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DuPont de Nemours, Inc. (DD)

Q4 2020 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by. And welcome to the DuPont Fourth Quarter 2020 Earnings Conference Call. At this time, all participants are in a listen-only mode, and later we will conduct the question-and-answer session. Thank you.

I would now like to turn the call over to Leland Weaver to begin.

Leland Weaver

Vice President-Investor Relations, DuPont de Nemours, Inc.

Good morning, everyone. Thank you for joining us for DuPont's fourth quarter 2020 earnings conference call. We're making this call available to investors and media via webcast. We have prepared slides to supplement our comments during this conference call. These slides are posted on the Investor Relations section of DuPont's website, and through the link to our webcast. Joining me on the call today are Ed Breen, Chief Executive Officer; and Lori Koch, our Chief Financial Officer.

Please read the forward-looking statement disclaimer contained in the slides. During our call, we will make forward-looking statements regarding our expectations or predictions about the future. Because these statements are based on current assumptions and factors that involve risk and uncertainty, our actual performance and results may differ materially from our forward-looking statements. Our 2019 Form 10-K, as updated by our current and periodic reports, includes detailed discussion of principal risk and uncertainties which may cause such differences.

Unless otherwise specified, all historical financial measures presented today exclude significant items. We will also refer to other non-GAAP measures. A reconciliation to the most directly comparable GAAP financial measure is included in our press release and posted to the Investors page of our website.

I'll now turn the call over to Ed.

Edward D. Breen

Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

Thanks, Leland, and good morning, everyone. I will provide comments on the tremendous progress we made on several strategic priorities during the fourth quarter of 2020 and the start of 2021. But first, let me give my appreciation to our employees and partners around the world who rose to the occasion, day-after-day, in the face of extraordinary circumstances.

2020 presented us with the challenges of a global health pandemic, social and political unrest, and the worst economic conditions in many years. Despite these challenges, our team's remained focused on health and safety, delivering for our customers, strengthening the financial position of the company, and continuing to drive our strategic priorities forward. It is because of our commitment of our employees that today we are able to announce strong financial results as well as significant progress on critical milestones to make DuPont a premier multi-industrial company equipped for growth and value creation.

Starting on slide 2, on February 1, we announced the completion of the merger of our N&B business with IFF, creating an $11 billion industry-leading company in the food and beverage, home and personal care, and health and wellness markets.

The new IFF will have unmatched capabilities to deliver for customers with leading positions in markets such as nutrition, probiotics, soy proteins, flavors and fragrances. The combination of these complementary portfolios puts IFF at the forefront of highly valued consumer ingredients companies that work closely with customers to meet the growing demand in areas such as all natural, clean label and sustainability.

The combined management team has planned and prepared for this integration and they are committed to delivering for all stakeholders. They are already executing on a playbook to capture both the cost and revenue synergies enabled by the combination. I am now on the IFF board, and I look forward to coming into the lead director role this spring to continue overseeing the transformation of IFF. This transaction also unlocks significant value for DuPont and our shareholders.

Earlier this month, we received about $7.3 billion in cash, which enables us to further strengthen our balance sheet by reducing our long-term debt and gives us the flexibility to continue generating shareholder value. As you know, we separated the N&B business through a split off transaction, in which DuPont shareholders were given the option to tender their DuPont shares in exchange for shares in IFF at a ratio of 0.718 shares of IFF for every share of DuPont.

The exchange offer was fully subscribed and all shares that were tendered were retired by DuPont, resulting in a reduction of 197 million shares or approximately 27% of our outstanding shares. This was a very efficient process for DuPont to get shares out of the market with zero cash outlay.

In closing, customers are excited about the potential this strategic combination can deliver in terms of being a partner of choice, R&D capability and innovation. Additionally, our N&B colleagues are energized by the opportunities before them and we wish them continued success as they embark on this exciting new journey.

Slide 3 highlights the impact of other actions we took throughout 2020 to strengthen our balance sheet and positioned the company to continue generating shareholder value through a disciplined financial policy.

As Lori and I came into our roles in February of last year, and with the initial indications of a global pandemic soon thereafter, we quickly implemented actions to improve working capital and [ph] tension (06:05) capital expenditures across each business and function. We achieved an $850 million improvement in working capital and reduced capital expenditures to $1 billion, a reduction of nearly $300 million from our initial targets for the year. Combined, these actions enabled free cash flow conversion of more than 150% for the year.

These actions combined with proceeds from Non-Core divestitures enabled us to close the year with zero commercial paper balances, a reduction of more than $1.8 billion. We expect to further reduce our debt balances by using $5 billion of the cash received from the IFF deal. We have already retired our $3 billion term loan and plan to redeem the $2 billion notes in May.

We closed the year with greater than $2.5 billion of available cash. And as I mentioned, we expect to have $2.3 billion of cash remaining from the IFF transaction. Combined with the continued strong cash generation and further proceeds from Non-Core divestitures, we are heading into 2021 in a very favorable liquidity position, with no debt maturities due until the fourth quarter of 2023.

As we look to uses of our available cash in 2021, our financial policy will remain disciplined and balanced, maintaining a strong balance sheet, growing the company through investments in CapEx and R&D, acting on strategic M&A targets and returning value to our shareholders. We remain committed to maintaining our strong investment-grade credit rating and are pleased that we have a stable rating from all the major agencies. We also look to continue our CapEx at about 5% of sales and R&D spending at about 4% of sales for 2021.

With regards to dividends, we intend to maintain our current quarterly per share dividend of $0.30 per share. Going forward, we will target a payout ratio between 35% and 45%, and we will work with our board to increase our dividend annually as we grow earnings.

Finally, share repurchases remain an important component of our financial policy, and we intend to resume buybacks utilizing our existing plan, which still provides authorization up to $1 billion. We are also actively evaluating a couple acquisition targets, which will enable even further acceleration of growth in key end markets. As we move through the year, we will redeploy our excess capital in ways which maximize shareholder value.

Turning to slide 4, we also recently signed agreements to sell our Clean Technologies and Solamet businesses, and we expect these transactions to close by mid-2021. Combined with the sale of the Biomaterials business, we anticipate more than $900 million in pre-tax proceeds from Non-Core divestitures this year.

Our priority of active portfolio management has focused our portfolio and generated significant cash for the company. Since June 2019, we have divested or signed agreements to divest nine businesses in addition to the separation of N&B, generating over $2 billion in gross proceeds. Additionally, exiting these businesses removes a significant amount of cyclicality from the DuPont portfolio and eliminates much of the volatility that was often in our Non-Core results.

With the agreements on Clean Tech and Solamet, we have divested a substantial portion of the Non-Core segment. We will wind down the Non-Core segment reporting in the first quarter of 2021 and report our results in three reportable segments going forward as we announced last week. I'll ask Lori to provide more color on our new segments as well as detail on our financial performance. But let me close with a few comments on the settlement agreement that DuPont and Corteva reached with Chemours.

I am pleased that we have reached an agreement that I believe is in the best interests of all three companies. For DuPont there were a few key principles. First, it was important that any settlement agreement capped our share of any potential liabilities at a defined amount. We also [indiscernible] (11:03) long-term agreement with the building of an escrow account over the term to provide stakeholders of all three entities the confidence that the parties to the agreement will be able to satisfy their respective obligations if they were to materialize in the future. The agreement we announced met these principles and was a key step in reducing the uncertainty around potential legacy PFAS liabilities.

The other aspect of what we announced a few weeks ago was the settlement of the remaining Ohio multi-district PFOA litigation. Our portion of the settlement is $27 million. To be clear, we continue to believe any exposure for DuPont related to potential legacy PFAS liabilities is contained due to [ph] heritage (11:56) DuPont's limited manufacture and use of PFOA and the fact that we never made firefighting foam. Having agreement with Chemours and Corteva enables us to work together as we move forward.

With that, let me turn it over to Lori.

Lori D. Koch

Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

Thanks, Ed, and good morning. With the completion of the N&B transaction on February 1 and the substantial progress we made on Non-Core divestitures, we announced our new segment reporting structure for DuPont going forward. We will be aligned around three business reporting segments: Electronics & Industrial, Water & Protection, and Mobility & Materials. Our new segment structure combines businesses with common financial characteristics, enabling clear line of sight and more effective allocation of resources across the company. Each business has a meaningful growth profile with a management team that understands how to best execute on its priorities and deliver for shareholders.

We will move the following businesses to the newly named Electronics & Industrial segment: Kalrez, Vespel, medical silicones and MOLYKOTE each previously reported in our T&I segment. We will move the Teijin Films joint venture, the Microcircuit Materials business, and the Tedlar business to our T&I segment, which will be renamed Mobility & Materials. Each of these was previously reported in our Non-Core segment.

Safety & Construction will be renamed Water & Protection to highlight our market-leading water business that we have grown both organically and inorganically over the past few years. As Ed mentioned, we will wrap-up the Non-Core segment, as part of our first quarter reporting. We will report the results of the Biomaterials, Clean Tech and Solamet businesses in our corporate segment until the divestitures are complete.

I'll cover our fourth quarter results on slide 6. As Ed did earlier, I'd like to acknowledge the significant efforts of our teams in delivering a strong fourth quarter, a capstone to what was an incredibly productive year. We set working capital and CapEx targets and challenged our teams to enable the reduction of commercial paper balances to zero at year end to improve our leverage heading into 2021. Our teams delivered once again.

Net sales of $5.3 billion were flat versus the fourth quarter of 2019 on an organic basis and ahead of expectations we had set at the start of the quarter. Demand for our technologies in smartphones and semiconductors remained robust through the quarter, with no seasonal decline in smartphones as we typically see in the fourth quarter.

Also contributing to the strong fourth quarter with further recovery in the automotive market. At the start of the quarter, industry benchmarks suggested fourth quarter auto builds would be down low single digits. However, with over 23 million automobiles produced globally, the fourth quarter was the strongest production quarter of the year, up 3% versus the fourth quarter of 2019, and up about 14% versus the third quarter of 2020. Our team's navigated a challenging raw materials environment across the polymer space to deliver volume growth in line with auto build on both a year-over-year and sequential basis. The end markets within S&C were very similar to the third quarter and consistent with our expectations.

Demand for our protective garments continues to be strong, with garment sales up nearly 50% versus the fourth quarter of 2019. The aramid side of our Safety business was up versus the third quarter on a sequential basis but continues to see year-over-year declines in volume, as a result of the pandemic impacting demand for aerospace, oil and gas and other select industrial applications. Similarly, the environment Shelter Solutions remain consistent with what we saw in the third quarter, with strength in do-it-yourself applications and continued recovery in residential construction offset by softer commercial construction demand.

Shelter sales were up slightly on an organic basis in the fourth quarter and demand for water filtration technologies remained strong across the world, however, in our fourth quarter results, were impacted by the timing of some shipments at year end resulting primarily from orders associated with capital projects. We will capture this demand in our first quarter results and return to mid to high single-digit growth. Likewise, results for

the N&B segment were in line with our expectations with ongoing demand strength probiotics and home and personal care markets offset by the continued softness in biorefinery and microbial control.

From an earnings perspective, we also delivered a strong quarter, driven by improved volumes and the delivery of approximately $130 million of non-manufacturing cost savings, which enabled expanded EBITDA margins in each of our core segments in the quarter. Excluding approximately $160 million of discrete gains in the fourth quarter of 2019, we delivered operating leverage with mid single-digit operating EBITDA growth.

From a segment perspective, E&I delivered operating EBITDA margins of 31.6% on strong volumes and cost reductions. T&I delivered 310 basis points of operating EBIT expansion on higher volumes, tight cost control and lower raw material costs offset by year-over-year pricing pressure. Likewise, S&C drove operating margin expansion of 40 basis points through cost control and favorable product mix more than offsetting the impact of lower volumes.

N&B operating margins expanded 100 basis points versus the fourth quarter of 2019 led by favorable product mix and non-manufacturing cost control, more than offsetting raw material price increases and costs associated with the planned slowdown of production across the N&B network to properly manage working capital.

Adjusted EPS of $0.95 per share was flat with a prior year. Savings from both structural and temporary cost reductions and benefit from a lower tax rate were offset by pricing headwinds and headwind of approximately $0.17 associated with the prior year discrete items.

We also delivered robust free cash flow in the fourth quarter, driven by controlled CapEx and working capital improvements. We closed the year with CapEx on target at $1 billion and approximately $850 million in working capital improvement, well above our target of $500 million for the year. Looking forward over the medium term, we continue to believe we have additional opportunity to improve our working capital turnover, primarily through better supply chain management through the use of data analytics.

Slide 7 provides our financial outlook for both the first quarter and full year 2021. Our guidance reflects DuPont on the new basis, excluding N&B, as it will be reflected at discontinued operations when we report our results. We have provided recasts first quarter and full year 2020 results, excluding N&B, for comparison purposes. Later this month, we will release fully recast segment results for 2018 and all quarters in 2019 and 2020, reflecting the segment realignment, the elimination of the non-core segment and reflecting N&B as discontinued operations. Our guidance also includes a full year of results for the three non-core businesses we have signed agreements to sell, and we will reset expectations as they close.

For the full year, we expect net sales of $15.4 billion to $15.6 billion, an increase of 8% at the midpoint, and operating EBITDA of $3.83 billion to $3.93 billion, an increase of 13% at the midpoint. We expect operating EBITDA margin improvement of approximately 100 basis points, driven by the impact of improved volumes and the remaining benefits of our structural cost actions we put in place last year. These gains will be partially offset by anticipated return of some 2020 temporary cost reductions.

Adjusted EPS of $3.30 to $3.45, an increase of 68% at the midpoint versus 2020 adjusted EPS of $2.01 per share, reflects stronger segment earnings and lower interest expense, which is enabled by the paydown of our debt balances, including commercial paper. Our adjusted EPS also reflects the reduced share count resulting from the exchange offer that closed on January 29 in connection with the separation of N&B. As a reminder, this took out about 197 million DuPont shares. This results in a weighted average share count for the year of 555 million, which excludes the benefit of any future buybacks.

With that, let me turn it over to Leland to open the Q&A.

Leland Weaver
Vice President-Investor Relations, DuPont de Nemours, Inc.

Thanks, Lori. Before we move to the Q&A portion of our call, I would like to remind you that our forward-looking statements apply to both our prepared remarks and the following Q&A. We will allow for one question and one follow-up question per person. Operator, please provide the Q&A instructions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from the line of Jeff Sprague of Vertical Research Partners.

Jeffrey Todd Sprague
Analyst, Vertical Research Partners LLC

Q

Thank you. Good morning, everyone.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Good morning, Jeff.

Jeffrey Todd Sprague
Analyst, Vertical Research Partners LLC

Q

Morning. And congrats on getting a lot done in a crazy tough pandemic year. Question for me is really just thinking about kind of the way the company now has reconfigured post-N&B. And Ed, you mentioned M&A a little bit in your prepared remarks. I just wonder if you could elaborate a little bit more on kind of the balance between opportunities for organic investment in the areas that you're strategically focused and what the M&A pipeline and/or kind of magnitude of activity on the M&A front might look like?

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Yes. Thank you, Jeff. Yes, look, as Lori highlighted, we were expecting 8% revenue growth in 2021, so we feel like it's going to be a robust year for us. And key for us is our 4% spend on R&D. So that's clearly number one. And we're very focused on the secular growth areas within the portfolio where we're spending the R&D. So we feel like we're going to have very good results organically as we move forward in the new configuration.

The way we're looking at M&A, I'd say, look, there's two targets that we're presently working on, I don't know if we'll be able to consummate them or not, we're not going to stretch to get them. We're going to make sure the numbers work for us and we're going to make sure the numbers work on the cost synergies side, not taking into account revenue synergies even though the couple that we're working on do have revenue synergies. So we'll see how that plays out.

We're actively in that right now. They're right down the middle of the plate and in a couple areas that we already participate in. We're not going to do anything on the M&A side that's a new segment or anything like that, but we

feel like there's some good consolidation opportunities right where we have our strengths and right where we have great relationships with customers. So, that's how we're looking at it.

And as we highlighted, we are – even though we just took 27% of our shares out of the market, not using any cash, we do have still $1 billion open on our authorization. So we're going to get back in the market and start repurchasing shares. We have a board meeting coming up in the next month and that will be a topic that we will have with the board, share buyback versus mix of M&A that we're planning on doing during the year.

Jeffrey Todd Sprague
Analyst, Vertical Research Partners LLC

Q

Great. And as a follow-up actually unrelated, different topic, this global semiconductor shortage fire drill that's going on, can you just kind of address how that impacts you? I'm sure it's going to impact auto production builds that might hurt you on one side, but then you're just kind of supplying the response on the other. Maybe you could just kind of tie that together for us.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Yeah. Well, I think it's going to affect the auto builds. I think the forecast out there are 650,000, 700,000 cars that'll be reduced by because of the shortages out there. But I mean, Jeff, we're running full tilt on the semi side and, quite frankly, the whole Electronics segment is running full tilt.

As Lori had mentioned, even the smartphone demand where we have additional content now because of 5G, that did not even soften up in the fourth quarter and usually seasonally, that even declines. So, we're pumping out as much as we can. But definitely, there's some – slight slowdown but the car production is still hot and heavy even with that, the 650,000 unit reduction. And hopefully, that works its way – those issues work its way through during the first quarter. So we're seeing a little bit there but, again, I think our forecast is very solid for what we're going to do in the Electronics business in the semi.

We're also seeing some headwinds on raw materials in the T&I business, which also somewhat relates to the auto business. So we lost a little bit of volume in the fourth quarter and will lose a little bit of volume in the first quarter because of those constraints, but again, our forecasts still is very solid and we're pretty much running full tilt there also.

Jeffrey Todd Sprague
Analyst, Vertical Research Partners LLC

Q

Great, thank you.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Thanks Jeff.

Operator: Our next question comes from one of Scott Davis of Melius.

Scott Reed Davis
Analyst, Melius Research LLC

Q

Good morning, guys. Good morning, Ed and Lori.

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

A

Good morning.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Good morning.

Scott Reed Davis
Analyst, Melius Research LLC

Q

What changed that got you to keep the non-core businesses, the Microcircuit, the Tedlar and the Films JV? Is it just a timing issue and they may still be for sale or maybe I'll just leave it at that, let you explain.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Yeah. Jeff – or Scott. Look, they're businesses that are kind of down right now because of the end market. So take the Tedlar business, somewhat aerospace-exposed, they're good businesses. Lori and I did a really a study of all the non-core businesses and decided we have some really nice upside in the businesses we're moving into T&I. Our T&I [ph] management (27:23) team is really great operators which is exactly what's needed here. So we think there's nice upside coming in these businesses.

It wouldn't have been productive to sell them, I don't think it would have been good for our shareholders. And we see some good long-term trends there so we made this decision, strategically, to hold on. Don't expect them to be up for sale during the year, that's not what we're doing. We're putting them in there and we're going to run them.

Scott Reed Davis
Analyst, Melius Research LLC

Q

Okay. That's helpful. And then as you just talked about, T&I having some challenges, obviously, with obvious things that Jeff brought up. The pricing headwinds, I mean, you're able to – I would imagine you're able to capture some of the – some of this back in price, it just takes a little bit of time. Is it as much of a mix issue as price issue when you say pricing headwinds or is in fact just explicitly price?

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

No. The headwinds in T&I are really the constraints – raw material constraints that we're having. [indiscernible] (28:28) we're going to have a very nice first quarter in T&I, but we could have had more upside. I think we're going to – we think we're going to miss out on about $60 million to $80 million in sales in T&I because of raw material constraints in the first quarter now. We think we'll get a lot of that back. We won't lose it because the whole industry is having a few issues there.

But [indiscernible] (28:48) specifically to your question on pricing, things have firmed up very well, it's a constructive market for pricing, as we've entered the first quarter. I think you'll see price increases in the industry across the board. But a lot of that won't kick in until you get it – by the time you put it in place with contracts you have with customers, usually 30 days, 45 days, you'll probably see more of that kick in second quarter. But it's turned very constructive at this point in time on the price front.

Scott Reed Davis
Analyst, Melius Research LLC

Q

Okay. Good. All right. Well good luck in 2021.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Thank you, Scott.

Operator: Our next question comes from the line of Steve Tusa of JPMorgan.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

Hey guys, good morning.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Good morning, Steve.

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

A

Good morning.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

Just following up on that last question from Scott on the price side. I guess, for the old T&I segment, what are you assuming for price, or if you just want to talk about the new mobility, however you want to kind of look at it, but what are you assuming for kind of price/mix for the year there?

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

A

Yeah. So for the quarter, maybe hit the quarter first of what we had guided to in the slide, so the new M&M segment, we will see sequential improvement in nylon price and so we were down about 4% in Q4. We're looking at about 2% in Q1. So there is some sequential improvement there. However, we still do expect to be down year-over-year just given that we were at a bit of a nylon run in the first quarter of 2020.

So, as we go through the year, as Ed has mentioned, that pricing environment in nylon is constructive. We do have an awesome team that takes advantage of price, so we do expect, as we get to the full year, that you could see positive price momentum, as reported for the full year basis.

Keep in mind, though, there are some raw material headwinds that Ed had mentioned that we're dealing with. So some of that price most likely will be offset by escalating raws, especially as oil price is expected to pick up, there are some raw material headwinds that we will offset that they could eat into some of the price appreciation that we would see.

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

Got it. So like flat kind of price-cost for the year for you guys?

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

A

I mean it'll depend how the nylon dynamic plays out. Yeah, so right now I think we could hedge it at saying at about flat but, potentially, with some upside if the nylon and the end markets in auto continue to remain tight, there's, I think, a couple of recent force majeures in the industry that's making the price environment even more conducive. So...

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

Got it. Got it. And then you mentioned that you're kind of running full out to keep up with some of the demand on the Electronics side, I mean, are you going to have to add capacity at all to keep up with this or are these just bottlenecks that are more temporary?

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

It's a combo of both, Steve. We're cranking out more and we're freeing up capacity with a lot of moves we're making on the factory floor, but we're also in capacity with our biggest single CapEx project is the Kapton expansion. We're running flat out on Kapton. So, I mean we could definitely ship more if we had more manufacturing capability. And that comes online as we go into 2022. And that's a big move for us. The Kapton is what we use for the 5G and the smartphones. And also, that's a major expansion [ph] coming along that we desperately need. (32:24)

C. Stephen Tusa
Analyst, JPMorgan Securities LLC

Q

Okay, great. Thanks a lot for the info. Appreciate it.

Operator: Our next question comes from the line of Jonas Oxgaard of Bernstein.

Jonas Oxgaard
Analyst, Sanford C. Bernstein & Co. LLC

Q

Hey. Good morning.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Good morning, Jonas.

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

A

Good morning.

Jonas Oxgaard
Analyst, Sanford C. Bernstein & Co. LLC

Q

Wondering about the capital allocation. So, you said you're going to seek board approval for more buyback. Can I just ask what kind of range of buybacks will you be seeking?

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Jonas, don't fully know yet. It's also partially going to be contingent on did we do some M&A during the year. I mean, look in aggregate, I mean we're in a really nice spot here. We've got $5 billion to $6 billion of cash available to us as we close the three non-core sales that we've made, but haven't closed them yet.

I think Lori mentioned, there's still $900 million gross coming in during the first half of the year. In addition to the $2.3 billion excess from the IFF transaction and the $2 billion – $2.5 billion we have just coming into the year from non-core sales and operating cash flow. So it's a really nice position to be in. And so partially, just in general on where we end up on the M&A front, not going to sit on cash through the year, net big numbers. So it'll either be M&A or buyback. So...

Jonas Oxgaard
Analyst, Sanford C. Bernstein & Co. LLC

Q

Okay, appreciate that. Then if you don't mind, [ph] as an ask, so (34:03) it seems you've been focused on the transaction, getting the businesses back up and running, so, when you're thinking of 2021, like as the CEO, what are your big focus areas for the year?

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Operational excellence, if I just put it into words. I think we have still nice runway for a lot of improvements. One of the areas that Lori and I are spending a lot of time on is really our throughput at our facilities. We think we have gross margin runway to improve. It's not – I think we're best-in-class when it comes to overhead cost structure, if you benchmark us against the very best peers. So that's not our opportunity, although we always look for ways to optimize that.

But the key for us is the gross margin line. We want to move that up over time to 40%. We've been running kind of 35%. We're installing a lot of digital analytics at our facilities. We spent about [ph] $50 million (35:09) last year in data analytics tools. This year, we budgeted $30 million. So you can kind of see how we're ramping there. A lot of it's on the supply chain and manufacturing efficiency. We're putting in some tools on smart demand forecasting, process optimization uptime. And we're seeing some real benefits from it. So that's a huge focus area for us from this year.

Jonas Oxgaard
Analyst, Sanford C. Bernstein & Co. LLC

Q

Okay, thank you.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Thanks Jonas.

Operator: Our next question comes from line of John Inch of Gordon Haskett.

John G. Inch
Analyst, Gordon Haskett Research Advisors
Q

Thank you. Good morning, everybody.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.
A

Good morning, John.

John G. Inch
Analyst, Gordon Haskett Research Advisors
Q

Good morning, guys. How are you thinking about working capital improvements from here? I think you'd called out – correct me if I'm wrong – $1 billion long-term potential, but you just did over around $850 million for 2020. And does working capital have to come back, let's say, in 2021 as your businesses cycle back, which I guess it's probably a good problem to have actually?

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.
A

Yeah. It is a good problem, John. But look, we look at it – I think when you're going back into an up environment here, I really look at it from what are the turns doing. And we took our turns from 4.3 turns going into last year to we exited the year of 5.2, and that is the $850 million improvement. And our plan this year is to slightly improve our turns from the 5.2, not a lot this year, but slightly. And that would be a victory for us.

John G. Inch
Analyst, Gordon Haskett Research Advisors
Q

Would those areas where the turns are higher correlate, Ed, with what you just stated as the sort of 5 points of runway overall for gross margin? So I was going to ask about, too, is the gross margin, is it comparable by segment, that 5 points, 35% to 40%, or how does that delineate across the three segments?

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.
A

No. The biggest opportunity is S&C. And it's also got our heaviest manufacturing footprint. So between Nomex, Kevlar and Tyvek, they are our biggest opportunities in the business. They're our biggest facilities. We definitely know we can improve our uptimes, our turnaround times, and that that's the number one area we're working on. By the way, it's across the board, but the biggest opportunity is there.

John G. Inch
Analyst, Gordon Haskett Research Advisors
Q

No, that makes sense.

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.
A

And the same goes for working capital, a lot of the opportunity still resides within inventory. I think our DSO is at a nice level and DPO, working capital we can continue to improve, and a lot of that back to the S&C, or the new W&P business, is where a lot of the opportunity lies.

John G. Inch
Analyst, Gordon Haskett Research Advisors

Q

No, it makes sense. Just as a follow-up. Ed, what's your appetite for doing something larger on the deal front in the next year or so? Maybe I was thinking, instead of just continuing to shrink DuPont, maybe even a possible asset swap with another company.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Well, John, let me just – we always look at every opportunity. So I don't think anything will get by us if there's something interesting. Let me just highlight, though, on the M&A side, maybe just to size it a little bit for you. We could spend up to $2.5 billion on M&A. Now things don't always work out and, as I said, we're not going to stretch to get something, so you never know. But we're kind of looking in that kind of range if it were to play out, so just to kind of size it a little bit for you. But look – we always look at other alternatives too, we get calls every week, if something makes sense, we'll study it.

John G. Inch
Analyst, Gordon Haskett Research Advisors

Q

Got it. Thank you.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Thanks, John.

Operator: Our next question comes from Steve Byrne of Bank of America.

Steve Byrne
Analyst, BofA Securities, Inc.

Q

Yes, good morning.

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

A

Good morning.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Good morning, Steve.

Steve Byrne
Analyst, BofA Securities, Inc.

Q

Ed, when you were talking about the PFAS liability settlement, you also commented that it's your view that your liability will be limited to the legacy DuPont facilities, given you didn't ever manufacture firefighting foams. Is there anything you can do to solidify that view?

And the reason I ask is in the past, DuPont supported the initiative to have the PFAS grouping regulated under CERCLA, and under the old Superfund [ph] days, (40:03) CERCLA allocated costs according to the ability to pay,

not necessarily to the contribution to the problem, and thus, is that a potential concern for you with regard to broadening this potential clean-up liability?

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Yes. So let me clarify that. We have been supportive. We've testified in front of Congress that if you designate it as a hazardous substance, we're totally in agreement with that, we'd rather have a national standard than every state doing their own thing. But remember, under the CERCLA or the Superfund designation, it's very narrow who is responsible for it. I mean, it's where you disposed of the material. And the party responsible, either had to be the site owner or the past site owner when it occurred, or the person that arranged to transport it to that location. That is the definition under the CERCLA which is very narrow. You have to be one of the players that did that.

DuPont – by the way, we have four sites where we use it as a manufacturing agent. And we disposed of it on our own sites with, by the way, approval to do that. One of our sites is 800 acres. One of them was 1,500 acres and that's why we had so much ground that's where the disposals occurred. So we're very contained where we did it. There's already cleanup going on with government authorities approving what we're doing and it's been ongoing for quite a few years. And so – and we never obviously, disposed the firefighting foam anywhere in a dump or anything because we didn't make it.

So I think – look, as the facts keep coming out, it'll get narrow and narrow here and then, we'll – as I've said before, and I don't want to get into too much detail, it's a little bit proprietary, but we'll look at a way to hopefully contain the firefighting foam issues so our investors understand the limited or no liability that sits there based on what we did as a company.

And by the way, we're very focused on it. As you can see, we said there was a three-pronged approach. We just did two of the pieces with the announcements we made with the agreement between the three companies and settling the rest of the Ohio MDL for really very little in the scheme of things. And so now we'll focus on this firefighting foam piece of it.

Remember, also, we have been sued in states. We don't even have anything in the state, State of Arizona, the State of New Hampshire, we don't even have a facility there. We didn't do anything there. So, the facts will keep coming out here and then, hopefully, we'll get resolution and, hopefully, something by the end of 2021.

Steve Byrne
Analyst, BofA Securities, Inc.

Q

Okay, thank you for that, Ed. And now that, N&B has been separated and you've reshuffled the segments and you've accomplished a bunch in the last year. Just curious, how long do you see yourself remaining CEO and is there a process underway that that could change?

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Well, I just signed a three-year contract. I don't know, a month or two ago, so at least that period of time. So no, we're – no process in place. I'm very excited for the next few years.

Steve Byrne
Analyst, BofA Securities, Inc.

Q

Okay. Thank you.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.
A

Yeah, thanks.

Operator: Our next question comes from the line of Bob Koort of Goldman Sachs.

Robert Koort
Analyst, Goldman Sachs & Co. LLC
Q

Thanks so much. Good morning.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.
A

Hey, good morning, Bob.

Robert Koort
Analyst, Goldman Sachs & Co. LLC
Q

Ed, I'm curious, maybe this was asked in other ways, but when you think about sort of what your aspirational peer set was, and there's some pretty good variance still in the valuations of your individual businesses, even though you've obviously made some great progress. You've cleaned up some of the non-core stuff, the portfolio, you've maybe diminished the angst around PFAS. What do you sort of see as the strategic options to narrowing that variance from a valuation standpoint?

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.
A

Well, Bob, it's one of the reasons we continue buying back shares. [ph] If you (44:43) look at our multiple, whatever it is, 13 times and, yeah, I stare at ITWs and Honeywells and Eaton, and we're just as good a company. I think part of it is we got to continue to post consistent results. I think consistency and people not having to worry, I think, means a lot in the multiple. I've been doing this for a long time and I've been saying that for over 20 years.

So I think we just keep posting good numbers. And I think we continue to close that gap and I think we're going to benchmark very well this year, all our metrics vis-à-vis those other very good competitors by the way in multi-industry companies. So, there's a gap to that peer set for us of 400, 500 basis points. And I truly don't believe that discount should be there at all. And so we'll continue to prove that out during 2021.

Robert Koort
Analyst, Goldman Sachs & Co. LLC
Q

Ed, you mentioned a few markets that have been quite hot, obviously, you've got a few in the portfolio, end markets that are maybe more of a post-pandemic glide path. Can you give us some update on how you see things progressing in energy or maybe aerospace or some of these other businesses that are going to take a bit longer to recover?

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.
A

Yeah, if I describe at high level and maybe Lori wants to give a little more detail, they all – some of those, the oil and gas, aerospace, they dropped 30% to 40% on the revenue line. And our gut is we kind of glide back up, get

half of that back in kind of 2021. That's kind of how – if you just put them all together, that's how we would look at it. So, we still would be down from 2019 levels in those end markets, and oil and gas, specifically, and aerospace, as you mentioned, would be two of those. So that's kind of how I would look at it.

Robert Koort
Analyst, Goldman Sachs & Co. LLC

Q

Great. Thanks so much.

Operator: Our next question comes from the line of David Begleiter of Deutsche Bank.

David I. Begleiter
Analyst, Deutsche Bank Securities, Inc.

Q

Thank you. Good morning. Ed and Lori, just on the sales guidance of up 7% to 9%, by segment, which would be above or below or in that range, do you think?

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

A

So, I'll give it to you on the current segment basis and then we'll remap it on the Q1 call when we have all of these recasts on to get to the new segment basis. So, from the old segment basis, we would see T&I probably at above that average 8%, just given by all the strengths that we had mentioned earlier with the V-shaped recovery in automotive, and potentially, some pricing tailwinds that could come our way.

Ed had just mentioned within S&C, is it more of a delayed recovery to full 2020, 2019 levels within a lot of the aramid end markets that sell into oil and gas and aerospace, for example, so they would probably be below that 8%. And we would say Electronics right now, right around that average, and so very strong in the first half as we see it. We're watching the second half to see how the trends continue across semi, across the 5G infrastructure, to see how we continue to trend there. Obviously, we posted very strong results in 2020, up about 8% in that segment. So I would say that's where you put it. So, T&I at the top, E&I right around the middle and S&C probably lagging the average for the company.

David I. Begleiter
Analyst, Deutsche Bank Securities, Inc.

Q

Very helpful. And I just – how was January, was it above or in line with your expectations? And what are you expecting or seeing around Chinese Lunar New Year?

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

A

Yeah. So you hit the nail on the head with the Lunar New Year, so January, it's hard to gauge from how the quarter is going to play out because it was strong just given the timing of Lunar New Year from this year to last year. So we're still comfortable looking at January results with the Q1 guidance that we gave. And we'll see how, we had mentioned, that nylon price continues to play out as well as availability of raw materials within the T&I business to satisfy that demand, and we'll see how much unconstrained demand we have at the end of the quarter.

David I. Begleiter
Analyst, Deutsche Bank Securities, Inc.

Q

Thank you.

Operator: Our next question comes from the line of Chris Parkinson of Credit Suisse.

Christopher Parkinson
Analyst, Credit Suisse Securities (USA) LLC

Q

Great. Thank you very much. Naturally, there a few moving pieces heading into 2021 as well as 2022. But just given the current end market trends you're seeing and how they're setting up for that timeframe as it pertains to op leverage mix, your efforts to further improve your overhead structure and improve your cost profile, how should we just generally think about incremental margins on a segment-by-segment basis over that period, versus how we used to think of them? Are there any major differences we should really be honing in on? Thank you.

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

A

Yeah. I mean I think on a steady state basis, there shouldn't be material difference between them. In 2021, it'll vary, because of the recoveries in the different shape [indiscernible] (49:53) recovery. So if we talk in a total company level, based on the guidance that we provided, you would see incremental margins sort of in the low 40s for 2021 over 2020 for the total company.

Christopher Parkinson
Analyst, Credit Suisse Securities (USA) LLC

Q

Great. And just as a follow-up, in terms of your Water Solutions portfolio, where do you see your largest strengths heading into 2021 and 2022 in terms of product offering? And can you also comment on just any additional substrates you feel could potentially augment, via M&A, to further enhance the breadth of your offering? So just trying to get a better sense of the longer term strategy within that portfolio. Thank you.

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

A

Yeah. So I think with the acquisitions that we made at the tail end of 2019, we now have probably the most complete portfolio in the industry. So we've got technologies within ultra filtration, reverse osmosis and ion exchange. And so as we look forward to capture opportunities there, we're looking to provide not only materials into those individual spaces, but also a solution set and a solution play more along the lines of a complete offering.

As we look to M&A, we'll look to continue to round out that portfolio from both enhancing existing businesses as well as also potentially looking at a geographic play. So obviously a lot of – the opportunity within the water space is in more of the emerging regions and if there are some M&A plays that we can utilize to take advantage to solidify our footprint in some of those geographies.

Christopher Parkinson
Analyst, Credit Suisse Securities (USA) LLC

Q

Thank you very much.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Thanks, Chris.

Operator: Our next question comes from the line of John McNulty of BMO Capital Markets.

John P. McNulty
Analyst, BMO Capital Markets Corp.

Q

...the questions. Just a follow-up on the water treatment side or the Water Solutions side, so you indicated there were some order delays just around capital projects being delayed. I guess, can you quantify that a little bit, or kind of frame it for us a little bit? And also can you speak to the visibility that you have in this business, how far out you can actually see, and how you see 2021 as a whole playing out this year?

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

A

Yeah, so if we size kind of the headwinds that we saw in Q4 so it was, as we had mentioned, the capital delays, there were also some logistical delays in the quarter [ph] to just basically to get (52:13) shipping out the door. It was probably about $15 million for the fourth quarter. So as we look at January results, they were strong, they were again up about 6%. We're looking for the quarter to return to that mid to high single digit growth within water, and for the year, generally, at that levels as well. So we're confident in the go-forward portfolio there, we just had a little bit around a capital project delay and, as I had mentioned, logistics.

As far as visibility is concerned, we have back-end loaded order patterns. And so a lot of the sales go into large capital projects that tend to be pushed to the back-end of the quarter. And so our visibility there, on those larger opportunities, is a little bit more limited than some of the shorter term opportunities of selling materials into, like I had mentioned, reverse osmosis and ion exchange.

John P. McNulty
Analyst, BMO Capital Markets Corp.

Q

Got it. Fair enough. Thanks for the color on that. And then just a follow-up on, Ed, your comments earlier around the hope of getting the gross margins to, at some point, getting them pretty close to 40% or above, with a lot of that tied to – or it sounds like, a disproportionate amount tied to S&C.

So I guess just back to the envelope, that kind of says S&C starts to see margins at some point in the low to mid 30s, Ed, which is an obviously a notable jump from kind of where we are. And I guess, what are the – is it just operational improvement that gets you there? Is it mix improvement as some of these higher margin businesses, like water, really start to accelerate? I guess, how do you get to those types of levels, if that's what you're really targeting, say, whatever over the next two to three years?

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Yes. So S&C, I would target it more towards the high 20s EBITDA margin, because not all of the opportunity is in that business, but it is the biggest single piece. And I would say the single biggest thing then in there is the factory optimization, our uptimes, our throughput on those assets. So that's the biggest area and that's where we're putting a fair amount of focus on digital tools going in to help us there. But I think that business should be a high 20s EBITDA type of business over the medium term here. And we could definitely run it there, but it's mostly on the factory optimization piece.

John P. McNulty
Analyst, BMO Capital Markets Corp.

Q

Got it. Thanks very much for the color.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Yeah. Thanks, John.

Operator: Our next question comes from the line of John Roberts of UBS.

John Roberts
Analyst, UBS Securities LLC

Q

Thank you. Ed, do you have to reset some of your sustainability targets here with the N&B business going away because, obviously, that was the greenest of the DuPont businesses?

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Yeah – no, we don't, John, I mean, we have our targets laid out by segment and – by the way, their public, obviously, so you can go look at all of them. So no, it doesn't really change what we're doing and what we've laid out. But I guess, overall, it does for DuPont because you're taking 30% of the EBIT out those businesses. But we have targets laid out by division and then totally for the company.

And it's a big focus area for us this year. We've actually – I don't think we said this publicly, but we've actually put sustainability in our bonus structure this year. It's a modifier of 10% in either direction in what the bonus payout would be for the company based on targets that we set with the board. So I'm happy and in fact I'm glad that we put that in place also. So all our employees know the importance of it to us, to hit the goals that we've laid out.

John Roberts
Analyst, UBS Securities LLC

Q

And then, can you quantify at all what the raw material inflation number might be for 2021, what percentage up should we expect year-over-year? And what are the couple things that are going to be above the average to push that high?

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

A

Yeah. So in total, I would quantify it about $100 million of a headwind in 2021 with the predominance of it being within T&I in some of the nylon feedstock.

John Roberts
Analyst, UBS Securities LLC

Q

Thank you.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Thanks, John.

Operator: And ladies and gentlemen, looks like we have time for one more question. Our final question will come from the line of Mike Sison of Wells Fargo.

Michael Sison
Analyst, Wells Fargo Securities LLC

Q

Hey, good morning. Hope it's warmer in Wilmington than it is in Cleveland, but...

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

A

[indiscernible] (56:55)

Michael Sison
Analyst, Wells Fargo Securities LLC

Q

Yeah, just one question. I guess in Transportation & Industrial, a lot of companies in polymer lands has talked about recycling, sustainability, recycle plastics and that type of offering. Maybe give us your thoughts on where you participate in that trend? And then is it maybe potentially an area for acquisitions to beef up that part of your portfolio?

Lori D. Koch
Chief Financial Officer & Executive Vice President, DuPont de Nemours, Inc.

A

Yeah. I would answer the second part, first, so around the M&A opportunities right now. I would say they're more biased towards the electronics space. Within automotive, they could be biased towards more – getting us more of a footprint within the electric vehicle space. And then obviously within, as we had mentioned earlier in the water space, rounding out that portfolio, taking advantage of the underlying growth trends within that space.

I think as far as the recyclability within that space, I don't see that as a large challenge for our business. I think that's more within the plastics space, I don't see that as a material driver of the overall new DuPont Company.

Michael Sison
Analyst, Wells Fargo Securities LLC

Q

Great. Thank you.

Edward D. Breen
Executive Chairman & Chief Executive Officer, DuPont de Nemours, Inc.

A

Thanks.

Leland Weaver
Vice President-Investor Relations, DuPont de Nemours, Inc.

Thank you, everyone, for joining our call. For your reference, a copy of our transcript will be posted on DuPont's website. This concludes our call.

Operator: Thank you, ladies and gentlemen. This does conclude today's conference call. You may now disconnect.