We need to see how this will go. It looks definitely more challenging now than it looked when we gave the guidance in February.

Andreas Heine (Stifel): In Agro, we have seen commodity prices being very much up, but no one in the crop protection and seed business could react on this as the season was already running. So now I guess everyone is hoping for price increases, especially for the second half in the Latin American season.

Is there anything you can share with us on these price increases for LatAm in the second half, especially also to offset what you have lost on the currency last year?

Dr. Hans-Ulrich Engel: Your summary was spot on: FX needs to be taken into consideration for the business in the southern hemisphere, increased raw material prices have to be taken into the equation. I think that will also be reflected in the pricing policy.