Dow Presents at 33rd Annual Credit Suisse Global Basic Materials Virtual Conference



Chris Parkinson, Credit Suisse
Howard Ungerleider, Dow President and CFO

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Chris Parkinson:

Next up, I'm very pleased to introduce Howard Ungerleider, the CFO of Dow chemical. As many of you know, Dow is one of the largest producers of polyethylene and polyurethanes on the globe, and retains some of the best feedstocks flexibility within the industry. Despite its recent rally, Dow still retains a dividend yield close to 6%, which we've consistently flagged in our research as sustainable. Today, Howard is going to be kind enough to start off with some brief remarks, but then we'll utilize our time in a fireside-chat format. As a friendly reminder, this event is open to the public and we recommend referring to the cautionary and forward looking statements in the materials Dow will post. With that, it's my pleasure to turn it over to Howard.

Howard Ungerleider:

Well, thanks very much for having us, Chris. And that was a nice introduction. Good afternoon, everyone. This quarter, team Dow has continued to deliver through, what I would call, a range of extraordinary circumstances. A pandemic that we're all dealing with, a flood that was specific to mid-Michigan, and now a hurricane on the US Gulf Coast. Now, to those who were impacted by the recent storms, because there were a couple of them so far, we hope each of you and your families are safe and healthy. We are immensely grateful that all the members of team Dow thankfully remained safe through hurricane Laura.

Our Dow sites in the US Gulf Coast reported minimal damage, the vast majority of the sites that shut down in preparation for the storm restarted within a week, and Dow has avoided major supply disruptions to our customers. We're still finalizing the financial impact and it's underway and we'll have more to share on that on our earnings call, but overall we've been very pleased with the low-level impact the storm has had on our operations. We anticipate the impact, financially, to be approximately $75 million, primarily in lost margin from downtime, with, what I would say, was minimal physical damage costs.

Now turning to the corner, overall, macro conditions are continuing to progress as we expected. The economic recovery is definitely continuing. It's continuing at various paces across those markets and regions around the world. Demand has definitely improved from the second quarter lows, and we continue to map supply levels accordingly. We have increased our operating rates across the enterprise and they are now approaching first quarter levels. And market tightness and polyethylene and isocyanates are both supporting price increases, which together, are driving improved earnings and incremental margin upside. We have continued to capture robust demand for packaging applications, and our year-to-date volumes are exceeding the same period in 2019.

You'll recall that the second quarter earnings we expected both the July and the August PE price increase is to be well-supported. And we now expect that the nominated September price increase is also likely to be implemented, supported really by the low level of industry inventories, coupled with the supply disruption from hurricane Laura. The increased durables demand we expected, really led by the improving automotive and construction industries around the world, is also benefiting our polyurethanes business. Also coupled with some supply disruptions caused by some unplanned European outages from our peers, the MDI markets have also seen pricing strength perform a little better than expected.

Some other markets where Dow participates are also improving, but they are improving at a bit of a more gradual pace. Personal care, for example, has really followed return-to-work activities, with most regions continuing to lag progress that we saw in the second quarter in Asia Pacific. And cleaning products have leveled off a bit from the pandemic-driven demand highs earlier in the year.

Now following our second quarter earnings call, Dow's first call consensus EBITDA was just north of $1 billion, and with the improving market conditions, now fits at about 1.1 billion. With the additional upsides I just mentioned, we now expect an additional $150 million EBITDA above the $1.1 billion consensus, which is a $250 million increase over the modeling guidance input we provided at the end of the second quarter. As you would expect, this also will have a favorable impact on our operational tax rate as well. We expect our third quarter tax rate to be in the range of 23% to 27%.

Now beyond these near-term improvements, we continue to progress our proactive focus on ensuring a competitive cost structure and delivering on our cost interventions, as well as executing on non-operational cash levers. At our second quarter earnings call, we increased our 2020 operational expense reduction target to $500 million, and we remain on track to deliver these committed savings this year. We also announced plans to initiate a restructuring program, targeting more than $300 million in annualized EBITDA benefit by the end of 2021, which includes a 6% reduction of our global workforce costs, as well as strategic actions to exit assets that are less competitive in today's market.

And we'll have more details to share on our third quarter earnings call, but for now I'd like to highlight that in the quarter, we expect to take a charge for the program in the range of approximately $750 million with a two-year payback period. The total charge includes estimated cash payments related to severance, asset exit and disposal cost, and some contract termination fees, in total of approximately $500 million, which will occur over the next several years.

Now, in addition to our costs and restructuring actions, we continue to focus on broader cashflow generation by progressing our slate of non-operational cash levers. In fact, this week we announced plans to divest select marine and terminal infrastructure assets to Vopak Industrial Infrastructure Americas. The transaction is expected to close by the end of this year, with more than $600 million in cash proceeds to Dow. This latest announcement builds upon the rail infrastructure assets sale we announced in July, which we now expect will closed three months earlier than expected, at the end of September, resulting in a cash proceeds of more than $300 million. Together, these two transactions demonstrate Dow's continued commitment to a best-owner mindset, and they will deliver nearly $1 billion in unique-to-Dow cash tailwinds this year. The Nova litigation also continues to progress, and we remain confident that awards from this matter could result in additional payments to Dow over time.

Continuing to strengthen our financial profile also remains a priority. Dow has already paid Down more than $740 million of net debt through the first half of this year, and we recently just completed a debt-

neutral bond issuance of $2 billion at historically low interest rates as we continue to proactively manage our liability profile. This debt-neutral issuance further extends our next substantive debt maturity by another year, which is now the second half of 2024. And on Sadara, negotiations are progressing well and remain on track to complete Sadara's debt re-profiling by the end of 2020, with the goal of Sadara achieving cashflow self-sufficiency.

Now as we move forward through the year and into 2021, we're confident in the competitive advantages that continue to set Dow apart, and I think Chris spoke to that in his introduction. And they will enable us to continue delivering leading results compared to our peers. Our feedstock flexibility allows us to maintain our advantage on the cost curve and drive incremental margins while feedstock costs have been higher than we anticipated entering the quarter. And our zero-naphtha capability enables competitive advantages, especially while co-product demand is expected to continue to be bumpy through this year and into next.

Progressing our ESG and sustainability efforts are also already providing positive, tangible impacts to both the top and the bottom line, in both the medium and the long term by growing market potential, opening new adjacencies, and reducing costs. Our ongoing relationship with Unilever, for example, is advancing to the design phase, where we're innovating new ingredients together in the home and personal care markets for more environmentally friendly products to help them achieve their sustainability commitments.

On our work to increase our access to sustainable feedstocks, both our partnerships with Fuenix and UPM are advancing. We're in the process of scaling our capabilities with Fuenix to start building a second pyrolysis oil line using recycled plastics. And we're on track to double our product sales containing UPMs recycled material this year as well.

In terms of cost avoidance, we have reached the halfway mark on our value in nature sustainability goal to uncover $1 billion in business value over 10 years in nature-based solutions that are good for our business, and for natural ecosystems. Just one example of these nature-based solutions resides at our manufacturing facility in Elizabeth Town, Kentucky, where instead of constructing a dry containment pond for fire and storm water, we created a five-acre wetland that meets our functional need, reduces downstream flooding, and improves groundwater all at the same time. We also view this period as a prime opportunity to accelerate our actions in areas that will drive long-term value creation for Dow. Things such as continuing our digital acceleration to drive improved customer experience and higher revenue.

Altogether, our proactive actions and our unique advantages continue to strengthen our ability to capture value, and position Dow competitively as the economic recovery gains further traction. Summing up the actions of team Dow so far this year, Chris, before I turn it back to you, we've lowered our operating expenses. We've liberated significant cash from working capital. We've initiated a restructuring program. We lowered our CapEx spending. We delivered increased free cash flow and cash conversion above 100%. We've extended our debt maturities. We delivered almost $1 billion already of non-operational cash tailwinds, and have another $1 billion left to go this year. We're making really good progress on the Sadara re-profiling. And I would just say, all of which positioned very well for the market recovery as it continues in front of us. And Chris, with that, let me hand it back to you to open the Q&A.

Chris Parkinson:

Howard, thank you very much for those remarks. They're incredibly insightful, as always. You did hit on the new term supply demand dynamics and polyethylene. Can you speak to just the process of, let's call it, further normalization on the supply side throughout the balance of the year? And then also if you could potentially hit on the less cost advantaged, which would probably be a kind term, production in Asia, that you and Jim have both spoken about over the last couple of quarters as we head into the next year or two?

Howard Ungerleider:

Yeah. And look, Chris, thanks, I think on the polyethylene side, demand has been resilient and that has been our consistent view. And I know some third party providers have thought, at the beginning, it was going to go down. Then they said, "Well, it's not going down. It's pantry stuffing." And then the pantry stuffing just has continued. And look, I think it speaks to the benefits of polyolefins and the demand has been, and I believe will continue to be, resilient. And in fact, the way we're all living right now in a lot of the world where you're not going to as many restaurants, you're not going to sporting events, you're consuming much more from the grocery store. That will only increase the amount of per square inch of packaging or polyolefins that'll be required to serve each of us as consumers. So, demand, I think is going to be there. Look, from a supply standpoint, you're right. When you look at the cost curve, and thankfully, we're typically in the first or the second quartile in almost every region of the world with almost every asset in the world. So, that speaks to our advantage, and then, the feedstock flexibility that you pointed out also helps.

But when you do the math, in an economic down cycle, which we are clearly still in, we are clearly still in an economic down cycle, old, less competitive or assets that are not integrated or not in the first or second quartile of the cost curve will typically get rationalized. We saw that in '08, '09, we saw that in '02, '03. In '08, '09, we had four million metric tons of capacity come out, two of which came out permanently, and two of which shut down in '08, '09, and then, between 2010 and 2012, started back up.

This time, to specifically address your question, as we look at the world today, there's probably about north of 20 million metric tons of ethylene and polyolefin capacity that's at risk, either due to age, due to scale, or due to the high conversion cost or being disconnected from the raw material feedstocks or the market. Of that 21 million metric tons, probably about six or six and a half of that 21 is CTO/MTO, which certainly needs an oil value with at least a five handle on it to be cash-flow break even. So, that sums it up in terms of what we think, in terms of both the supply and demand.

Chris Parkinson:

That's great color. Just on this front, it's probably an easy leeway into another question I had, just given the current environment, how should investors be assessing your non-US P&SP production assets, just given your cost outlook as it pertains to your other thoughts on the long-term polyethylene cost curve.

Howard Ungerleider:

Yeah, look, I think it comes down to our geographic breadth, our market application mix, and then the depth of customer and application. I think I put the Dow portfolio and P&SP up against anyone of our peers. The fact that we are geographically... You think about our feedstock flexibility, the US Gulf coast is really second to nobody. We have max ethane capability versus anybody, we've got two to three times the propane, butane, we've got the ability to go to zero naphtha.

But then, as you go around the world, to your point, we've got the Alberta advantage in Canada, which is pretty unique. Only Dow and one other player has that advantage. You've got our Argentinian advantage, which has gas based on the Vaca Muerta shale field. And there's plenty of shale in Argentina for us to compete within the Mercosur duty barrier.

Then, you go to the middle East, clearly Equate is all gas. Sadara, mixed feed. So, you have the ability to switch feedstocks to some degree. And then, of course, in Europe, we have a sizeable position in Europe. And because of our investments over the last several decades, we have the capability to crack 65% today, LPG. So, we can go naphtha if we want to, but we can go as much as 65% LPG if the market's favorable. And then, you've got our tie assets in Asia as well.

So, I really think the Dow portfolio is very well positioned in terms of feedstock flexibility, location, and then obviously, the markets and the applications. You think about P&SP, we have our polyethylene franchise around the world, but we also have about 20, 25% of our portfolio is in what we call functional polymers. These go into, typically, higher margin, more durable goods. Think pipes, think food packaging, think wiring cable compounds.

And so, these things will generate higher margins and tend to be more resilient over an economic cycle. That part of the portfolio definitely got hit harder because of the COVID pandemic. And a lot of it goes into automotive and transportation more broadly and more durable goods. So, that took a step back here in the second quarter, but as the economy recovers, that will be a nice tailwind for us over the next several years.

Chris Parkinson:

Thank you. And just, while we're speaking on the cost curve, let's shift back to the lower end and just talk about US ethane for a moment. Over the last two years, I actually two years ago, and at the time, I think it was at around 60 cents. We reached a low around 10, now, we're around 19. When your team is analyzing everything that's going on in the global energy markets and effects on the US GC, just how should we be thinking about your own cost position over the next, let's say, 12 to 24 months?

Howard Ungerleider:

Yeah, look, if your question is, is there enough ethane out there, my short answer is yes. There is plenty of ethane out there. I know there's a debate going on in the investment community right now, but look, oil and gas producers are guiding the flat production through the remainder of the year. And I would say the abundance of wells drilled but not completed will allow producers to bring gas and oil to the market before the actual rig counts recover. I think some people are looking at rig counts and coming to different conclusion.

There's significant ethane rejection today, and it's expected to be in the future, even with the additional gas demand. And I would say, look, while oil demand is in a low right now because of the economic environment, is that the rate of global recovery will determine demand for oil. And I would say that will also then drive even more gas as well. Depending on the third party analysts that you read out there that covers the oil and gas industry, I would say most folks believe that we'll be back close to a hundred million barrels a day of demand at some point in 2021.

So, within the next 12 months, you're likely to get back to 2019 oil demand levels. And that speaks well to the overall pricing, which most of the world cracks naphtha, so naphtha will trade off of oil. And so,

that will put pressure on naphtha over the next couple of years to move up. And then, our view on ethane says that your shale advantage will continue to improve and not go away as some people have predicted, I think, as the crisis of COVID and the oil drop first indicated. I just don't think that that's likely to happen for the reasons that I talked about.

Chris Parkinson:

Howard, one of the key debates in the marketplace right now is there is this whole debate, I'd say beginning in July even into early August, about the sustainability of the polyethylene price increases. A lot of people were expecting, I'd say pennies, and you are on your way to getting dimes. When we think about that, you've got this near-term dynamic and then the intermediate to long-term dynamic, which still isn't a huge focus, but where do you really assess yourself in terms of mid cycle earnings and why, just given all the factors we're discussing?

Howard Ungerleider:

Look, I would say, let me step back from polyethylene just for a second. I can circle back to that if this doesn't answer your question. But if you think about the enterprise, and you take consensus today. Consensus for Dow for this year is in that $4.7 to $5 billion range, depending on which analysts you want to look at. Mid-cycle earnings for Dow is probably in the... As we did all of the analysis, all the Monte Carlo simulations, with this portfolio, mid-cycle is in the eight to $9 billion range. And cycle peak is in the $11 or $12 billion range with taking reasonable margin forecast and an economic up cycle.

So, we are clearly still in an economic and a petrochemical trough, and there's a mid-cycle in front of us. How long it will take to get there as an open question. Part of that will depend on how quickly the world recovers from the pandemic. And then, there'll be an earnings cyclical peak in front of that. When you think about polyethylene, you've got good demand drivers, you still have a growing population, and over time, it has grown more than one time GDP.

For the last 30 years, it's grown about 1.4, 1.5 times GDP. Now, one, because of the law of large numbers, that ratio likely starts to go down, and then, you've got the whole recycling sustainability point, which will also probably reduce it. But even if it starts trending down to one, you're still talking about a significant amount of growth over the next seven to 10 years that you have in front of us.

And I think what the pandemic just proved, once again, is that polyolefins win because they are the most sustainable and they do provide the least amount of greenhouse gas emissions, the lowest carbon footprint of any other material. They keep food safe, they keep medical supplies clean, they make cars lighter, more fuel efficient, and have better safety performance. So, no matter what your application is, polyolefins have really proven their value to society over many, many, many decades. And I just personally don't see that changing.

Chris Parkinson:

Now, I want to jump back to a question I had at the end, but I think this is a good time to bring it in. You're mentioning that a trip we had together in London a few years ago. And we had a discussion at, I believe it was lunch, about just ESG and recycling. And it's naturally been a very important and integral topic of this conference among your peers and everyone else.

There seems to be a lot forgotten about plastics. You just mentioned too, so no need to rehash those in terms of food spoilage and lightweighting and so on and so forth. But can you just remind the investment community on where you stand, all the various initiatives you're involved in, because if I recall, I received an email from your IR team with about 20 things you were actually doing behind the scenes. So, I'd like to give you the opportunity to convey those to the audience and point us to the two or three we should really be honing in on.

Howard Ungerleider:

Yeah, look, thanks, Chris. And that lunch in London, I was joking before we got on. That seems like just yesterday and it seems like 20 years ago. It was about 18 months ago. So, I remember it fondly. Look, on the environmental side, we're doing a lot. We've been a leader in the sustainability space. For our 125 year history, we've had stated 10 year sustainability goals for now three decades. We just announced some significant goals around getting to carbon neutrality by 2050, making sure all of our polymers are 100% recyclable and a few other things. We're doing a lot. A couple of things I touched on, I think, in my prepared remarks are really around feedstock recycling and percent of recycled content. The partnership that we have with Phoenix and UPM around fossil fuel replacements, as well as plastic road offerings ...

On plastic roads today, we have now, not Dow specifically, but we contributed. There's now over 150 kilometers of plastic, recycled plastic modified roads in 10 different countries around the world, and we've helped make that happen. We've launched our agility CE series last year, which utilizes 70% post-consumer content. We're working with UPM to use their wood-derived renewable naphtha into our slate of raw materials for the production of bio-based polyethylene in Europe.

On the overall carbon side, we're also doing, I would say three different sets of things. We're working on optimizing our current assets, we're working on implementing transitional technologies, and then we're really innovating for next generation technologies. I can talk about this for several hours, but let me just give you a couple of examples in each of those buckets. Optimizing current assets, we're already the number one user of clean energy in our industry, and we're one of the top 25 in terms of global corporations utilizing clean energy. We just ratchet it up, several hundred megawatts increase in terms of what we have under contract.

On implementing transitional technologies, we've worked with FCDH, so we're piloting FCDH in Louisiana to produce propylene with much lower energy and much lower carbon emissions. Then we're working on taking the learnings from that technology and transitioning into what we call EDH technology for ethylene. If we're able to get that done, that has the potential to reduce our emissions by 40-50% by significantly reducing our energy usage.

Then when it comes to innovating next generation technologies, one of the things that we announced earlier this year was a joint development agreement with Shell to accelerate technology, to electrify ethylene steam crackers. That's clearly early development, but if we can do that, that allows you to potentially completely decarbonize when you think about it from that perspective.

We're working on things in all three of those buckets. In addition to what I talked about in my prepared comments up front with customers. Whether it's with Unilever that I talked about or what I've talked about in the past with our partnership with Kellogg or other brand owners or other retailers, we're working with every one of our customers to really try and accelerate the sustainability of our products and their products.

Chris Parkinson:

That's great color. Let's switch over, another very interesting topic and integral topic of this conference given we have had some of your competitors, is just the recovery in polyurethanes. You've seen a lot. You already mentioned the near term action into it. One of the things I just want to hit on very quickly, the view of the sustainability of the demand equation is naturally, you see the demand improvement, there's some spread improvement. How should we be thinking about auto construction? It seems like durable goods has seen a nice pickup. How should we be thinking about that for next year, and also just on the spread front, what would be your latest views?

Howard Ungerleider:

Yeah. When you think about urethanes, isocyanates, MDI specifically, that product line clearly has suffered the most since covid because of its tilt toward downstream, durable end markets. Think automotive. Think construction. Think furniture. Think appliances. Even before covid, I would say we were at a historical trough-level margins. There was just no way. The fourth quartile producer was negative cash even before covid. When you think about where we were because of covid, when you think about Dow, our polyurethanes franchise probably dipped below. The bottom operating rate was in the fifties, in the second quarter. You're clearly not making any money when you're at that level.

Now, even before covid, we started to see project cancellations and announcements of rationalization of older, smaller capacity, just like what we talked about in the ethylene chain. Now what you see since we've bought them, you've seen a lot of the durable good markets start to re-engage, right? If you think about all the big automotive production facilities in North America and Europe, they were basically all closed for the bulk of the second quarter.

Since we've seen the third quarter, there's clearly been a decent ramp in automotive production, probably even better certainly than we saw, or we thought on our second quarter earnings call. That's part of the reason why we increased our guidance today. The same is true in the construction space. Those markets have come up. You have a combination, I think, of what's happening. There was zero margin before covid. Covid dropped that into really cash losing, if you're in the third or the fourth quartile of the cost curve. Then, now, you have a ramp back of demand.

Then what typically happens is that everybody tries to run hard to meet the demand, and then these assets are old. Several of the assets have had production issues because you haven't been maintaining them for reliability. You've been maintaining them for license to operate and for safety, but not necessarily to maximize the reliability. Several of the assets around the world have had production issues, and that's allowed us not only to get some incremental margin back just because of the operating rate improvement, but now you're seeing pricing in Asia, pricing in Europe, and now pricing in North America start to move up because you have more demand than you have supply.

You just typically get that commodity response in the high society chain. That's what we're seeing. I would still say, you're far away from mid-cycle and you're really far away from where we were during the fly up in 2017. I would say, for all three of those reasons, that's why over the next several years, as demand normalizes and then we start to get back onto a GDP growth path for the world, that will deliver more earnings and more incremental margin to the bottom line for Dow.

Chris Parkinson:

That's helpful. That was actually my next question, but you've already answered it, in terms of the approach back to mid-cycle learnings and even potentially above, depending on demand. Just in the context you did mention three delayed/canceled deferrals. When we think about the industry over the next several years, and we think about mid-cycle, and as I said, potentially just over the longer timeframe, what type of pricing do you think we would actually even need to see at this juncture to even consider the two cancellations for the Europeans and the one in Asia or for Asian competitor?

Howard Ungerleider:

Look, I don't want to give any specific pricing numbers. I think that will move around a lot, depending on the raw material inputs and depending on the economic activity and everything else, all the different variables that we talked about in terms of supply and demand, both the feedstocks, raw materials, and then ultimately the downstream markets themselves. I would just say that, look, we are in ... The second quarter, this is my fourth down cycle, and the second quarter of this year absolutely felt like the fourth quarter of 2008. I would say there are different reasons of how we got there, though. Fourth quarter of '08 was a financial subprime bubble. This time we had, just before covid we had the oil drop and then covid really pounded us because of the demand destruction, especially in the markets that hit polyurethane.

Over the next several years, as we come out of this, there is a mid-cycle in front of us. Then there's a cyclical peak from there. We're still bouncing around that cyclical bottom. The third quarter is definitely going to be better than the second quarter, but it's still not going to be where we were even in 2019. It probably is going to take 2021, 2022 in that timeframe for us to get back to those pre-covid demand and pre-covid, the combination of pre-covid demand and pre-covid unit margin. That's what we probably need to get back to mid cycle. 2019 for us was not a cyclical peak. 2019 is more looking like a mid-cycle number.

Chris Parkinson:

That's very helpful. Just let's switch over very quickly to PM&C. You mentioned some brief remarks in the near term movements. There's been a lot of focus on DIY construction, so on and so forth. What are the two to three end markets we should be really monitoring into 2021 to see that business get back to normal? Then if I'm not mistaken, you've also been working on improving the long-term returns in that platform, as well. Any color in that would be greatly appreciated.

Howard Ungerleider:

Yeah. I know you're talking about silicones. The big markets are certainly construction, automotive, packaging. Those are probably the big markets for silicones. Then obviously on the acrylic side, our big market is construction, both architectural and industrial coatings. I would say, look, silicones definitely got hit hard on the construction side during the second quarter. Clearly, so did our coatings business because of the shutdowns and the stay at home orders. As we've moved into the third quarter, you're seeing improvements in both.

I would say that improvements in the architectural coating space have probably been faster than what we've seen in silicones, because silicones also goes into personal care applications. When you think about the need for makeup or the need for moisturizer or lotion, those things typically coincide with people going out and seeing people. Because we're seeing the same people over and over again in our house, and not going out as much, that's lagging a bit.

We've seen that snap back much faster in China because remember, we were in the first quarter dealing with covid in China, and the second quarter was already an improvement in China versus Q1. That gives me optimism as we get into the back half of this year and probably more like early next year in silicones. I would say the demand in the acrylic side, in architectural coatings, typically this is a seasonal low period, but we've had an extended summer season, I would say, in architectural coatings. A shout out to Neal Sheorey if he's listening. He's doing a good job.

Chris Parkinson:

Good to hear his name. I've been criticized for having my basement that's apparently a little too white, and I need to increase my palate. So, maybe I'll soon be a customer.

Howard Ungerleider:

If you want us to tell you which paints are made with Dow materials, we'll be happy to send you the list.

Chris Parkinson:

Hit me up afterwards. I appreciate it. So, let's shift over to Sadara very quickly. You had some helpful remarks in terms of your conviction, in terms of the debt service, which not naturally, all of us have been monitoring. How should we actually think about the improvements of the asset in the near-to-intermediate term? And then, you mentioned your last quarterly call, just give some additional long-term efforts to further improve feedstock flexibility, at the asset. So, just any color on those fronts would be greatly appreciated.

Howard Ungerleider:

On Sadara, the operational asset is doing very, very well. It's running hard. Obviously, it was not immune to the oil drop, and it was not immune to the COVID pandemic. So, it was dealing with both of those issues, as well.

But, in terms of our operability capability, how much asset capability there is, relative nameplate, all doing actually very well. I will give you more color on this, on our third quarter earnings call, but I do expect that Sadara's earnings this year are now actually going to be above last year. And that's because of all the self-help that they've been doing, the additional work on the feedstocks, as well. Continuing the process to sell up each of the assets. Because remember, I mean, we sold it out, and now we have to sell the asset up.

And those are all things that point to... Sadara's a really good asset. It's got leading technologies. Dow and Saudi Aramco have been great partners that are highly aligned to continue to drive it forward. Clearly, it's got a leverage issue. It's got a capitalization challenge, and that's why Dow and Saudi Aramco are working with Sadara and the lenders to re-profile the debt.

The debt was project financing, and as project financing goes, once the project starts up, it takes all of the debt to zero over about 10 years. And Sadara is now a company, not a project. So, we really need a debt structure that mirrors what a public company, or a private company debt structure is. And so, that's what we're working with the lending syndicate to do. We have achieved everything that we need to do to declare PCD. But Dow and Saudi Aramco jointly have made the decision of, as we are having

positive and healthy negotiations with the lending syndicate, we're going to hold off on declaring PCD because we're making really good progress.

And the goal is to achieve a term sheet that everyone can sign off on before the end of the year. So that, next year, and for the next several years, we've got Sadara in a place where they can continue to take their cost out. They can continue to de-bottleneck and creep their production. They can continue to sell up, and all while doing that, be cashflow self-sufficient. And so, that's what we're focused on.

I would tell you we're having regular dialogues with the export/ import credit agencies, and the conversations have been going very, very, well. I feel very good. I can't guarantee anything because it's a multi-party negotiation. I feel really good that we'll be able to get to a term sheet that everybody will be willing to accept before the end of the year. And then, we'll start 2021 in a place where Sadara will be cashflow self-sufficient. And that continues to be the goal.

Chris Parkinson:

That's great detail. Spending the last couple of minutes we have, I'd like to shift over to the balance sheet. And even during the downturn, in terms of your cost progress, working capital improvements, as well as some other items, you're always really moving in the right direction. And obviously, you've made the most of that. Just starting with, focusing on the cashflow aspect of it, how should we be thinking about working capital, operational improvements, cost savings. Do you have any additional color on that before we get into some of the one-time items?

Howard Ungerleider:

I can talk about our balance sheet all day long. I'm very proud of the work that our treasury team has done. I mean, I think we've been on offense on our balance sheet before spin. I think we spun out in a very good way. I will not say... Like the timing of you buying your house on Long Island, maybe you got lucky. So, we may have gotten lucky a little bit.

We didn't know COVID was going to happen, but we certainly knew we were in the late innings of an economic upcycle. And so, we put in a fortress balance sheet. So, I mean, if you think about what we've done this year, we continue to go to the market opportunistically. We just did this $2 billion debt neutral, or leverage neutral, raise. It moved out our debt maturities another year.

So now, we don't have any substantive maturities until the second half of 2024. We've got $3.6 billion of cash on the balance sheet. We've got more than $12 billion of committed liquidity, including that cash. We've got uncommitted liquidity on top of that. And we've been really working on cash. That was one of the things, when Jim and I spun out the company, we really worked with our leadership team.

Every one of our leaders has a P&L. So, they have an income statement. They now have a balance sheet. And they have a cashflow statement, and everybody's cashflow statement adds up to the enterprise cashflow statement that Jim and I are accountable for. We're looking at that with the leadership team and the operations team of our company every day, every week, we're looking at changes. And we're looking at making improvements in working capital that are structural, as well as the tailwinds that we've gotten so far with obviously, the lower revenue. And the lower of the lower feedstock costs.

We've delivered about $500 million of just working capital improvements in the first half of the year. We're going to do more in the second half of the year. We've also been working on the non-operating.

So, if you think about, what have we received already this year from a non-operating cash tailwind, the Olin payment that was supposed to come at the end of the year, we were able to get that in the second quarter, the Nova tax refund that we got from the Canadian government, those two alone are, just doing the math, about $700-800 million that we've already received, plus the 500 million working capital.

And then we just announced the marine infrastructure assets sale, and the rail infrastructure. Those two are more than $900 million that we should receive before the end of this year, and we're not done.

So, we're continuing to look at that. I'm very proud of the fact that even doing the margin earnings reduction, we've, up until the second quarter, been able to deliver a higher cash from ops and a higher free cashflow, than the same quarter a year ago. I can't promise that we'll be able to keep that up. But, what I can say is I am highly confident that, where we are, we have enough cash to do everything that we want to do that are our priorities.

And if you think about what our priorities are, from a capital allocation standpoint, in terms of where we are in the cycle, our first priority remains to safely run the assets that we have to meet the needs of our customers. The second capital allocation priority is the dividend. And then, the third priority is incremental de- leveraging. We've already done $740 million through the first half. And I'll be disappointed if we aren't able to do a billion dollars before the end of the year. And so, that's what we're working on.

Chris Parkinson:

The last quick question I have is the one I always like asking you after our fireside chats is, throughout your discussions with investors, or Jim's, or the IR teams. What do you think is being missed amongst the investment community? What do you believe we're being too skeptical on, not optimistic enough? What are the key puts and takes?

Howard Ungerleider:

Far be it for me to second guess our owners, I think our owners are smart people and they ask great questions. I think people, as we were going through the second quarter, I think their concern was how bad can it get? Where is the bottom? I think that was the question that people had. I mean, our stock and the whole market went down dramatically in that March/April/May timeframe.

And I think what what people are seeing is a rebound in China, and now a reopening and reasonable demand, given what we all expected in Europe and North America, and even Latin America. And so, now I think the conversation is pivoting away from how bad can it get, to what's the earnings power of the portfolio? And, when will that earnings power manifest itself to the P&L and the cashflow statement.

And I would say, what we're focused on is, with the team, managing through a difficult period. And I think we managed through the second quarter very well, we're working to do the same thing. Like the shampoo bottle says, wash, rinse, and repeat. We're working to do the same thing in the third and the fourth quarter.

And then, I think as we get into 2021 to the 2023 period, I think the potential is really there to move to mid-cycle. And I'm not going to make a prediction of when that is, but I think at some point in the next

few years, we will be moving toward a mid-cycle number, and that's all we're focused on, meeting the needs of all of our stakeholders.

Chris Parkinson:

Howard, as always, I'd like to personally thank you for joining me here today. It's always a pleasure to have these discussions. I'd like to thank the rest of your management team, as well as the IR team for making this happen. And I certainly look forward to hosting you again soon.

Howard Ungerleider:

Us, too. Thanks, Chris. Appreciate the opportunity.

Chris Parkinson:

Thanks, Howard.