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Q3 2018 Covestro AG Earnings Call

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to the Covestro Investor Conference Call on the Q3 2018 results. The company is represented by Markus Steilemann, CEO; Thomas Toepfer, CFO; and Ronald Koehler, Investor Relations. (Operator Instructions)

I would now like to turn the conference over to Ronald Koehler. Please go ahead, sir.

Ronald Koehler ***Covestro AG - Head of IR***

Thank you. Good afternoon, and welcome to our Q3 2018 conference call. For your information, we have posted our Q3 interim statement and the conference call presentation on our website, and we assume you have read our Safe Harbor statement.

I would now like to turn the conference over to Markus.

Markus Steilemann ***Covestro AG - CEO & Member of Management Board***

Good afternoon, everybody. This quarter, we delivered solid results despite several headwinds from internal as well as from external factors. Thus, core volume growth was broadly flat with 0.2% in Q3.

Thanks to a strong volume leverage and despite a negative pricing delta, we defended the high EBITDA level of the previous year's quarter. Additionally, helped by our ongoing share buyback program, we achieved a 7% year-on-year earnings per share increase.

Based on the solid results achieved during the first 9 months and despite the increasingly challenging economic conditions, we confirm our full year 2018 guidance. In addition, I would like to highlight 2 major projects that support our long-term profitable growth.

Firstly, we decided to invest into new world-scale MDI plant. We announced this investment 2 weeks ago. Secondly, we are today announcing a new efficiency program called Perspective. Combined with the carryover savings from the existing performance enhancement program, we now target cost savings of EUR 350 million by the year 2021.

During Q3, we faced 3 unexpected headwinds. Firstly, we suffered from an unplanned shutdown of our MDI site in Caojing, China. Secondly, we were affected by the force majeure declaration of our supplier for a key precursor in polyols, which significantly limited our product availability in Europe. Both incidents reduced our growth rate by about 3 to 4 percentage points during Q3.

As both plants are now back on stream, we do not expect any spillover effects into Q4. However, as we remain sold-out for these products, we will be unable to catch up during Q4. Thirdly, we noticed a summer weakness in Europe, especially pronounced in automotive and construction. This reduced our core volume growth by an additional 1 percentage point during Q3.

Although it is part of a regular seasonality in our businesses, it was stronger than expected. In addition, this year compared against 2 past years without the typical summer dip. In Europe and Latin America, volumes declined for the given reasons driven by our automotive, construction and wooden furniture businesses. Volumes in North America slightly progressed based on a positive growth in automotive and electronics. Asia-Pacific and especially China remained the region with the highest growth rates, despite the constrained availability on MDI. We achieved high single digit growth rates in automotive and transport as well as double-digit growth rates in many other smaller customer industries like sports and leisure, medical, engineering and packaging.

Globally, we once again achieved a solid growth rate of above 2% in automotive. Therefore, we continue to outgrow global OEM production by around 4 percentage points.

I will now hand over to Thomas.

Thomas Toepfer ***Covestro AG - CFO & Member of Management Board***

Well, thank you, Markus, and also very warm welcome from my side to everybody who is on the call. I'm on Page 4 of the presentation that hopefully you have in front of you, and you see here our sales bridge for Q3.

So our third quarter sales posted a solid growth of 4.8%, driven by prices and also volumes. As you can see, the higher volumes had a positive sales effect of 3% and that is the EUR 107 million in the chart and all the segments contributed to that positive development. And secondly, the higher selling prices had a similar positive sales effect of also 3.1% and that was driven by our Polycarbonate segment.

As expected and as you can see also in the bridge, the FX had almost no effect in Q3, reducing sales only marginally by less than 1%. And for the first time, we have a portfolio measure in that bridge, because we have divested our U.S. polycarbonates sheets business, which reduced our sales by 0.7%.

Now if you turn the page to number 5, you have our EBITDA bridge for Q3, and we achieved the guided EBITDA of around last year's level, despite the previously mentioned headwinds in terms of our production. So if you look at the volume effect despite only 0.2% core volume growth in terms of kilotons, we managed to achieve a euro nominated volume increase of 3% that I mentioned on the previous page, driven by a higher share of higher value-added product and this allowed for a very high volume leverage of [63%] (corrected by company after the call) and that then comes down to the EUR 67 million that you see here in the bridge.

Then for the first time since Q2 2016, we faced a negative pricing delta, entirely driven by polyurethanes. While I would clearly say that polycarbonates continued to generate a positive pricing delta in Q3. If you look at the other items in the EBITDA bridge, we benefited from a book gain from the disposal of the U.S. polycarbonates business that I already mentioned and the order of magnitude of that is EUR 36 million. On the other hand, we faced higher maintenance and logistics costs and additionally specifically in this quarter, we saw some outage-related expenses due to the previously mentioned unplanned production shutdowns.

So if you go to Page 6, and if you look at the lower part of the page, you see that the group EBITDA margin declined from 24.4% in Q3 2017 to 23.2% in Q3 of this year. And if you exclude the TDI fly-up margin and also the positive one-time item that I just mentioned, our margin would have been at around 19%, which we believe is a better reflection of the underlying performance and that then represents a slight decline of 2 percentage points versus the previous year period, if you look at it from a like-for-like perspective.

So with that, I would like to turn it back to Markus.

Markus Steilemann ***Covestro AG - CEO & Member of Management Board***

Thanks, Thomas. And we are continuing on Page #7. Looking at our Polyurethanes segment. In Q3, global demand was strong for the polyurethanes industry. Based on our insights, we expect a PU industry growth of 4% to 5% in 2018. MDI remains globally a high-growth area with an expected full year growth of above 5%. We did not notice any structural changes in global demand drivers.

As explained, we faced limited product availability for MDI in Asia and for polyols in Europe and Latin America due to unplanned shutdowns. These were the main drivers for the decrease of core volumes this quarter. The MDI industry currently faces some short-term volatility due to the recent startups of 2 new plants. Generally, global demand growth requires 1 additional world-scale plant per year. This year, 2 new plants came on stream, increasing supply pressure. Next year, we expect significantly less capacity additions. Hence, our overall view is unchanged that the MDI industry will remain balanced in the mid and long-term.

For TDI, we again realized the contribution from fly-up margins of around EUR 130 million in Q3 due to the continuous tight industry last quarter. With that, the total TDI fly-up added up to around EUR 0.5 billion already in the first 9 months of 2018.

With the new capacities finally being on stream, we observed the industry rebalancing, as expected. TDI prices are currently normalizing quickly, thus we assume no fly-up contributions during Q4. Finally, the margin polyether polyols remains resilient, but slightly below the long-term average as higher raw material prices were not fully compensated by price increases.

Let's move towards Page #8. In polycarbonates, we delivered a solid core volume growth of 2.6% in Q3. The ongoing product mix improvement and the deemphasis of low-margin businesses are well reflected in the Q3 figures. We continue to outgrow significantly the global auto market. In Q3, we achieved a mid-single digit core volume increase compared to a 2% decreasing global auto production. In the first 9 months, our high single digit growth compares to a flat global auto production. Electronics also contributed nicely with an above-average growth. As we continue to focus on less volatile and high margin business, we accept a double-digit decrease in volumes in the construction businesses.

The EBITDA margin progressed from 22.6% in Q3 2017 to 30.3% in Q3 2018. Excluding the one time benefit of EUR 36 million from the disposal of the sheets businesses, the EBITDA margin reached around 27%. The margin increase was mainly driven by a strong pricing delta, supported by a positive volume leverage and the ongoing product mix improvement. In Q3, higher raw material prices could again be more than compensated by increased selling prices. Nevertheless, prices came under pressure during the quarter on more commoditized grades in Asia-Pacific due to the ramp-up of new capacities in China.

Despite some fading short-term tailwinds, the industry outlook for polycarbonates remains attractive. We consider the industry supply and demand to remain balanced mid-term.

Moving on to Page #9. In Q3, CAS achieved the second quarter of high core volume growth with a year-on-year increase of 7.2%. We recorded a stable EBITDA compared to last year, which was above our expectations. A strong volume leverage was counterbalanced by higher costs, as expected. For the last quarter of the year, we expect a negative earnings impact from higher raw material prices, especially driven by significantly higher prices for HMDI. Still, due to the assumed good growth, we likely expect a year-on-year improvement of the EBITDA in Q4. We therefore, target to achieve a full year EBITDA close to last year's level.

Now let's move on to Page #10. Let me take the opportunity today to provide more details on 2 long-term initiatives we kicked off during Q3. Firstly, our investments for securing long-term growth opportunities. On October 9, we announced the long-term MDI CapEx program until the mid of the next decade. In case you have not seen the detailed investor presentation on this subject, it is posted on our IR website. For now, I describe the highlights. Besides the already public capacity extensions in Caojing, Brunsbüttel and Tarragona, we have announced our plan to build a new highly efficient, world-scale MDI plant on our existing site in Baytown, U.S.A., as well as a new aniline plant in Antwerp, Belgium.

Focusing on the new MDI plant, the total amount of EUR 1.5 billion includes investments into the complete chemical backbone. This will extend our leadership position in a number of areas. By 2024, it will boost our nameplate capacity in the U.S. from 330,000 tons to 740,000 tons per annum, after closing a less efficient MDI unit of 90,000 tons. With that, we will become the #1 player in terms of capacity in the region and the #2 player globally. Equally important, we will be able to extend our long-term competitiveness by further improving our cash cost position. Overall, the long-term MDI CapEx program will allow us to satisfy increasing demand and accompany growth in a highly attractive industry.

On Page #11, you will see that we plan to significantly increase our capital expenditure over the next years. Despite these major new projects, however, we are sticking to our previously indicated upper end of annual CapEx of EUR 1.2 billion. In MDI, we now have a comprehensive program that allows us to grow long term in line with the industry. The expansion of our 200,000 tons MDI plant in Brunsbüttel is slightly delayed. This said, we expect to ramp-up the plant in the second half of 2019. With the startup of Brunsbüttel, we will become short of in-house aniline supply. In order to achieve once again the best possible cash cost position, we decided to build a new aniline plant in Antwerp. The construction of the new chlorine plant in Tarragona is on track for a startup in 2020. This will also significantly enhance our cash cost position. In addition, we are now starting the engineering work for our new U.S. MDI plant.

Construction is expected to start in 2022. We are convinced that the MDI industry remains highly attractive in the long term, given solid structural demand growth and distinct entry requirements, such as access to technology. As a consequence, we expect to generate a decent return on capital employed on our CapEx, well above our cost of capital. This assessment is based on conservative assumptions, such as a payback time of less than 10 years, while our plants can operate for around 50 years. The long lifetime of our assets is well demonstrated by 90,000 tons line in the U.S., which started up in 1974 and is going to be closed in 2024.

Back to Thomas.

Thomas Toepfer ***Covestro AG - CFO & Member of Management Board***

Let's turn to Page 12 and look into the second long-term initiative of the group and let's have a more detailed look at our continuous efficiency programs. So the background to this is that in 2015, we launched our first profitability enhancement program, which we called PEP. And with that, we achieved total savings of close to EUR 250 million by the end of 2017, and we forecast another EUR 110 million in the next 2 years to come from this program. The PEP program, initially running until the end of 2019, is now being replaced and complemented if you like by the new efficiency and effectiveness program, which we call Perspective.

And with a set of new projects designed all along the value chain, we plan to implement all measures and projects by the end of 2020 and achieve all savings of around EUR 240 million until the end of 2021. So as a part of these projects, we also plan to reduce our personnel by around 900 full-time equivalents, and I would also like to mention that we have already achieved an agreement with the Works Council on exactly this reduction.

So for Perspective, we calculate with a total one-time cash outflow of around EUR 150 million and the indicated timing of the cash effects that you see in the chart might deviate from their respective P&L effects. So that means that we may need to book some provisions for major cost items in Q4 2018, and obviously, such provisions are not included in our current EBITDA guidance for Q4 and also for the full year.

If you turn the Page to number 13, you can see that the program has actually has 2 goals. Firstly, it's about the way of working in cross divisional processes, which should be further developed, for example, through the growing potential of digitalization. And secondly, it's about the competitive cost position that will be sustainably improved and secured. So the savings are driven by 3 quarters, by efficiency gains and by 1 quarter by personnel and that essentially means personnel cost reductions. And as you can also see on the page is that the program is designed around 4 main work streams, and we expect the highest share of savings in the area of supply chain and manufacturing then followed by procurement, SG&A and then also sales and marketing.

So let's now have a look at the overall benefit of the program on our EBITDA development over time and that is depicted on Page #14. So as you can see, our long-term investment strategy also triggers additional CapEx-related operational costs. And these are mainly driven by more engineering hires and other production related costs. In addition, the regular labor cost inflation also has to be counterbalanced. So if you bring this together with Perspective, overall, we expect that with the help of Perspective, we will be able to limit the additional cost increases to around EUR 150 million next year. And for 2020 and 2021, we aim to limit the additional cost increases further, and we're only willing to allow around EUR 50 million higher costs annually.

So with that, let us look on Page 15 on our free operating cash flow. So as you can see, the first 9 months of 2018, we were able to generate a record free operating cash flow of EUR 1.3 billion, even surpassing the very high level of last year's period by around 10%. And a strong free operating cash flow improvement was driven by a significant EBITDA increase of 14% and a lower working capital buildup, and components that partially offset the improvement were significantly higher CapEx of EUR 429 million as we can see in the bar and tax payments of EUR 505 million.

In terms of working capital, our working capital to sales ratio reached 18.4%, which is a similar level as in the first 9 months of the last year. However, for the full year of 2018, we target to be back in the range of 15% to 17%, which we have indicated to you previously. I would also like to mention that the relatively low cash tax rate for the first 9 months is the result of tax payment phasing. So I would clearly say that for the full year of 2018, we expect tax payments to be around 2 to 3 percentage points below our P&L tax rate, which we have guided to be between 25% and 27%.

Let's go to Page 16, and you have the key items of our balance sheet. So as of September 30, our total net debt level decreased again compared to the level of around EUR 2 billion, which we had at the end of June of this year. However, the ratio of total net debt to EBITDA remains essentially unchanged at 0.4x. And as you can also see, the high free operating cash flow of EUR 1.3 billion more than compensated the cash outflow of above EUR 1 billion for the share buyback program, if you take it as a whole, because between October last year and the end of September this year, we now bought back around 14 million shares, equaling 7% of our capital stock. And the overall program runs until we have achieved either EUR 1.5 billion or the equivalent of 10% of our capital stock. And as we said last time already, we plan to complete the share buyback latest by the mid of 2019.

So if you look at the bridge from December 31 to September 30, you see that together with the dividends, which were paid out in Q2, we now return more than EUR 1.4 billion cash to our shareholders within the first 9 months of the year. You can also see that the pension provisions increased by EUR 77 million, mainly due to negative returns of our plan assets, and our equity ratio continued to improve and now reached 51% at the end of Q3.

So let's go to Page 17 and talk about the KPIs and our guidance. So what I would like to say is we confirm the targets for all our key KPIs. We aim for low- to mid-single-digit percentage increase of our core volumes, as you can see in the first line item. However, as we have achieved 1.5% core volume growth in the first 9 months of the year, it is now more likely that we will end up with a low digit percentage increase for the full year. However, we assume a solid growth in Q4 driven by the structural demand growth and improving internal availability. If you look at the second line item for the free operating cash flow, we confirm our target of above EUR 2 billion, but we recognize that there is a higher risk of achievement, which is related to the current oil price developments. Therefore, we expect a certain upward pressure on our working capital and in addition, we expect some higher inventories through shifts triggered by the unplanned outages, which we had in Q3. And in terms of CapEx, we are now expecting to finish the year at the upper-end of the previously given range of EUR 650 million to EUR 700 million.

If you look at return on capital employed, third item, we are fully on track of achieving our ROCE target of around previous year's high level of 33.4%, which is obviously well above our weighted average cost of capital of around 7%.

Look at the line item referring to EBITDA. Remember with half-year reporting, we increased our full year EBITDA target from around last year's level to above last year's level, and we also confirm this guidance. However, we note increasingly challenging economic conditions.

Now if you look at Q4, usually, we'd like to provide you with the main EBITDA year-on-year bridge items for the upcoming Q4 quarter. So given the current trend of decreasing prices for TDI, MDI and also polycarbonate, we assume a negative pricing delta of more than EUR 300 million for the quarter. On the other hand, the expected solid volume growth should allow for an EBITDA benefit in the high double-digit millions. And in terms of the other items, please remember that we have booked a provision relief for our Tarragona plant of EUR 63 million in the fourth quarter of last year, which obviously will not repeat itself. And this is why we expect a high double-digit million burden in the other items bucket for Q4. And last but not least, the FX effect is expected to be neutral. So just one last point in terms of current news, as you might have noticed, we might face a specific risk for our German production sites due to the historic low levels of the Rhine River. The messages at this point in time, we expect no material negative financial impact, but of course, every day that passes along without relief makes our guidance more challenging. So far, we're confident with respect to the specific Rhine issue.

And with that, I would like to turn it back to Markus.

Markus Steilemann ***Covestro AG - CEO & Member of Management Board***

Thank you, Thomas. We are now on Page #18. Let me close our presentation with a wrap up. During Q3, we achieved stable core volumes despite several headwinds. Earnings per share increased by 7% in Q3 and by 25% in the first 9 months, supported by our share buyback program. Despite an increasingly challenging environment, we confirm our guidance for the full year 2018. We operate in highly attractive industries that allow us to generate a significant premium above cost of capital over the cycle. We continuously work on our future growth as well as on our cost base. We believe that investments into organic growth will yield attractive returns, given our leading global cost positions.

We do our utmost to defend this position. We initiated a new efficiency program perspective in a year of record results. This underscores our motivation to continuously work on costs regardless of the stage of the cycle.

Thanks for listening, and we are now open for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question comes from Mr. Thomas Swoboda from Societe Generale.

Thomas Swoboda ***Societe Generale Cross Asset Research - Research Analyst***

I have 2 questions. I think we have all being waiting for TDI to be really in trouble. Now it looks like MDI is under pressure stronger than TDI. I'm just wondering, if you could give us a little bit more insight why do you think TDI is holding up better versus MDI. And the second question on your expansion project in MDI, I'm sure you have done it but still the question, would you need the MDI greenfield expansion in case we should see a global recession in the next 2 to 3 years? So would you still need the capacity by 2024 as you plan?

Markus Steilemann ***Covestro AG - CEO & Member of Management Board***

Thanks for your question. This is Markus. So as we have lined out, we have already seen in the first 9 months an effect of roughly, let's say, EUR 0.5 billion in terms of TDI fly-up. And given that fact, as we said previously, we do not expect any further, let's say, effects coming from the TDI and there's numerous, let's say, reasoning for that. One of the reason could also be that despite the fact that now all capacities are on stream, that obviously the market is in demand for TDI and needs the TDI that is currently being produced from the assets that are up and running in the way how they're up and running.

On MDI, we must not forget that we are entering into a kind of low season, and that we have seen 2 major capacity additions, which do not change the long-term picture and the mid, let's say, term picture how we look at the MDI development. MDI is still in high demand. MDI is still the key material for many applications and cannot be replaced in those applications. So despite the fact that we had a long term historical growth of 6% to 7% in MDI, we only plan the, let's say, MDI long-term growth with around 5% and that also leads me now to answering the second question that you have raised in this context. We have made rather conservative assumptions about the capacity additions in MDI as well as on, let's say, historically speaking, demand development in MDI. And that's why we believe that mid to long-term, this respective MDI investment is absolutely necessary to fuel the market. Still considering that any announcement that has been made publicly is coming in full on time. And as we know, and we have pointed out this previously numerous times, the respective MDI investments in many cases come either delayed or when they come on time, they're not coming in full. So putting all this into context, we still believe that we have based the investment case on very conservative assumptions and the 6% to 7% historical growth by the way, have also included recession periods in the last 20 years.

Operator

The next question comes from Christian Faitz who's calling from Kepler Cheuvreux.

Christian Faitz ***Kepler Cheuvreux, Research Division - Equity Analyst***

I typically [like the sentence] but given the condition financial markets are in, congrats on the results. First question, can you give us an indication of how your price/mix in your MDI creates move in Q3? And then second question, can you please share your thoughts on key demand trends at this point in time for polyurethanes as well as polycarbonate products in terms of global customer demand trends?

Markus Steilemann ***Covestro AG - CEO & Member of Management Board***

To be honest on your first question on monomeric MDI and polymeric MDI, we would prefer not to give a specific answer here. That leads me immediately to your second question. If you look at the overall demand trends and I'm seeing customers normally on at least almost weekly basis, and if I'm traveling around the world and see where customers are, there's one fundamental trend that I specifically see for the customers in our industries. What they're doing, they have, for sure, high uncertainty and there's also a lot of psychological momentum going on, yet what we also see that they're starting to getting their feet on the ground to adjust to the changed global supply situation and the new, let's say, let's call it, world order in terms of tariffs, in terms of Brexit, in terms of Turkey, in terms of Iran. So what they're doing is, they're just adjusting their respective supply chains. And this transition and this adjustment leads to not only short-term, let's say, insecurity, but in particular it also leads to the fact that we have seen some dips here and there in demand. But overall, we just have to say and also our strong October indicates that also in terms of our order books that they're just adjusting. To give you an example, Chinese appliance manufacturers, they have a very clear strategy to globalize their business and also internationalize their production. And now, they're just speeding up this process because the overall economic situation and geopolitical situation forces them to be quicker. On the other hand, visiting Mexican customers, for example, in this industry but also in the automotive industry, clearly indicate that they are now benefiting from some of the imposed tariffs that they're seeing, for example, from Asia Pacific, from the U.S., and we also see now some of the Chinese customers moving, for example, into markets like Mexico, to making sure that they still can continue to supply the U.S. market. So what we see is less overall of a end consumer driven demand dip more than a structural change and also high uncertainty level in the industries that we are serving. And that's why also, as I've said, indicating what we're seeing in our order books does not really point towards a global recession rather towards general adjustment that is going on.

Operator

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

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

Moving to your new cost reduction program, can I just ask for a couple of points of clarification, please? Firstly, the net increase in fixed cost that you anticipate for this year of approximately EUR 250 million, how much of that has already occurred in the first 9 months of the year? And then within that the same topic, can I just make sure that I understand this correctly that the EUR 150 million net cost increase that you anticipate for next year, is that the total amount by which you expect fixed costs to inflate, or is that an additional amount over and above underlying fixed cost inflation? And then final question, the EUR 300 million or so price decline that you -- I think you said for Q4 that you anticipate, is that a net price raw material effect or just a former? And if just a former, could you please give us any indication of what you'll anticipate the raw material effect to be?

Thomas Toepfer ***Covestro AG - CFO & Member of Management Board***

Yes. So let me start with the last question. So if we talk about the bridging items for Q4, and we say we're expecting more than EUR 300 million negative effect, this comes from pricing and raw materials so it's the net effect that we're talking about. It corresponds to the EUR 27 million that you have seen in the bridge for Q3.

Then in terms of the cost, as you've seen, we've indicated for EUR 250 million cost increase for 2018. This is a relatively evenly distributed number so you should not expect any specific spike in the fourth quarter to come. And then for 2019, we're expecting an additional EUR 150 million of fixed costs in terms of energy, wage increases, wage inflation, et cetera, et cetera, which will come on top to the EUR 250 million roughly that we were indicating for this year.

Operator

The next question comes from Mr. Sebastian Bray calling from Berenberg.

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

I would have 2, please. The first is on definition. What is the difference between core volume growth and total reported volume growth in the Polyurethanes segment, please? I think the volumes were stable as a whole, but there were 2% decline in core. What explains the difference? The second is a question about a statement that was made earlier on the growth trajectory of MDI. Am I right in saying that the percentage figure of, let's say, about 6%, 7% historical demand growth is purely an average and the demand did actually contract in 2008, 2009? The data around that, which is publicly available, is sometimes a bit sketchy.

Markus Steilemann ***Covestro AG - CEO & Member of Management Board***

If we are looking into the definition of core volumes, we intend to produce product like TDI, MDI and polycarbonates. But given, let's say, the chemical nature of our production, we also have quite a large amount of products, which we not, let's say, as a primary purpose producing, for example, caustic soda; for example, hydrochloric acid and also styrene. And we have to also sell those products in the respective markets and with that also generating quite -- let's say, generating also external sales. So if you're looking at the polyurethane business, it is very clear that we have here definitely sold some of those side products, which then contribute also to their respective volume growth. But if you just look at the core product MDI, TDI as well as polyether polyols, we just exactly have the negative core volume growth in Q3 that we have lined out. Now talking about your second question, 2008 as part of the, let's say, general economic meltdown that we have experienced in those 2 years 2008 and 2009, yes, we have seen a minus 2% volume dip. That is what we have seen in 2008. Yet to be also very clear, that was historically, absolutely exceptional year, which we have not seen in that order of magnitude before. And still despite this claim, this very one year, we still have seen an historical average growth of 6% to 7%. And that's why I think, the planning ahead with 5% is pretty solid and pretty conservative.

Operator

The next question is from Mr. Geoff Haire who's calling from UBS.

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

I was just wondering if you could comment a little bit about what we should think for pricing delta as we move into the first and second quarter of next year, and how you see that progressing. And then secondly, I was just wondering if you could comment about your visibility on volumes and market cycle also, whether it's a very long supply chain. At least that's the perception we have and just how confident you are in the comments you've made about structural change.

Thomas Toepfer ***Covestro AG - CFO & Member of Management Board***

Geoff, it's Thomas speaking. I think in terms of the visibility for 2019, I think it will be too early at this point. So we're in the middle as many companies of our annual planning phase, et cetera, et cetera. So therefore, I think it will be premature to come up with any specific guidance. And of course, we will come up with a full year guidance in our annual press conference next year. In terms of the visibility that we have, I would say it's about 8 to 12 weeks in terms of visibility on our key market and customer groups. That being said, October is promising. We see good volume growth and that makes us confident that the volume uplift, which we have indicated for Q4, is on a good track and we feel some good momentum here.

Operator

The next question comes from Mr. Markus Mayer who's calling from Baader Bank.

Markus Mayer ***Baader-Helvea Equity Research - Lead Analyst of Chemicals***

Two remaining questions. One is on this outage related expenses in the third quarter. Could you quantify this? Maybe that would help. And secondly, on this point that potential problem with the low Rhine water levels, maybe you can also shed some light what could happen and if you already experienced higher logistic cost due to this low Rhine water levels.

Thomas Toepfer ***Covestro AG - CFO & Member of Management Board***

It's Thomas speaking. I mean, quantifying the 2 outages, I think what we can say is that it cost us in terms of volume growth approximately 3 to 4 percentage points. And that really also explains why in terms of our core volumes we were only seeing a growth of 0.2%. So I think that gives you the order of magnitude that these 2 effects had. With respect to the Rhine water level, I mean, currently we would say it has caused a low one digit million additional cost in Q3 and that's mainly supply chain costs because the fact is we're keeping our production up and running. But we can only load the barges with 20% of the load, so the logistics cost are quite negatively affected by this. But as I've said in terms of the product availability, we still have our plants up and running in our German sites.

Operator

The next question comes from Paul Walsh from Morgan Stanley.

Paul Walsh ***Morgan Stanley, Research Division - MD***

Just 2 questions from me. I wondered on the EUR 300 million that you're talking about for the fourth quarter, if you could give us a notional split between the polyurethanes and polycarbonates. My sense is, it's mostly polyurethanes, but maybe you could steer me better on that. And the second question I had, as a sold out on a number of these products, you're still talking, Markus, very positively about volumes. And yet maybe I'm looking at the wrong data, I've seen TDI, MDI, certainly polymeric MDI and polycarbonate spreads collapsing in spot markets back to levels that we saw in 2016 and '17. So what I'm really asking is what am I missing in terms of what's changed apart from a bit of capacity coming on stream. It seems like the spread reset is a little bit stronger than perhaps the strength in the markets that you're communicating from a demand side. I'm trying to reconcile those 2 things.

Thomas Toepfer ***Covestro AG - CFO & Member of Management Board***

Let me take the first question with the pricing delta. So I think it's a fair question. If we talk about more than EUR 300 million negative pricing delta, I would say you will find negative pricing delta for both, our polyurethane and also the polycarbonate business. However, polyurethane is anything between 80% to 90% of the total, just to give you the order of magnitude. So the polycarbonates, it's much less pronounced.

Markus Steilemann ***Covestro AG - CEO & Member of Management Board***

It's Markus speaking. As you direly addressed this also to me, if you look at the overall situation, we think that the entire situation currently is much more supply driven than demand driven. Yes, we're entering into, let's say, the fourth quarter, which is traditionally weaker quarter of all 4 quarters in the year. Yet, currently, all MDI plants are running flat out. We have no outage or planned shutdowns currently. So having said that, that explains a little bit in which direction currently short term the market is heading. It does not change, let's say, that we have seen those 2 major capacity additions coming on stream. But yet on the other hand, we still see MDI being overall in strong demand. And we also have to consider, let's say, in terms of pricing. What you see in pricing charts is normally spot markets and only a particular group of MDI grades, which does not reflect the entire product that we're having in MDI grades. So from that perspective, the picture that you have based on, let's say, this very much reduced data might look different from what we are seeing currently in the business.

Paul Walsh ***Morgan Stanley, Research Division - MD***

Okay. Okay. And just one follow-on, please, on polycarbonates. Given what you can see in those charts and maybe they're wrong because I know you guys have got kind of a broad spread of products in there, some of which are very specialty. But given the spread dynamics you're seeing right now, does polycarbonates get worse before it gets better? If you see what I mean, i.e. you're not feeling the full brunt of the recent price declines in spread reduction in Q4 and that gets deferred to Q1 or is it just the data we see is not relevant to your business because of the grades you have?

Markus Steilemann ***Covestro AG - CEO & Member of Management Board***

Yes. Well, if you look at the, let's call it for the time being, more specialized grades business, which roughly represents 60% of our business and counting. Here we normally have a contract of around 3 to 6 months, so that will maybe come later depending on how the demand side is developing. But as I said, we're still continue to outgrow in some of the key industries that we're talking about and what we see in in customer industries like automotive, it's still something that does not entirely reflect the business development for our materials because we continue to replace other materials. We continue also to shift our product mix towards higher and more resilient grades, and we're also seeing that the mix, let's say, in automobiles and vehicles that is sold is preferring materials like polycarbonate in the entire industry and less preferable for highly commoditized plastics like polyolefins, for example. So all in all, there will be a short-term effect, in particular on the commodity side before we will see a rebound.

Operator

The next question comes from Chetan Udeshi who's calling from JPMorgan.

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

Just a couple of questions from myself. Number one is when you say more than EUR 300 million of net pricing delta negative, of course, can you confirm or can you give us some sense of what you've assumed there? Have you assumed the current spot pricing? Or have you taken some sort of a haircut on top of the spot pricing? That's number one point. And number two question is when you talk about these fixed cost increases of EUR 250 million or EUR 150 million, it sounds quite a bit in terms of as a percentage of your total OpEx. So maybe can you help us understand what is driving such a big inflation in the business, given that you also have some savings from ongoing efficiency program that you've had even before the new one that you announced today? I know -- does it also include some of the pressures you might see from higher electricity energy prices in Europe?

Thomas Toepfer ***Covestro AG - CFO & Member of Management Board***

Yes. Chetan, it's Thomas. So on your first question, the negative EUR 300 million, essentially we're not assuming to freeze the current prices and assume them for the rest of Q4. But essentially, what is baked in into that number is the assumption that there will be a further slight decline in prices relative to our current level until the end of the quarter. So I think there is -- that is baked in that sense. So we're not assuming that prices will stay at the current levels, but slightly continue to decline. And then I think the key reason for the cost inflation that we're seeing here is it's a precursor in terms of cost because of our investment program, because we are significantly ramping up our troops that do the planning and then the installation and also the vendor management for our large investment project. That is the main item that we have to compensate here. Part of it of course is some energy, which we have assumed and part of it is the normal labor cost inflation, because we have about EUR 2 billion of labor cost that gets inflated every year. And that relatively quickly leads you to this number and this is why we've said, we need the Perspective program to counterbalance that with cost cuts, especially in the administrative and central functions. And you see the effect then in 2020 and '21 where we allow for almost no cost increase, despite the massive investments that we're making in those 2 years.

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

Understood. So just to be clear, you are assuming some further moderation in your pricing versus what you see right now?

Thomas Toepfer ***Covestro AG - CFO & Member of Management Board***

The answer is yes. The answer is yes.

Operator

The next question comes from Laurence Alexander from Jefferies LLC.

Laurence Alexander ***Jefferies LLC, Research Division - VP & Equity Research Analyst***

Can you speak a little bit about how the -- with the way the -- end market uncertainty and the way the spreads are playing out? How you think about the buyback programs and in particular, how you think about the calculation around doing a reload once you've completed the current buyback.

Thomas Toepfer ***Covestro AG - CFO & Member of Management Board***

Well, I mean, the buyback is running. You know that the third tranche we started in August 13, and we said it would have a maximum volume of EUR 650 million and should be latest executed by February 8. So theoretically, the program could be finished by that point, but there's also a certain possibility that we will only finish by the mid of next year. And in terms of the reloads, so to speak, I mean, I think it would be premature to say what is exactly on the agenda for the next AGM. But I think nobody should be surprised if in the next AGM, we ask for a reload of a potential second buyback program.

Laurence Alexander ***Jefferies LLC, Research Division - VP & Equity Research Analyst***

Can you maybe just elaborate a little bit? I mean, just looking at, for example, the Q4, if you just annualize that as a run rate or take the winter months as run rate, even -- the shares are pretty close to discounting that as your sustainable level. How do you think about the size or how much scope you have or are there constraints in the size of a buyback that you can do, given your balance sheet strength?

Thomas Toepfer ***Covestro AG - CFO & Member of Management Board***

Well, I mean, again, I think the current program, I think there's no doubt that we will finish it just as planned maybe even a little faster. I think now linking potential plans for buyback program that comes back to the guidance questions. I think we're in the middle of the process of bringing all these things together, and I think it would be too early to say what the exact plans are for buyback, in light that we have not come out with a precise guidance for next year. So I beg for your understanding that we will come up with some more detailed data and comments then in our press conference next year.

Operator

The next question comes from Ms. Georgina Iwamoto from Goldman Sachs.

Georgina Iwamoto ***Goldman Sachs Group Inc., Research Division - Associate***

I've just got one question, if that's okay. You were mentioning that you made some very conservative assumptions on the market outlook before taking the decision to announce your MDI facility in the U.S. I was just wondering if you could confirm whether your supply outlook included the full EUR 1.5 million additional capacity from Wanhua in your supply forecast. And if not, can you indicate what level you anticipate from the company?

Markus Steilemann ***Covestro AG - CEO & Member of Management Board***

Short answer would be yes to your second part of the question.

Georgina Iwamoto ***Goldman Sachs Group Inc., Research Division - Associate***

Okay. So includes the full EUR 1.5 million?

Markus Steilemann ***Covestro AG - CEO & Member of Management Board***

As I've said earlier, Georgina, we have included all announced investments as they were announced. That means that they come on stream in full at their respective announced dates. And we have not taken into consideration, let's say, further insight that may indicate a delay in startup or even if the plant would come up on time but not in full. That is also one part of the some -- why we said we took a more conservative approach by having, from a historical perspective, a lower than witnessed demand growth rate; yet on the other hand, we took the maximum. That means fastest addition of supply into consideration before we're doing the math.

Operator

We have a follow-up question from Neil Tyler.

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

I wanted to ask you whether you're able to share any information you have on the ongoing DOJ investigation that was launched in July around polyurethane pricing. Is there anything you can tell us with regards to that investigation whether you know what's being looked into, and over what time frame when we might find out whether there's a conclusion to that?

Thomas Toepfer ***Covestro AG - CFO & Member of Management Board***

Well, I mean, what I can tell you is, I can confirm that we have been contacted by the U.S. Department of Justice regarding an investigation with the polyurethane industry, and I can also tell you that we are fully cooperating with the authorities throughout the investigation. But what is also clear is that we strongly deny all allegations that have been made and that we are clearly defending ourselves. You know that there is also 12 civil lawsuits that have been filed in addition to that. We think they are completely unbased and as I said, we will vigorously defend ourselves in these lawsuits.

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

Okay. So when you refer to allegations, are you referring to the lawsuits or has the DOJ made an allegation or are they just carrying out an investigation?

Thomas Toepfer ***Covestro AG - CFO & Member of Management Board***

Well, I mean, they're carrying out an investigation with respect to antitrust behavior in the polyurethane industry and that is at the core of the allegations that the DOJ has made. And as I said, we think there's not a basis for any of the points that they are claiming.

Operator

And the final question for today comes from Mr. Thomas Wrigglesworth who's calling from Citi.

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

To focus on CAS, very strong volume growth. Could you remind me what's driving that? And then could you define how much the impacts has been because of the HMDI outage and when you expect that to reduce? And then thirdly, the volume growth guidance that you gave out for 2022 of EUR 200 million to EUR 300 million impact to years. We're thinking of that bridge. I assume you're sticking to that guidance. And how do we think about -- obviously, there's a top line impact but was that set a base price level that we can think about or is that based both in terms of the sensitivity and the absolute amount of that guidance?

Markus Steilemann ***Covestro AG - CEO & Member of Management Board***

Yes. Thomas, this is Markus speaking. To your first question on coatings, adhesives and specialties, we have had -- last year, if you recall, we were still in the aftermath of a price increase and that's why we had a low basis from which we were starting. That's number one. We also currently assume based on what we understand from the market that we gained market share in the respective segment, and that is the 2 major explanations for the volume growth that we have seen Q3 this year compared to Q3 last year. On HMDA, one of the largest suppliers actually, which is Solvay plants, large turnaround next year. So we assume that the limitations should be around for a while, maybe for the next, let's say, 6 to 9 months and that's the current situation. And if you could help us, let's say, on the third question. Can you just raise the third question again?

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

Yes. Sorry. It's all been clear. So you said EUR 200 million to EUR 300 million volume impact and you've kind of -- at your Capital Markets Day, you said that would -- you've implied that's the number in there for 2019. But to get to that volume number, I assume you've had to assume a price level. And what price level did you assume to get to the EUR 200 million to EUR 300 million guidance on volumes? Does that now change because prices are getting a bit softer? That number's going to be EUR 150 million.

Thomas Toepfer ***Covestro AG - CFO & Member of Management Board***

Exactly. I mean, what we've given you is a range of EUR 200 million to EUR 300 million; EBITDA uplift through the volume effect. We were assuming 2 things, one is a 4% CAGR in terms of the volume uplift. And we were assuming a more or less normal price level, and I would say the current prices that we're enjoying still would fully qualify to be within that range. So at current price levels, we would still be within the EUR 200 million to EUR 300 million uplift.

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 all for your contributions, for your questions. If you have more questions, don't hesitate to call the IR Department, and we also might help you there then. And see you then next conference call or during the next months. Bye-bye.

Operator

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

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