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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to the Covestro Investor Conference Call on the Q2 2019 Results. The company is represented by Markus Steilemann, CEO; Thomas Toepfer, CFO; and Ronald Koehler, Investor Relations.

(Operator Instructions) I'd now like to turn the conference over to Ronald Koehler. Please go ahead, sir.

Ronald Koehler Covestro AG - Head of IR

Good afternoon, and welcome to our second quarter conference call. For your information, we have posted our half year financial report and the conference call presentation on our website. We assume you have read our safe harbor statement.

With that, I would now like to turn the conference over to Markus.

Markus Steilemann Covestro AG - CEO, Chief Commercial Officer & Chairman of Management Board

Good afternoon, everybody. The second quarter developed in line with our expectations. The year-on-year comparison continues to look weak. However, we see a stabilization of margins since Q4 2018 based on sequentially flat prices for the group overall.

A strong achievement this quarter is certainly the positive core volume growth of 1.1%. It demonstrates our capability to compensate a very weak development of the automotive industry and even withstand weaker demand across industries overall.

Our EBITDA decreased significantly in a year-on-year comparison but stabilized nicely quarter-on-quarter. On the cash side, we took countermeasures to limit the seasonally higher working capital. Thus, we could achieve a solid operating cash flow under the given circumstances.

Based on this set of results and despite continuously challenging economic conditions, we confirm our full year 2019 guidance.

Now moving to Page #3, let me provide some more insight into our core volumes development by regions and industries in the second quarter of 2019.

NAFTA was the best growth region this quarter. We achieved a strong core volume growth of 6%, despite declining auto production in the United States.

Double-digit growth in construction, wood and furniture, medical and other smaller customer industries was able to more than compensate the weak development in automotive and electronics. Asia Pacific suffered from the economic slowdown. The weak demand led to negative core volume growth in automotive and construction. Still strong volume growth rates in electronics and wood and



furniture compensated the development and enabled us to post positive growth of 2%.

Europe, Middle East and Latin America suffered the most from the weak automotive industry. Additionally, a weaker industrial production in Germany led to volume declines across several industries.

This negative volume development could not be compensated by volume growth in construction and wood and furniture. Overall, we are satisfied to see that our diversification across industries and regions helps us to counteract the current weakness in the automotive industry and allows us to manage a challenging demand environment.

I now hand over to Thomas for the full set of financials.

Thomas Toepfer Covestro AG - CFO, Labor Director & Member of Management Board

Thank you, Markus, and good afternoon also from my side. I'm on Page 4 of the presentation where you have the sales bridge and you see that we have posted a year-on-year decline of 16.9% in terms of sales. However, I think it's worth noting that sequentially the sales increased by 1.1% relative to Q1 2019.

If you look at the chart, you see that the main driver was the price effect was declining and deteriorating prices in MDI, TDI and also PCS, reducing our sales by a total of EUR 724 million. You see that there was a positive volume growth contribution of EUR 33 million and the FX effect added some EUR 68 million and that's mainly attributable to the U.S. dollar.

Finally, you see that there is a portfolio effect of negative EUR 29 million and there's 2 things in this bucket. First of all, it reflects the negative effect from the divested U.S. polycarbonates sheets business, which we sold in Q3 2018 and there's a positive effect included from the stake increase from 50% to 80% in the Japan-based company DIC Covestro Polymer Limited, in Q2 2019, which we report at our CAS segment.

So with that, let's turn the page to Page #5, where you see the EBITDA bridge. And as you can see on the right-hand side, we achieved an EBITDA of EUR 459 million for the second quarter, which is in line with our guidance and also as forecasted, the higher competitive pressure in polyurethanes and polycarbonates led to a continued decline in contribution margin. And therefore, you see a negative pricing delta, which amounted to EUR 636 million in this bridge.

The volume effect is almost negligible and so is the FX effect. And if you look to the other items, you see a positive effect of EUR 94 million and the main contributors were the lower cost driven by lower bonus provisions followed by a positive impact of EUR 31 million stemming from the adoption of IFRS 16 and also, the onetime effect from the remeasurement gain of EUR 19 million in connection with the acquisition of DCP, which I just mentioned is in here. What we also had was a negative effect from restructuring costs related to our Perspective program and that was in the same order of magnitude as the positive EUR 19 million from DCP.

So overall, the macroeconomic environment has not improved compared to the fourth quarter of 2018. The strong price and margin pressure remains. However, we achieved a slight volume increase, which we believe was a good result.

And overall, I would like to say at this point that, of course, we do pursue a price volume strategy that maximizes the absolute EBITDA of the company.

So with that, let's turn to Page #6 where you see the sequential development of the group results. And I think the highlight of this page is the stable EBITDA margin of around 14%, which you see on the lower part of the page for the last 2 quarters. Again, just as a reminder, the strong price decline, which has reduced our margin started in Q4 2018 with selling prices down by 9.3% year-on-year in Q4. And then in Q1 and Q2 2019, the selling prices declined by 18.3% and 18.7%, respectively.

However, sequentially, we saw only a minor selling price decline in the second quarter of 2019.

And with that, I would like to hand it back to Markus for the segment details.

Markus Steilemann Covestro AG - CEO, Chief Commercial Officer & Chairman of Management Board

Thank you, Thomas. We are now going to Chart #7 and talking first about polyurethanes.

In the second quarter, we recorded slightly increasing core volumes. Strong core volume growth in TDI compensated for a weaker MDI performance, while polyols remained on prior year's level.

The lower MDI volumes were driven by our limited availability due to a scheduled maintenance shutdown in China.

In our view, the MDI market growth remained healthy. Overall, industry utilization stays at low level driven by the additional capacities adding during the last 12 months.

For MDI, prices were moving up and down in the last months, reacting to short-term effects like for example, several maintenance shutdowns in China end of April, or destocking and restocking measures by customers.

Due to the current volatility in the industry and the low visibility on demand development, we stay cautious about the further development during the course of the year.

Mid-term, we expect that the current overcapacities will be absorbed by growing market demand.

For TDI, the industry environment remains under pressure, also in the second quarter. Margins did not move away from their low point as a consequence of significant capacity additions in the industry. On the positive side, we see limited further downside risk as we believe that high-cost producers are currently operating at cash-break-even levels.

Finally, margins in polyether polyols continue to be below the long-term average mainly driven by weak U.S. market.

Overall, the EBITDA margin of 11.6% in PUR in the second quarter was clearly below last year's level, primarily driven by significantly lower MDI and TDI margins.

Taking a quarter-on-quarter perspective, we see a slight improvement driven by a higher MDI margins and higher TDI volumes.

Now let's turn to polycarbonates. In polycarbonates, we recorded a solid core volume growth of 4.4% in the second quarter. The demand drop in automotive could be compensated by strong volume increases in construction, electronics, medical and other smaller industries. Prices were clearly below the level of previous year after continuous price drops in all regions, mainly in the commodity businesses.

Consequently, net sales decreased by 15% year-on-year. The EBITDA margin came in significantly below previous year's level, impacted by the negative pricing delta. In a quarter-on-quarter comparison, the segment margin slightly decreased due to continuing price pressure.

Thanks to our position as cash cost leader in the industry, we have some flexibility to switch sales from one application and industry to the other, thus helping us to counteract short-term weakness in one industry.

Turning to Page to coatings, adhesives and specialties on Chart #9. The impact from globally weaker demand became most visible in our coatings, adhesives, specialty segments. Core volumes declined in almost all customer industries, thus, we recorded a negative core volume growth of 4.7% in the second quarter.

In consequence, net sales declined by 1.3% year-on-year, although prices stayed almost flat. Positive effects from currency and the portfolio impact from DCP could not fully compensate the volume loss.

EBITDA increased by 7.9% versus second quarter 2018, mainly helped by the remeasurement effect of DCP. The underlying business

suffered from the negative volume leverage.

For the full year 2019, we confirm our guidance on core volume growth, based on an assumed catch up in the second half. However, the risks are increasing given the weak start into the year and the current macroeconomic uncertainties. The segment should continue to deliver an EBITDA margin of above 20% and strong free cash flow.

Thomas will now explain more financial details.

Thomas Toepfer Covestro AG - CFO, Labor Director & Member of Management Board

Yes, I'm on Page 10 of the presentation where you see the details of the free operating cash flow development and the first thing that I would like to state is if you look at the first half year, the numbers were characterized by 2 phasing effects related to fiscal year 2018.

First of all, the cash out of around EUR 350 million for the 2018 bonus payment and secondly, roughly EUR 100 million for higher cash taxes compared to the P&L taxes. And in addition, let me remind you that the end of the first half is obviously, the seasonal peak in terms of the working capital.

However, talking about working capital, effective countermeasures reduced the working capital buildup and therefore, we were able to generate a positive operating cash flow of EUR 274 million. So broadly speaking and disregarding the mentioned 2 phasing effects, we were on a comparable free operating cash flow level as we had seen it in the first half of 2016.

What I would also like to mention is that in our Q1 conference call, we guided for a significantly more negative free operating cash flow in the second quarter compared to Q1.

However, thanks to the working capital improvement measures, we managed to come out better than expected. If you look at the chart, you'll see a negative EUR 98 million, so working capital buildup which is significantly less than the buildup in the first 6 months of 2018. But more importantly, if you look at our quarterly report, you will see that in Q2 itself, we actually released working capital and generated a positive effect from a reduction of working capital of EUR 159 million.

So with those measures, working capital to sales ratio was reduced to 18.4% at the end of H1, and this is a lower level compared to the first quarter of 2019, and it is also a lower level relative to the first half of 2018.

So that for the full year of 2019, we assume that we can continue to reduce our working capital with a beneficial effect on free operating cash flow, and we expect to finish the year in the targeted working capital to sales range of 15% to 17%.

Talking about the full year, obviously lower EBITDA and higher CapEx will continue to influence our free operating cash flow. However, after having digested the cash phasing effects that I mentioned, which are related to 2018 in the first half, we should be able to generate a solid free operating cash flow in the second half of 2019. And overall, we see ourselves on track to deliver on our guidance of a free operating cash flow between EUR 300 million and EUR 700 million.

So with that, let's turn the page to Page 11, where you see the net debt development. On June 30, our total net debt level increased to EUR 3.3 billion and you see the key effects in the bridge. First of all, the dividend payment of EUR 438 million, secondly, the effect from the adoption of IFRS 16 with EUR 642 million, and finally, you see that the pension provision increased, again, by EUR 259 million and that's mainly due to lower discount rates in Germany.

So in combination with a lower EBITDA, these developments led to an increased ratio of total net debt-to-EBITDA to 1.6x at the end of June 2019 compared to 0.6x at the end of 2018.

And in this context, I would briefly like to mention that on July 2, Moody's confirmed our Baa1 rating with a stable outlook and likewise, ourselves, we do continue to regard our balance sheet as being very solid because the main increase in the total net debt has been triggered by accounting changes since the beginning of the year.

So that leads me to our full year guidance on Page #12. We reiterate our guidance of a low to mid-single-digit percentage year-on-year increase in core volumes.

In the first half of the year, we posted a small decline of negative 0.4%. We continue to assume a catch up in the next 2 quarters helped by a lower comparison basis and more available capacities after we have digested the peak of our maintenance shutdowns in the first half of 2019.

We confirm the EBITDA expectation of between EUR 1.5 billion and EUR 2.0 billion for 2019. The mark-to-market analysis at current price levels indicates an EBITDA of EUR 1.6 billion to EUR 1.7 billion and the reduction compared to our last mark-to-market calculation of EUR 1.8 billion is driven by both, somewhat slightly lower margins and also slightly reduced volume assumptions for the full year.

At this point, I would like to remind you the mark-to-market analysis as a snapshot at today's prices, it is not a specific guidance for the year, which is our range of EUR 1.5 billion to EUR 2 billion.

As explained on the previous charts, we also confirm the free operating cash flow guidance delivering between EUR 300 million and EUR 700 million. And for Q3 2019, we assume an EBITDA of around EUR 410 million, that means that sequentially we assume further declining margins, which cannot be fully counterbalanced by somewhat higher volumes and please note, in this context that "around" implies a single-digit percentage deviation both potentially upward or downward.

And with this, back to Markus for the summary.

Markus Steilemann Covestro AG - CEO, Chief Commercial Officer & Chairman of Management Board

Thanks, Thomas. So the second quarter developed in line with our expectations. We achieved positive volumes in a challenging economic environment. The diversification of our sales towards several customer industries and the capability to switch volumes rapidly from one industry to another, thanks to our cost leader position enabled us to counteract the automotive industry weakness.

Our EBITDA stabilized quarter-on-quarter, based on a broadly flat selling price. We demonstrated in the second quarter, how we manage our working capital with efficient countermeasures to alleviate the seasonal peak and compensate the negative phasing effects. Our cost savings program Perspective is fully on track. Additionally, our continuous focus on innovation and sustainability lays the foundation to defend our industry and cost leadership for the long term.

In light of the first half year results, we fully confirm our guidance for the full year. It might be too early to call it the bottom of our earnings now, but at least earnings have stabilized quarter-on-quarter. We also expect only a slight further decline of earnings in Q3 compared to Q2 thanks to our strict cost discipline. Overall, we currently operate in very challenging markets characterized by oversupply due to increased capacities and simultaneously weakened demand. As a consequence, our earnings in 2019 remain below mid-cycle levels, but still meaningful above our cost of capital.

We continue to assume that under mid-cycle conditions, we generate a return on capital employed after tax of 15%. In between, we will work on all internal levers to counterbalance the market-given circumstances. Creating long-term shareholder value remains at the core of any decision, especially with regards to the use of cash.

With that, we would like to thank you for your attention and are glad to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And the first question comes from Mr. Christian Faltz calling from Kepler Cheuvreux.

Christian Faitz Kepler Cheuvreux, Research Division - Equity Analyst

A couple of questions for my side, please. I'm fully aware and I'm actually glad that you don't run your business on a quarterly basis, still what is behind the observation that CAS has seen the weakest growth in Europe ever since your stock market listing in Q2? That is question number one. And then second, it seems to be a long way from your H1 free cash flow generation as good as it might have been on a comparable basis to your fiscal year-end target of EUR 300 million to EUR 700 million. Can you give us a sort of bridge how to get there in the second half?

Markus Steilemann Covestro AG - CEO, Chief Commercial Officer & Chairman of Management Board

Yes, Christian, this is Markus speaking. I give it a shot on the first question, the so-called historical weak quarter that you have mentioned for our coatings, adhesives and specialty business is primarily driven by the demand patterns that we see on a broad-based industry weakness and here, in particular, the coatings market and here, in particular, the exposure to the automotive business. If you take for example, PPG, which reported minus 5% and always volume-based on business development, and if you also take Akzo, another industry player, here was minus 7. I think with our core volume development in the coatings, adhesives and specialty business, we are somewhere in the middle, let's say, of the quarterly development in the respective industries and that's why I would see this more in line with what the broader industry development shows, rather than a very specific topic for our business only. Again, as I said, basically driven by general industry demand and here particular, the automotive industry demand. For the second question on H1 cash flow, I would like to hand over to Thomas.

Thomas Toepfer Covestro AG - CFO, Labor Director & Member of Management Board

Yes, Christian. 2 things that I would mention. First of all, the phasing effects obviously for the second half of the year will fall away, as I said, EUR 350 million bonus payment for 2018, which don't belong into '19 and also EUR 100 million cash payment above the P&L tax rate obviously will not repeat themselves in the second half of the year. And secondly, the working capital will be a contributor to our cash flow. Let me just remind you in the second half of 2018, we had working capital savings or a positive contribution from working capital of more than EUR 400 million. We're assuming less than that in the second half of 2019. But still let's say a sizable positive effect and if you take those things together, we feel comfortable that we will achieve the range of EUR 300 million to EUR 700 million.

Operator

The next question comes from Thomas Swoboda calling from Societe Generale.

Thomas Swoboda Societe Generale Cross Asset Research - Research Analyst

I have 2 questions, if I may, please. Firstly, on the potential drought in Europe this year, again, do you see a risk there to face the low Rhine water levels this year, again and if so is anything you can do to prepare? And the second question is on CapEx. I mean you have quite a sizable CapEx program going forward. It does not seem that the economy is bouncing back, again, very soon. My question is, what would make you reconsider the speed and the amount of the CapEx you want to spend over the next 3 years?

Markus Steilemann Covestro AG - CEO, Chief Commercial Officer & Chairman of Management Board

Thomas, this is Markus speaking. On your first question and also growth patterns in Europe and here particularly, Rhine river levels, if you look at our growth rates in Europe, in the first half of the year, we still think that this overall situation will not significantly change in the second half. But that is also included in our guidance that we have given. If you now particularly look at Rhine river levels as of last year, in Q4 you could say that in 2018 we had an effect in terms of EBITDA of roughly EUR 50 million plus/minus and for sure, we have taken the experience of last year into consideration. What does that mean? You have 4 major modes of transportation, one is pipeline and we're talking about railway, we're talking about trucks and we're talking about ships. And the Rhine river level, for sure, affected the ship transportation. So for this year, we prepare ourselves as good as we can to compensate as much as we can potential impacts of lower Rhine River levels. However, we could never ever fully compensate if all ships would not be able to ship the Rhine River. And if this would take on for longer, however, we have opportunities here in pipeline, in trucks and also, in railway cars, to partially compensate it, in particular, if it's just the short-term topic and also on very short term, we could also do something on inventory levels on the raw material side and also on the finished goods side. But that is also limited in terms of how long we can do that and that is actually what we are preparing for. We currently do not have as anyone, any idea how the Rhine River levels will develop. However, if it gets as worse as last

year, we, I think will be better prepared.

With that, I would like to hand over to Thomas for your second question.

Thomas Toepfer Covestro AG - CFO, Labor Director & Member of Management Board

Yes, Thomas, with respect to CapEx, I mean, let me say a little bit bluntly. Of course, we're not stubborn and just stick to our CapEx numbers without looking left and right what is happening in the economy. We monitor this very closely and therefore, we have a very, I would say, clear review of all the CapEx projects and check whether they make sense strategically and whether they add value. And we do this review in autumn in connection also with the business planning. However, on the other hand, I think, it's fair to say we do have 7-year CapEx cycle, so we cannot steer the business on a short-term notice for those kind of projects. And therefore, in terms of flexibility, I would say, the EUR 900 million that we've indicated for this year, are pretty much fixed. In the outer years, of course, we do have flexibility and I think, we've proven this in the past that if really we should face a prolonged and deep recession, we can, of course, stretch projects or take products out, especially in the outer years. But again, I think we have to balance the strategic ambition because the CapEx is the foundation for future growth and in the long term, we do see that the markets that we serve, especially with MDI, but also with the other product have a solid and secular growth rate above GDP and therefore, that justifies also a CapEx program.

Operator

The next question comes from Mr. Neil Tyler calling from Redburn.

Neil Christopher Tyler Redburn (Europe) Limited, Research Division - Research Analyst

And a few for me, please. Firstly, within the restructuring, when the topic of restructuring, you mentioned that the additional costs year-on-year broadly offset the revaluation gains, so around about EUR 19 million. And can you talk through what you saw as the year-on-year benefit of savings achieved in the second quarter? And also how you expect both of those figures to develop in the second half of this year? That's the first one.

And secondly, probably more briefly, I think, I've missed your earlier comments on the contribution margin and why that remains very low, so I wonder if you could help me with that, please.

And then the final question, in your mark-to-market, I think, you said that you assume lower volume assumptions. But you also mentioned that you've seen a volume catch up in the second half. So I guess, my question there is within the guidance as opposed to mark-to-market and if volumes don't recover, can you still achieve the low end of that guidance?

Thomas Toepfer Covestro AG - CFO, Labor Director & Member of Management Board

Yes, let me maybe start with Perspective program.

So I mean, to put into context we said, we want to with Perspective you want to say EUR 350 million and cumulative cost savings up until the year 2021. And we're on a good track to achieve cumulated savings of EUR 140 million in 2019, which is EUR 92 million more than what we had in 2018. And on the restructuring costs side, we're expecting roughly EUR 50 million for Perspective to be incurred in 2019. Now in terms of what is the ramp up of the EUR 92 million that I just mentioned, it's somewhat back-end loaded because a lot of it is related to personnel, and we're releasing personnel, but it takes a little while before it really flows through as a full year effect in our P&L. But in terms of the trajectory, I would say, we're fully on track to deliver the numbers that I just cited.

Neil Christopher Tyler Redburn (Europe) Limited, Research Division - Research Analyst

Okay. Is it fair to say that the cost is more front-end loaded, therefore?

Thomas Toepfer Covestro AG - CFO, Labor Director & Member of Management Board

Yes. I think it's fair to say. Yes. Yes. Sorry, Neil, can you repeat your second question? We're just scratching our heads a little bit. Can you say that again?

Neil Christopher Tyler Redburn (Europe) Limited, Research Division - Research Analyst

Yes. Sorry. Second one, in terms of the contribution margin, the drop-through into EBITDA from the volumes seem to be relatively low. I think you made some comments as to why that was? I apologize I think I missed it.

Thomas Toepfer Covestro AG - CFO, Labor Director & Member of Management Board

Yes. Well, I mean, in general, we say that we have a relatively clear volume drop-through of some 40% in terms of EBITDA. Now what we're looking at here is very small numbers. So -- and I think it's a little bit erratic because of the small number effects. Remember in Q1, our EBITDA effect was 100% of the volume. And this time, it's a little lower, simply because there's some mix effects playing into it. Simply, it is really due to the low -- due to the small absolute numbers. In general, our drop-through is unchanged from what we've seen last year.

Markus Steilemann Covestro AG - CEO, Chief Commercial Officer & Chairman of Management Board

Maybe Neil, on your third question, you asked about the mark-to-market and also that we have clearly said that our volume assumption still within the guidance are a bit lower. But if you take everything, let's say, as we look at it today, we would need something like 6% volume growth in the second half year-on-year, but please consider in this context that we have also a lower starting base, in particular, looking at the fourth quarter of last year, so the places that we really compare and let's say, for the midpoint, again, to reiterate that in terms of the guidance that we have given 6% is what we have assumed. So if you then go now and that was what your question was about would touch under these assumptions the low point of the guidance, we would talk about 3% volume growth, but again, based on the mark-to-market snapshot so to say, so anything that would be positive on prices would then give also further room to maneuver on the volume side. So mark-to-market, based on July prices, 3% would be more point towards the low point. So but again, even that would be still covered by the EUR 1.5 billion to EUR 2 billion range to be very clear.

Operator

The next question comes from Geoffrey Haire calling from UBS London.

Geoffrey Robert Haire UBS Investment Bank, Research Division - MD and Equity Research Analyst

It's Geoff Haire here. Just want to ask a couple of questions. Just on the volume drop-through in the bridge. It fell to 15% in the quarter. I appreciate it's small numbers, but does that imply that you were selling a lot more commodity product than and specialty product through the group? Is that the reason for the low volume drop-through? And secondly, just I wonder if you could comment on how you left the second quarter from a volume or demand point of view to enter the Q3.

And then finally, just on the cash flow, if the free cash flow you generate is below the dividend payments, can you borrow to pay the dividend?

Thomas Toepfer Covestro AG - CFO, Labor Director & Member of Management Board

Yes, let me tell. I mean first question, your question was did we sell somewhat lower on what commodity-type products and I think the answer is yes because what is happening obviously is that especially in PCS, the automotive industry is weak and we're shifting volumes into other industries. In automotive, we have high specialized products, co-engineered with the OEMs, et cetera. But we have very nice prices and also very resilient margins, but obviously, the volume is going down, and we're shifting this to some extent into, let's say, lower margin applications and that is also what you see in the volume bridge here.

Markus Steilemann Covestro AG - CEO, Chief Commercial Officer & Chairman of Management Board

This is Markus speaking. On your second question, can you just repeat it because I think we had somehow difficulties with the lines. We're not sure whether we fully caught what you tried to express.

Geoffrey Robert Haire UBS Investment Bank, Research Division - MD and Equity Research Analyst

Sorry, it's probably my accent. I just want to know how you'd entered Q3 leaving from Q2 from a demand point of view. Was it higher or lower than you started Q2?

Markus Steilemann Covestro AG - CEO, Chief Commercial Officer & Chairman of Management Board

Well, generally speaking flat. So that's what you could see. There is some slightly nuances here and there, but I would say, generally speaking, we started flat. But let me also maybe help you to build a bridge in terms of the volume demand also in Q3. We were in our businesses sold out in second quarter. And if we're now entering into third quarter, what gives us the additional push is not that we see an increase in demand, but we are able to deliver more because we have less shutdowns. Because the first half of the year and also second quarter were still or can be still described by maintenance shutdowns. So we have higher availability of volumes. And that's why we also are positive about that we can sell more because the demand side for us in the second quarter was not the limitation, but the supply side. And that's why we are with more supply availability on our side also given our positions in the market with customers, we believe that we also can sell more. And that is from our perspective also helping us in the third quarter.

Thomas Toepfer Covestro AG - CFO, Labor Director & Member of Management Board

And then to your last question in terms of the relation between free operating cash flow and dividend. And what I would say is we have made a very clear commitment that we want to keep our dividend at least stable. And if you look at the free operating cash flow, I'd say the midpoint of our guidance should, therefore, also fully cover a respective dividend payment. But even if that was not exactly the case, then I would say we would not have spent the free operating cash flow in the way of our dividend commitment, especially as in 2019, it is driven by several onetime effects that I mentioned, which belong to 2018. So we were probably in one way or the other bridge that gap.

Operator

The next question comes from Chetan Udeshi calling from JPMorgan.

Chetan Udeshi JP Morgan Chase & Co, Research Division - Research Analyst

Just couple of questions. Just on Q3 guidance, can you maybe give some color by the 3 key product segments or maybe even CAS if you want, so TDI, MDI, polycarbonates and CAS, how do you see the development there for each of those businesses? And then I had a question on the comment made previously during the opening remarks that the climate is challenging and you guys will take whatever it needs to improve the business? And frankly, when I look at the pricing development, only been weak across the board, or it's been incrementally weakening since the end of last year and now you're talking about volume growth slowing down. So I'm just wondering what is sort of internal strategy to cope with this current environment because you also said at the same time that you don't want to change something on CapEx in the short term as well.

Thomas Toepfer Covestro AG - CFO, Labor Director & Member of Management Board

Yes, let me maybe take your first question, Chetan. So I mean, just roughly speaking, I would say, if you go through the segments, in CAS, obviously, you have to strip out the EUR 19 million revaluation effect, which will not repeat itself. And if you project CAS into Q3, otherwise, I think it's a pretty stable development in terms of EBITDA. And then I would say, our PUR segment also we expected to be broadly stable and maybe a slight decline in PCS due to ongoing pricing pressure that we see, especially in Asia. This is broadly speaking the development that leads you from the result in Q2 to the -- around EUR 410 million that we indicated for Q3.

Markus Steilemann Covestro AG - CEO, Chief Commercial Officer & Chairman of Management Board

Yes. And Chetan may be on your second part, I hope that I hit the nail here on the head because I was not absolutely clear what you're referring to, short- or mid-term topics on let's say, climate challenging. I think what we have observed and what we're currently striving for is in the third quarter, we are able to deliver more, particularly because we have more volume available. Secondly, you could say that we somehow see first signs of things bottoming out as we also stated earlier in our presentation. Some of the high cost producers are now really reaching the point where they would burn cash if they would continue. So that is also helping a little bit and that is slightly differently pronounced in the different product groups. So let me also give you here some ideas. On MDI, I think we could observe that we are kind of bottoming out in terms of pricing. On TDI, yes, there's still some room that prices might be lowered a little bit, but here I would again, reiterate that we have a leading cost position and many producers are really hitting now the point of where they would be cash negative. And on polycarbonate, we see still that prices might further decline, but also, here some producers are hitting already cash costs. So from that perspective, also here limited downturn and if you look at our product portfolio, we have taken a quite strong hit on the higher specialized rates. But we were still able to shift you to our cost leadership. Volume growth towards the higher commoditized arenas and areas, so that is currently the overall situation.

So bottom line is, we feel very well prepared to deal with this challenging climate, and we also feel very well prepared to deliver volume growth and with that also deliver the best option of volume and price to deliver absolute EBITDA. And that is exactly what we're striving for and here I believe that we are better positioned than many other players due to the strong and broad geographical footprint, but also industry footprint that we are having.

Operator

(Operator Instructions) The next question comes from Tom Wrigglesworth calling from Citi.

Thomas P Wrigglesworth Citigroup Inc, Research Division - Director and Chemicals and Basic Materials Analyst

A couple of questions, if I may. Small ones, hopefully. Just with regard to the comments, just following up there on your comments by product, can we take it that your sense is that tonnes are now leaving the market in the 3 major product classes? And I guess, in that context, you obviously gave Capital Markets Day kind of supply outlook. Have you seen any major project deferrals across any of the major 3 products just the supply response, any color there would be helpful.

And the second question on CAS, small one. I think you called out HDMA outages as a challenge in the first quarter. Is that now behind us and we're looking at CAS margins and top line without any HDMA back in under normal conditions?

Markus Steilemann Covestro AG - CEO, Chief Commercial Officer & Chairman of Management Board

Tom, this is Markus speaking. On your first question, we can at least assume because we have strong hints that there is a lower utilization rate as earlier stated by high cost producers as they're now hitting really their cash cost margins. We have no signs of any complete shutdown, neither temporarily, or forever. You might, however, have seen that there was an announcement by, for example, Trinseo that they would do a complete review considering all strategic options of their polycarbonates plant here in Europe and also another sign is that different from past years, China has taken off polycarbonates of their other so-called incentive lists of materials that they encouraged industry to invest in. And we also see a slower ramp up of new capacities, so the initial estimate based on announcement of 11%, maybe now down to only 5%. Just to give you a hint here also on polycarbonate. So there is a lot of things going on, but there's definitely no signs of complete shutdowns in the respective industry. So...

Thomas P Wrigglesworth Citigroup Inc, Research Division - Director and Chemicals and Basic Materials Analyst

Sorry, Markus. The 11% -- sorry, just for clarity. The 11% to the 5% number, that's the supply growth for 2019, is that -- sorry, that you just quoted?

Markus Steilemann Covestro AG - CEO, Chief Commercial Officer & Chairman of Management Board

Global supply growth in 2019 for polycarbonates, correct. But, again, it's rough numbers because this is extremely difficult to really judge on that. But all we have in terms of market intelligence indicates more towards the 5%, rather than towards the announced 11%. As you know, there's always some challenges bringing things up on stream, running the plants technically, delivering in spec and so on, and so forth.

On your second question, yes, a bit more complicated. I try to make it as simple as possible, less auto demand means less demand on nylon 6,6. That means there is due to that less demand on nylon 6,6 more HMDA available. However, there will be a bigger maintenance shutdown from a company called ButaChem a maintenance shutdown in September and that is absolutely critical because that could lead to an additional shortage in the market. So keep fingers crossed that this works well, but currently, the overall short-term situation is less stressed than it looked at the beginning of the year.

Operator

The next question comes from Sebastian Bray calling from Berenberg.

Sebastian Christian Bray Joh. Berenberg, Gossler & Co. KG, Research Division - Analyst

I just have a quick factual one. Could you please give us a reminder of the relative auto exposure across CAS polycarbonates and polyurethanes?

Thomas Toepfer Covestro AG - CFO, Labor Director & Member of Management Board

Well, I mean, just briefly, the auto exposure for the entire group is just below 20% of our sales and for PCS, it's 1/3 of their sales and I think the others and CAS's I would say within group average. So that PUR is a little less.

Operator

And the last question for today comes from Isha Sharma calling from MainFirst.

Isha Sharma MainFirst Bank AG, Research Division - Analyst

Quickly, please correct me if I'm wrong, but you said that you have seen higher margins in MDI quarter-over-quarter, I'm guessing and could you please put some color as to why that is? Is it because of the shutdowns that you have seen and therefore, limited availability for just the quarter, or is it something that you see as a trend going forward? Also, if you could please talk about the end market trends a bit region wise, especially for North America, if you see any weakness there, or are the prices still sticking?

Markus Steilemann Covestro AG - CEO, Chief Commercial Officer & Chairman of Management Board

Isha, maybe on your first question, so the -- if you took the full quarter view, we had higher MDI prices in April and here, in particular, in China and that was also is somehow coming together with what we would call the peak of the maintenance shutdown and therefore, also some restocking. Now prices came down, again. So that was just a short peak and that was predominantly what has driven the quarterly margins higher than we have seen them in the first quarter. So from that perspective, we would not see this as a long-term trend now already, but rather a peak in the second quarter and now we are back to the levels that we more or less have seen beginning. So having said that, I would like to turn to the second question.

So what was very strong actually in the quarter-to-date, we have seen strong construction in North America, the development. We have seen strong wood and furniture, whereas, automotive as globally, you have seen the picture was a negative. Just to give you an indication, in construction double-digit growth, and for wood and furniture double-digit growth, and in automotive and transportation from our perspective, a higher single-digit negative growth, just to put some flavor on that. And we do currently not see to those numbers a significant change moving forward into the third quarter.

Operator

And we have one more question from Sebastian Satz who's calling from Barclays.

Sebastian Satz Barclays Bank PLC, Research Division - Director

And so just 2 quick ones and both on volumes actually. In polycarbonates, you saw a big swing in terms of the volume growth. It was minus 6 in the first quarter, but then plus 4 in the second, even though I don't think the end markets have changed a great deal. So could you just elaborate please what happened there?

And the second question is a follow-up. Did I understand you correctly that you need to deliver 6% core volume growth to come out at EUR 1,650 million EBITDA for the full year? And if so could you just give us a little bit of an idea what gives you confidence you can achieve that because I don't think you have delivered that kind of growth over the past 2 years?

Markus Steilemann Covestro AG - CEO, Chief Commercial Officer & Chairman of Management Board

Okay. Maybe on your first question, it is simply not always so easy to immediately shift between different industries when you are reacting to respective drop in demand and that's why it took us a little bit of time to shift from the significant decline in the automotive industry to industries like construction or industries like electro and electronics, which in the end of the day have more than compensated the decline in the automotive industry. It just takes a little bit of transition time and that is exactly what you have seen in the first quarter to shift significant volumes from the automotive industry into the respective other industries, but in the end of the day, we managed it successfully, and so far we do not have any indication that we will not continue to manage this successfully.

And on the second question, I will hand over to Thomas.

Thomas Toepfer Covestro AG - CFO, Labor Director & Member of Management Board

Yes. Sebastian, maybe just to put the numbers into perspective. So the 6%, purely as a pure mathematical exercise, if you take 6% for the second half of the year, that brings roughly 3% for the entire year. And we've just named this number because 3% would be the mid-range or the midpoint of our guidance that we have given for core volume growth, which is low to mid-single-digit and therefore, that is the only reference how it's related. It's not directly related to the guidance of the EBITDA, and it's not directly related to the mark-to-market that we've given.

Operator

Mr. Koehler, there are no further questions at this time. Please continue with any other points you wish to raise.

Ronald Koehler Covestro AG - Head of IR

Thank you very much for your participation and for all your interesting questions. As usually, the IR team is ready for any more questions you might have. And then we are happy to talk to you later with Q3 results. See you then. Bye-bye.

Operator

Ladies and gentlemen, this concludes the investor conference call of Covestro. Thank you for your participation. You may now disconnect.

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