Dow Chemical (DOW) Earnings Report: Q3 2015 Conference Call Transcript

The following Dow Chemical conference call took place on October 22, 2015, 09:00 AM ET. This is a transcript of that earnings call:

Company Participants

- Jack Broodo; Dow Chemical Company; VP of IR
- Howard Ungerleider; Dow Chemical Company; EVP & CFO
- Andrew Liveris; Dow Chemical Company; Chairman & CEO

Other Participants

- P.J. Juvekar; Citigroup; Analyst
- Steve Byrne; BofA Merrill Lynch; Analyst
- Frank Mitsch; Wells Fargo Securities LLC; Analyst
- Jeff Zekauskas; JPMorgan; Analyst
- Peter Butler; Glen Hill Investment Research; Analyst
- David Begleiter; Deutsche Bank; Analyst
- Don Carson; Susquehanna Financial Group / SIG; Analyst
- Hassan Ahmed; Alembic Global Advisors; Analyst
- John Roberts; UBS; Analyst
- Jonas Oxgaard; Sanford C. Bernstein & Co.; Analyst
- Vincent Andrews; Morgan Stanley; Analyst
- Bob Koort; Goldman Sachs; Analyst
- Jim Sheehan; SunTrust Robinson Humphrey; Analyst
- Aleksey Yefremov; Nomura Securities Co. Ltd.; Analyst

MANAGEMENT DISCUSSION SECTION

Operator:

Welcome to the Dow Chemical Company's third-quarter 2015 earnings results conference call.

(Operator Instructions)

Also, today's call is being recorded.

I'd now like to turn the call over to Mr. Jack Broodo. Please go ahead, sir.

Jack Broodo (VP of IR):

Good morning, and welcome. I'm Jack Broodo, Vice President of Investor Relations.

As usual, we are making this call available to investors and the media via webcast. This call is the property of the Dow Chemical Company. Any redistribution, retransmission or rebroadcast of this call in any form without Dow's express written consent is strictly prohibited.

On the call with me today are Andrew Liveris, Dow's Chairman and Chief Executive Officer, and Howard Ungerleider, Vice Chairman and Chief Financial Officer (sic). Around 7:00 AM this morning, October 22,
our earnings release went out on Business Wire and was posted on the Internet on Dow.com. We have prepared slides to supplement our comments in this conference call. These slides are posted on our website and through the link to our webcast.

Some of our comments today include statements about expectations for the future. Those expectations involve risks and uncertainties. We cannot guarantee the accuracy of any forecasts or estimates, and we don't plan to update any forward-looking statements during the quarter. If you would like more information on the risks involved in forward-looking statements, please see our SEC filings.

In addition, some of our comments reference non-GAAP financial measures. A reconciliation to the most directly comparable GAAP financial measure and other associated disclosures are contained in our earnings release and on our website. Unless otherwise specified, all comparisons presented today will be on a year-over-year basis.

Sales comparisons exclude divestitures and acquisitions, EBITDA, EBITDA margins, return on capital and earnings comparison exclude certain items. The agenda for today's call is on slide 3. I will now turn the call over to Howard.

Howard Ungerleider (EVP & CFO):

Thanks Jack, and good morning everyone. Turning to slide 4, our results this quarter demonstrate once again the value of Dow's integrated structurally hedged portfolio, our focus on execution, and the strong financial position the Company has built. Operating EPS rose to $0.82, an increase of 14% year over year. Operating EBITDA rose to $2.4 billion versus the same quarter last year on continued demand growth, margin expansion, and self-help actions. Volume grew in nearly all geographic areas, reflecting stable underlying demand for Dow's innovative solutions. Operating EBITDA margins expanded in nearly all operating segments reaching 20%, up 370 basis points year over year, the highest quarterly results since 2005.

Our disciplined approach to price/volume management enabled us to deliver these rules even in the midst of ongoing and significant top-line headwinds, with year-over-year price declines in oil of 50% and currency headwinds of 17% for the euro and 51% for the Brazilian real. The consistent earnings growth, margin expansion and strong cash flow results we delivered in Q3 continue the steady drum beat over the last 12 quarters and underpin our ability to return increasing value to our owners, as illustrated on slide 5.

As we have covered in past quarters, we benchmark our quarterly results against our key financial goals that provide a clear view on our performance. Quarterly EPS has grown at a 21% CAGR over the last three years on an operating basis. I think it's important to note that the one-time gains resulting from portfolio actions has resulted in an additional $0.71 of as-reported EPS above the year-to-date operating EPS of $2.58.

ROC is now 11.9%, up more than 170 basis points versus the same quarter last year, and we expect ongoing improvement as our growth levers, particularly on the US Gulf Coast and in Saudi Arabia, continue to produce and as we complete our portfolio management actions. Cash from operations reached $2.5 billion in the quarter, up $700 million, or 41% versus the year-ago period, and has now reached $8 billion over the last 12 months.

And we continue to return this cash to shareholders. Year to date Dow has returned $1.9 billion to shareholders through declared dividends and share repurchases. Additionally, our recent completion of the Dow Chlorine Products divestment, which successfully closed on October 5, had a tax efficient value of $5 billion, or a taxable equivalent value in excess of $7.5 billion.
This is a significant value for a commodity business and created a win/win/win for Dow, for Olin, and for the shareholders of both companies. Overall as a result of this transaction, our net debt went down by $3 billion, and $1.5 billion in Olin common stock was distributed to Dow shareholders in exchange for 34.1 million shares of Dow stock. A slide is available in the appendix for additional details.

Let's please now turn to segment operating results on slide 8. In Ag Sciences operating EBITDA for the segment was down from the year ago period, reflecting declines in price, the sale of AgroFresh, and a gain of $44 million from the one-time sale of a joint venture. The business saw continued strong demand for new crop protection molecules with a 40% increase in new product sales versus the same quarter last year and an 8% increase year to date led by strong growth in spinetoram insecticide.

Results in the quarter also reflected significant improvement in year-over-year cost reduction actions. Overall the ag market continues to be challenged, with high inventory levels and currency pressures more than offsetting higher volume gains in Europe, Middle East, Africa, India, as well as North America.

We do expect ongoing weakness to continue over the next 12 to 24 months. While conditions in Brazil ag were weak in the quarter, Dow continues to gain share and in fact has now moved up to second place in corn seed market share. We also achieved a significant regulatory milestone with the approval of ENLIST cotton.

Moving to slide 9, Consumer Solutions reported record operating EBITDA despite a year-over-year decline in equity earnings. Dow automotive solutions achieved a quarterly operating EBITDA record, reflecting growth in both OEMs, as we see continued adoption of aluminum, high-strength steel and composites, as well as in our aftermarket segments. Our business continues to outpace industry growth, driven by Dow's innovative structural adhesive solutions, and there is significant upside potential as we continue to expand into adjacent applications.

Consumer care volume grew in pharma and personal care sectors, offset by sales declines in the lower margin home care and industrial markets, as well as by ongoing currency headwinds. We continue to see demand strength in the high-value portions of our cellulosics chain.

In Dow electronic materials, EBITDA growth in semiconductor and display was offset by declines in interconnect technologies. Display profitability was improved this quarter by self-help actions, including the intentional exit of low-margin business and our focus on upgrading the portfolio.

Turning now to Infrastructure Solutions on slide 10, overall operating EBITDA for the segment decreased, as growth within several businesses was offset by declines in equity earnings, reflecting a one-time tax credit Dow Corning received in the third quarter of 2014. Dow building and construction reported record quarterly operating EBITDA as well as volume growth in most regions, particularly in cellulosics and spray foam technologies. Our innovative product lines are driving growth that is outpacing that of global construction markets, and our proprietary flame retardant technology is capturing attractive licensing income.

Dow coating materials reported volume gains in most regions led by double-digit growth in [EMEAI]. The business has expanded its market participation with a robust innovation pipeline in new vinyl acrylic binders and rheology modifiers across a broad range of customers. On a global scale, performance monomers continue to remain in industry-wide trough-like conditions. Energy and water solutions reported double-digit volume growth in emerging market for reverse osmosis solutions, partially offsetting declines in energy sales in North America.

Turning to slide 11, Performance Materials and Chemicals reported a decline in EBITDA reflecting the impact of divestitures and lower MEG pricing. Strong volume in Asia, as well as in a majority of businesses, was more than offset by global pricing pressures and ongoing currency headwinds.
Industrial solutions reported earnings declines due to compressed glycol margins and weakness in North America oil and gas drilling demand. Polyurethanes once again continued to deliver strong volume growth, with share gains due to broader market participation, expanding system house sales, the startup of our Thailand polyols plant, as well as underlying fundamental demand growth in EMEAI and Asia Pacific.

On slide 12, Performance Plastics EBITDA achieved record levels due to robust demand in all businesses. Dow packaging and specialty plastics reported a record quarterly operating EBITDA as the business captured gains from demand growth in emerging markets, high operating rates, strong asset reliability and tight inventory across the chain.

Dow elastomers delivered a second consecutive quarterly operating EBITDA record due to demand in key markets such as transportation, high-end footwear and infrastructure. Dow electrical and telecommunications also reported volume growth in North America and EMEAI as new home sales and construction spending rates trended higher.

Turning to slide 13, we want to illustrate the importance over time of owning the full polyolefin value chain. As you can see, the source of income has shifted over time. It’s hard to predict which bucket the value will come from in any given period.

In the 2002 trough, for example, the ethylene to naphtha spread was high in very weak markets, with some contribution from the oil-to-gas spread. Our differentiation in 2002 was much lower than it is today. In the strong markets of 2005, there was virtually no oil-to-gas spread.

In 2009, Dow retained market share and decent trough margins due to product differentiation, while competitors that didn’t own the differentiation or feedstock flexibility struggled to the brink of insolvency. In 2014, the oil-to-gas spread was the main driver of margins, but full chain integration and differentiation played an important role. This differentiation for Dow is based on unique polymers, catalyst, process and comonomer combinations.

In 2015 the margin has been shifting to both the polymer and to differentiation as supply/demand tightness, especially across the integrated chain, continues to progress, even in a climate of soft GDP. The Dow strategy has been to continue to be a leader in all three of the margin opportunity buckets, leveraging the Dow materials science backbone to provide differentiation that amplifies that performance.

I also want to take a minute and share our latest outlook on supply/demand for the ethylene/polyethylene value chain on slide 14. This outlook utilizes the most recent GDP forecast, assumes historical growth multiples to GDP, a gradually recovering China as well as the latest data on capacity additions. Integrated polyethylene and elastomer balances are tight today, and the outlook indicates these balances will stay tight for at least the next several years.

Additional tightness is likely to come from an industry operating reliability issues, both at the monomer and polymer stages of the value chain. As we have discussed many times, much of these assets are old, and unplanned outages across the sector have been and likely will continue to happen at relatively higher frequencies.

With these tight industry balances, any significant unexpected operating event will be met by shortages and a pricing response, which has certainly had an impact on conditions in the US, Europe, and Asia in the last two years. The bottom line in our view is that Dow is well positioned for favorable ethylene and polyethylene industry conditions through at least 2020, based on current announcements and timing to complete the projects.

Before I turn it over to Andrew, let me provide some modeling guidance heading into the fourth quarter
on slide 15. I'll just cover some highlights. On a year-over-year basis the fourth quarter will be impact by divestitures, mainly AgroFresh, Angus, Sodium Borohydride, and Dow Chlorine Products in three material ways.

First, on the revenue line. Please remember revenue will be lower by between $1.3 billion and $1.8 billion. We also expect to realize a negative impact on EBITDA of between $150 million and $225 million and depreciation and amortization will be lower by between $35 million and $50 million.

The other item I would like to point out is the tax rate for the fourth quarter will likely be between 24% and 27% on an operating basis. If Congress enacts the extenders R&D benefit before year end, we will settle at the lower end of the range. As you all know, we closed the Dow Chlorine Products transaction on October 5, which will have a tax impact on the as-reported earnings in the fourth quarter. As a result, we expect our as-reported tax rate will be between 10% to 13%.

Once again, we provided the popular macroeconomic heat map in the appendix of the presentation. And now I would like to turn the call over to Andrew who will provide an update on our outlook, as well as our strategic drivers for the next 24 months. Andrew?

Andrew Liveris (Chairman & CEO):

Thank you, Howard. And slide 16, you will just see in a few moments I'm going to share the next series of our goals that our Board and our Management have come up with for our portfolio transformation over these next two to three years. If you reference slide 17. At our Investor Day in 2014 we summarized what you could expect from Dow for the next 12 months. This series of commitments was a continuum from our 2013 strategy reviews undertaken by our Board, which culminated in a series of choices in our growth engines and our self-help actions.

And what underpinned those reviews in 2013 and was reinforced by our statements at the Investor Forum in 2014 is that we are an emergent and are a cash flow story, that our portfolio fine-tuning would continue with an acute focus on carving out our chlorine chain and cleaning up our joint ventures.

That we would raise our divestment target to $7 billion to $8.5 billion. And that we would continue to fund innovation and organic growth with no big M&A. And that we would return cash to our shareholders through dividend increases and share buybacks.

Slide 18 is a readout of how we did versus what we said. We have over-achieved our targets, and there's no gap between what we said and what we did. We have built a portfolio that has as its foundation both integration and innovation and is structurally hedged to handle all economic conditions. And as I have already referenced, is a cash flow machine.

Let's look at slide 19. As a result of these achievements, the Dow Board and Management have deliberated on our focus for the next 24 to 36 months, and we've built a simple road map for this period and the goals on this page are very clear. Our execution focus over these last three years has been granular and laser-like. This will continue.

First, our productivity goal of $1 billion of cost reductions over three years starting in 2015 will be delivered through Dow's previously announced change management program, Dow 10.0. Second, our large assets in Sadara and on the US Gulf Coast are commencing their commissioning phases. These huge new assets will change from being investment headwinds to cash and earnings tailwinds.

Our CapEx will be ranged down to near depreciation levels over the next two years. We anticipate no new mega projects during these next five years. Third, we will conclude our joint venture portfolio work by providing full clarity on our large joint ventures and their future in Dow.
And turning to slide 20. On Kuwait, these large, highly profitable JVs will pivot through equity restructuring and move to a growth focus. Our partners in Kuwait are excited at the opportunity to consolidate all of their JVs under one ownership umbrella, retain Dow as a minority partner and move forward to a growth path while extracting synergies in their consolidation. The deal structure on this slide will yield over $3 billion of pretax proceeds to Dow by mid-2016, with $1.5 billion by the end of 2015.

On slide 21, our joint venture of 72 years, Dow Corning , is a tremendous asset with a focus on specialty materials and specialty chemicals and, of course, polysilicon via the Hemlock joint venture. Dow and Corning are in discussions around a potential transaction involving Corning's ownership in Dow Corning. We will have more to say on this in the not too distant future.

Slide 22. Dow's portfolio work over these last five years has been to methodically exit commodity cyclical value chains such as those in styrene, butadiene, chlorine, and all their derivatives. As you can see on slide 23, these commodities exhibit no predictability, either on their import price, which is mostly oil-based, or their output price, which have been commoditized and genericized, and have no technology advantage. We have been successful in repositioning the portfolio to growth markets with clear integration and technology differentiation.

Slide 23 shows how we have divested $15 billion of primarily high-beta businesses over these last six years. What is clear to us is that our owners are continually looking at ways enterprises like Dow, with all of our attendant complexity, can not only create value, but actually release that value.

We are very proud of what Dow has built in the agricultural market via Dow AgroSciences. This business has doubled EBITDA over the last five years and has the most envied technology pipeline in chemistry and in traits. By all accounts, this is a successful business with a bright future.

So, despite Dow AgroSciences being a low-beta business, there is a rationale in our opinion that, given the potential synergies in a newly consolidating agricultural market, an attractive opportunity to release value may be upon us. As a result, the Company is only considering those prospects that will extract further value from this business while comparing it to the value of retaining the business.

Slide 24 and 25, the final point on our emphasis goals for the next 24 to 36 months, is captured by the notion that we are generating a lot of cash, have more in our imminent future. And as slide 23 has shown, we have been a returner of that cash -- slide 25 is showing, we have been a returner of cash to you, our shareholders. This will continue. We are pleased to announce our dividend increase to $1.84 a share, this represents a new historic dividend level and we're going to continue to accelerate our share buybacks.

We will continue to return cash to you. We have no plans for any big new CapEx or large M&A in this time frame. We have built a structurally hedged portfolio with tremendous organic growth drivers.

And slide 26 gives you a sense is of these growth drivers. We believe they're unique. We have built three strong integrated pillars of value that uniquely define our enterprise.

We start with cost advantaged monomers in geographies with attractive markets. In the second pillar, we select into industry leading science and engineering, enabling us to create value differentiation with our customers. And in the third pillar, we are select into attractive growth segments of key markets to lower volatility and drive reliability of earnings and cash flow.

The first and second pillars, well, they define our integration. The second and third pillars, they define and leverage our innovation. The key is that no one else in this sector brings both operational and commercial excellence across all three pillars.

And if you look at slide 28, our broad scope of scientific capabilities really creates -- slide 27, really
creates a very highly competitive hurdle, not easily replicated or imitated, creating a benefit for both Dow, and more importantly Dow's customers. Look at those examples that you can see on that slide. They're all unique, all highly valuable to Dow and to our customers.

And looking ahead, we believe the market outlook favors the products, technology, and geographic position of the Dow portfolio. If you look at the market outlook on slide 29, we expect ongoing expansion of growth opportunities that will enable Dow to continue to capture that growth. Growth in mark such as China, the United States, and Europe, despite challenges in soft pockets around the world, such as those in Brazil.

We anticipate strength in construction, packaging, and transportation markets, as well as in electronics, as the interconnectivity of the world continues to increase. And Dow is well positioned to manage, and in fact win from the weakness in agriculture. Our forecasts indicate that there will be a gradual recovery in the oil markets, and gas-based cracking will continue to be advantaged.

In the midst of all of this, our new investments on the US Gulf Coast and in Saudi Arabia are coming online at exactly the right time, further boosting Dow's ability to capture and expand margins. The bottom line is this. Today's macroeconomic realities mean the importance of driving differentiation into the portfolio will only increase, and companies that aim to win will need to invest in innovative solutions and work closely with customers.

Overall, Dow's strategy, our integrated portfolio, our innovation engine, and our proven track record of execution are delivering results. And going forward, and as always, capturing growth where growth exists is not the only way that we will demonstrate consistent earnings growth and strong cash flow. Our self-help and our productivity actions underpin all of our operational and execution tactics.

And our third quarter results highlight this intense focus on delivering the potential of Dow. 12 consecutive quarters of EPS, EBITDA and margin growth, 8 consecutive quarters of volume growth, the highest EBITDA margin result since 2005, the Dow machine is generating strong cash flows and returning that cash to its owners.

And today's announcements outline for you the next 24 to 36 months of actions that will drive continued results and demonstrate our commitment to being exceptional stewards of the opportunities at hand by combining exceptional capital utilization with our drive to return cash to Dow's owners across the intermediate, mid-, and long-term horizons. Our team is distinguishing itself by its performance, and it will continue to do so. And with that, Jack, let's turn to Q&amp;A.

Jack Broodo (VP of IR):

Thank you, Andrew. Now we will move onto your questions. First, however, I would like to remind you that my comments regarding forward-looking statements and non-GAAP financial measures apply to both our prepared remarks and the following Q&amp;A. Rochelle, would you please explain the Q&amp;A procedure?

QUESTIONS &amp; ANSWERS

Operator:

(Operator Instructions)

And our first question, we'll hear from P.J. Juvekar with Citi.

P.J. Juvekar (Analyst - Citigroup):
Good morning. Howard, I like your win/win/win comment.

Howard Ungerleider (EVP & CFO):

it was, P.J. It was a tremendous transaction for both Dow, for Olin, and for all of our shareholders. I mean, it really was.

P.J. Juvekar (Analyst - Citigroup):

So my question is on ag. Andrew, you mentioned that you want fair value, and there's pressure to do something. But is it the right time to divest ag, given that ag markets are depressed? And then on seeds, it doesn't make any money today, but you have this great pipeline. So how do you capture all that in your divestiture comments?

Andrew Liveris (Chairman & CEO):

You have to take it from the two angles that we are taking it with. You have just given us one angle, which is the retention angle. And in a consolidating ag market, the affordability of R&D budgets and the capturing of synergies is another angle. And if you look at our total market cap and you look at the contribution of Dow AgroSciences, both revenue and EBITDA, then projected EBITDA, you could take some molecules and say that its percent of market cap is higher then its percent of either revenues or profit in the enterprise. So that begs value release, and we have talked to many, all of our owners about that.

You can entrust upon us, all of our owners, that we will definitely compare it, as I said in my remarks, to the value of retention. But look, we believe that over time the hurdle of doing business in this sector will only keep increasing. We've done a phenomenal job through collaboration of building our capabilities and we've done a tremendous job, as you acknowledged, on building the pipeline of both chemistry and traits. And we will extract full value in whatever construct we come out with that beats anything towards retention.

Operator:

And next we'll move on to Steve Byrne with Bank of America.

Steve Byrne (Analyst - BofA Merrill Lynch):

Thank you. Your outlook comments include an indication of a widening oil/gas spread benefiting your polyethylene chain. I was wondering what your thoughts were on the outlook for a looming surge of anthracite-based petrochemical production, and do you see that as an opportunity for China to become more competitive in this area? Any leverage you think they can pull to lower the variable costs of that industry?

Andrew Liveris (Chairman & CEO):

I really appreciate the question, and it's a recurring question. Actually way back in 2003, 2004, China's cold olifants projects were looming large, especially with the oil/gas price structures that existed back then. Look, we have been part of it. We've actually assisted one of our partners there to actually move through the approval process. We at one point in time even considered participating ourselves.

But in our view, despite the variable cost comment you just made, there's unlikely to be any new projects being brought forward. These are very hard to run, highly polluting projects, very water intensive. They're all in the wrong place. And we believe that their ability to operate even is suspect, as already witnessed by the one that's online. And if you throw on top of that that there will be subworld scale on the
derivative side, and actually be mostly in the commodity areas, like glycol and gas phase commodity-based polyethylenes and polyprop, it will have little or no effect on the value chain comparisons to either the Middle East production, which we're a part of, or the US production, which we're a part of.

**Operator:**

And our next question we'll hear from Frank Mitsch with Wells Fargo Securities.

**Frank Mitsch (Analyst - Wells Fargo Securities LLC):**

Hey, good morning.

**Andrew Liveris (Chairman & CEO):**

What about the Mets, Frank?

**Frank Mitsch (Analyst - Wells Fargo Securities LLC):**

Andrew, I was just going to say that I'm not sure who is doing a better job of managing, you or Terry Collins of the Mets, so keep --

**Andrew Liveris (Chairman & CEO):**

Terry is a Midland gay. He's born and bred in Midland.

**Frank Mitsch (Analyst - Wells Fargo Securities LLC):**

I did not know that. I did not know that. Sorry, Howard, about the Yankees.

**Howard Ungerleider (EVP & CFO):**

Hey, but are you going to write the check for Cespedes? I mean, Detroit -- I think Detroit helped the Mets this season.

**Frank Mitsch (Analyst - Wells Fargo Securities LLC):**

we are very grateful and we're keeping Murphy. Hey Andrew, you made the comment no large M&A, and then obviously you indicated that you are in discussions with Corning. I was wondering if you could at least conceptually speak about the positioning of the Dow Corning joint venture within Dow proper, the logic behind it, what your expectations might be if in fact you are able to execute on that?

**Andrew Liveris (Chairman & CEO):**

Yes, 72-year JV. Despite the comments on execution with the Mets, we are not foreshadowing an easy execution play here in terms of the partnership being such a strong one. But the good news is both partners know the company inside out, as you might imagine, having been on the boards of this company for a long time, we know the company. Look, Frank, it's just down the road here in Midland, Michigan. The synergies are very unique and are available to one partner, i.e., Dow.

And then of course there's more than that. There's the point you just made about market synergy. As we've rebuilt our portfolio these last many years, Dow Corning's become a much more logical fit on the market side. That wasn't true 10 years ago. Clearly whether it's in the consumer sector, the infrastructure sector, there's electronic materials, building construction, home and personal care, we also see growth synergies on the market side.

This will only happen if it's value accretive to both companies. The win/win/win of Olin, if we can construct
it here, something might happen. But we've been very public about JVs and bringing them on balance sheet or off balance sheet. The Kuwait announcement is obviously moving in the other direction. And we anticipate that if something happens here, it will only happen because it's hugely value creating.

**Operator:**

And next we'll move on to Jeff Zekauskas with JPMorgan.

**Jeff Zekauskas (Analyst - JPMorgan):**

Maybe I can ask Frank's question in a different way. If there are no large M&A transactions that you plan, but there is something that you plan with Dow Corning, is it that we would rule out that Dow would buy the piece of Dow Corning that it doesn't own because you don't plan to make large acquisitions? Or is that not the right inference?

**Andrew Liveris (Chairman & CEO):**

Look, I don't want to be -- there's no vagueness in the two commentaries, just to be very clear.

**Jeff Zekauskas (Analyst - JPMorgan):**

Sure.

**Andrew Liveris (Chairman & CEO):**

There's no big M&A outside of our joint venture work. We've been very clear, our joint venture work is our joint venture work, and will consolidate or deconsolidate. And yes, some people might say that's big M&A. But no, it's not big M&A because it's a joint venture that we're either consolidating or deconsolidating. There's no problem with those statements staples coexisting, Jeff, but I understand your point. There could be cash outlay here. But there will only be cash outlay if it's hugely accretive, just to be very clear.

**Operator:**

And next we'll move on to Peter Butler with Glen Hill Investments.

**Peter Butler (Analyst - Glen Hill Investment Research):**

Yes. Good morning, Andrew.

**Andrew Liveris (Chairman & CEO):**

Hi, Peter.

**Peter Butler (Analyst - Glen Hill Investment Research):**

Is, in fact, your stock market goal is to become a sustainable earnings growth story to replace the old Dow cyclical growth story? And if so, could you talk some about what remains to be done on your M&A and restructuring program? What might reasonably happen in the next, say, 1.5 years?

**Andrew Liveris (Chairman & CEO):**

So the three goals that we punched out today are very clear. We believe that the Kuwait joint venture and the way we're restructuring that will yield cash, and of course for them it will yield growth. So it's a win/win/win. We believe that we have got bolt-on M&A in our future but no big M&A, to Jeff's question, other than whatever we end up doing with Dow Corning.
We believe that Sadara and US Gulf Coast, which by the way Sadara is already sold out on first product and we are pre-marketing as we speak on polyethylene. We’re bringing those assets on at exactly the right time. So the $3 billion EBITDA run rate from the US Gulf Coast assets and the $700 million net income boost steady-state run rate on Sadara is new cash flow.

And Peter, I think the way we should all think about the Company is that it’s going to be a cash flow machine these next several years. As you can already see, our cash flows are being boosted substantially. If we do any degree of monetization on ag of any sort, that just adds even further. And so this is all going to be returned to the shareholder.

We're going to be a consistent dividend payer at the payout ratio of roughly 45% and we're going to be a buyer of our shares while our shares in our view are undervalued. And I think the collective view is you generate cash, you spend that cash to grow organically. We've done that. We've got a lot of organic growth in our innovation pipeline. And we'll keep returning cash to our shareholders.

Operator:

And next we’ll move on to David Begleiter with Deutsche Bank.

David Begleiter (Analyst - Deutsche Bank):

Andrew, nearer term, can you discuss polyethylene price expectations for Q4? [Vimes] as well. And Performance Plastics, how do you view that business versus Q3 sequentially on an EBITDA basis?

Andrew Liveris (Chairman &amp; CEO):

Howard, why don’t you take that?

Howard Ungerleider (EVP &amp; CFO):

Yes, sure. Good morning, David. Yes. I would say, look, when you think about polyethylene around the world, and I would point you to the slide and some of the prepared comments, but November price increases are in the market, positive sentiment is building. I think Andrew made some comments in some of his interviews early this morning about Dow and other producers in Europe closing their order book. So October order books for Dow had been closed for about two weeks, and a few other producers as well.

So that tells you a couple of things. One, inventory through the chain are low, and fundamental underlying demand in Europe is good. We've had really strong demand in Asia. At a Company level, this is a Company comment, not specific to polyethylene, we had 12% volume growth in China versus same quarter year ago. Our packaging business was north of 20%.

So you are seeing demand growth in Asia. You're seeing demand growth in Europe. The US economy still is a bright spot. You've got unplanned events happening. There was a big issue in Brazil in the last week. So that just reinforces the point.

Margins over the next several years should continue to move up. That is the expectation. Fundamental underlying demand will outstrip the additional supply growth. And that's our view.

Operator:

And Don Carson with Susquehanna Financial will have our next question.

Don Carson (Analyst - Susquehanna Financial Group / SIG):

A question on ag, just on near term. On slide 15 you talk about 3% to 5% down sequentially. So are you
expecting ag to lose money again in fourth quarter, kind of a reversal from last year? And then more broadly, as you look to restructure ag or monetize your position, is DCP the model where you might do a reverse Morris Trust and then distribute the shares in the combined entity to Dow shareholders so they can continue to participate in the growth of ag?

**Howard Ungerleider** (EVP & CFO):

So, Don, good morning. Why don’t I take the first question then I’ll throw to the Andrew for the strategic. When you think about ag, no, I don’t think we’re going lose money in the fourth quarter. But it is soft. The market is soft, it’s a highly competitive price environment. We’re still dealing with significant currency headwinds. Brazil in the third quarter was a 50% drop versus a year ago. You’ve got economic issues in Brazil. Argentina is certainly -- we potentially have a devaluation coming here in the fourth quarter after the election. So we’ve got to get through that.

But my point would be in a down market, we are winning. We’re winning with our new molecules on the chemistry side. I highlighted earlier that we are now number two in Brazil corn. That’s a new fact. We were number three. We are now number two. So we are winning. And I think you’re really seeing the pipeline start to come through the market on both the chemistry side and the biotech side. Andrew, you want to (multiple speakers) strategy?

**Andrew Liveris** (Chairman & CEO):

Yes. Don, look, we’re open to all constructs. That was a great construct with the win/win/win of Olin. So we’re open to all constructs that releases more value and actually that value stays with the shareholders. It doesn’t atrophy away in an (inaudible) disadvantaged deal.

**Operator:**

Next we’ll move on to Hassan Ahmed with Alembic Global.

**Hassan Ahmed** (Analyst - Alembic Global Advisors):

Good morning, Andrew.

**Andrew Liveris** (Chairman & CEO):

Good morning.

**Hassan Ahmed** (Analyst - Alembic Global Advisors):

Two-part question on Performance Plastics, if I may. This is a nice sequential bump-up in EBITDA. So the first question is that you mentioned in the press release that Europe, obviously European margins are strong. How did North America fair? Was it sort of flat, down? Just trying to get a sense of how feedstocks flexibility within North America played a role in the quarter. So that’s the first one.

The second one is as you look at 2016, there seems to be a pretty heavy turnaround schedule on the ethylene side of things globally. So do you expect to see effective utilization rates tighten materially from here, particularly through the first half of 2016?

**Andrew Liveris** (Chairman & CEO):

Howard, why don’t you take those?

**Howard Ungerleider** (EVP & CFO):

Yes. Certainly Europe margins were strong in the third quarter. North America came off a little bit, but not
as much as everybody was expecting, or the third-party pundits were pontificating. We've got North American operating rates in the industry are in the either the very high [80%s] or low to even [mid-90%s]. You've got -- the ACC data, you had below 40 days of inventory. So again that tells that you fundamental underlying demand is there. And we're taking advantage of that.

If you project forward the next few years, we've added in -- when our slide in the slide deck, we've added in all the new capacity. I think, frankly, we've been conservative. We added nine crackers on the Gulf Coast coming on between now and 2020. I don't think it's going to be nine, but we wanted to stress test it. Operating rates still go higher from here between now and 2020.

Operator:

And we'll move on to John Roberts with UBS.

John Roberts (Analyst - UBS):

Morning. Why the new executive leadership counsel separate from the Office of Chairman/CEO? Could you talk a little bit about the shuffling you did there?

Andrew Liveris (Chairman &amp; CEO):

Yes. Look, I wouldn’t over-read anything about team structures. Every company does their own thing. We've got the most important part of the team announcement you saw today, John, is the team at the top. The top three of this Company, Howard, Jim, and I, we're going to run the Company. Howard and Jim have got significant responsibilities, new responsibilities, very excited by that. It's a very strong team.

Actually, we've had this team in place for a long time now and they continue to show exceptional performance, as this quarter has shown. But the team that also reports to the CEO, all the governance functions, some of the key functions that now report to Jim and Howard, we're going to pull that together as an executive leadership council that gets together and makes sure that we leverage every aspect of this Company. The three of us have everything. And the three of us, there was a term used at Dow for historians, from back in the 1970s and early 1980s called a troika. I don't know whether that means anything to anyone, but call us that if you like. But the three of us run the Company in terms of the big decisions and the operational decisions.

Operator:

We'll move on --

Howard Ungerleider (EVP &amp; CFO):

I think you just gave at least one of them a headline.

Andrew Liveris (Chairman &amp; CEO):

Of course.

Operator:

And we'll move on to Bob Koort with Goldman Sachs.

Bob Koort (Analyst - Goldman Sachs):

Thanks very much. Andrew, I'm curious as you look about the JVs and then maybe doing something with ag, historically Dow has been pretty flexible. So is there an opportunity to maybe use earn-outs or other mechanisms if you can't come to an agreement on current values for those assets?
And then secondly, I’m guessing as we go through earnings season we’re not going to find many companies that produce the numbers you showed in China, the numbers Howard talked about in the architectural paint markets in Europe. Can you give us some sense of where there’s some one-offs? Was there some trade opportunities, arbitrages, or what kind of confidence do you have that you can sustain those really pretty surprisingly strong volume trends? Thanks.

Andrew Liveris (Chairman & CEO):

Thanks, Bob. I’ll take the first one and give Howard the second. There’s no question that the Dow AgroSciences property is at the top of that beta pyramid, low beta that you saw on one of the slides in the deck. We’ve nurtured it, grown it, cared for it, fed it in terms of R&D, and it’s grown, grown, grown. And it now has the technology pipeline. In the many years we’ve been doing that, the Board has done extensive reviews, certainly no less than semiannually, and some very big deep drills where we spent days at a time.

To look at the ag market, because it’s been obvious that since 15 years, 10 years ago that another round of consolidation will come one day and whenever it does, Dow should be able to answer the questions of releasing the value in the portfolio in the best available construct. So yes, all options are available to us, including the one you just spoke about. Howard, do you want to take the polyethylene thing and the China thing?

Howard Ungerleider (EVP & CFO):

On the flexibility side, I would just say, Bob, we have had a track record of being flexible with our divestitures. So you look at just in the last 12 months, Angus and SBH were straight divests. You look at AgroFresh, which was a SPAC. I think we’re the first Fortune 50 company to do that. I think at the time we announced $900 million of value for AgroFresh. Embedded in that transaction was an earn-out. So that will bring future value, assuming AgroFresh delivers on their financial plan, which we’re confident that they will. there’s also a tax receivable agreement. When you had a the value of earn-out and the tax receivable agreement, that brings the AgroFresh value on an MPV back to Dow of north of $1 billion of value.

Then the Olin RMP. It shows that we’re willing to look at everything. We’ve got a very -- this management team has a very large focus on return on capital, and we’ve been increasing ROC between 100 and 150 basis points a year. And our focus is any transaction we do, we want it to be a help in EVA momentum and ROC increase.

Andrew Liveris (Chairman & CEO):

The China question?

Howard Ungerleider (EVP & CFO):

I’m not even sure I remember what the China question was.

Andrew Liveris (Chairman & CEO):

Why are we seeing the contrarian --

Howard Ungerleider (EVP & CFO):

It’s simple. It really is a -- it plays to our portfolio. If you think about where China is, they’ve exited this heavy industry phase. And it really is all about light industry/consumer. So you think about our materials, whether it’s RO membranes in water, whether it’s our elastomers, whether it’s our architectural paints.
Where 10 years ago you would sell very low-end paint to a developer who would look to spray an entire building. Today you've got people in China who have been in their apartments or their homes for 10 years, they're making the choice and their value proposition is going to be very different from a developer. They're looking for technology, they're looking for things, whether it's our FORMASHIELD, to take formaldehyde out of the air and trap it in the formulation, or one-coat hiding. These are the kinds of products that we have, and you're starting to really see that through each of the three-quarters of the year.

Operator:

And next we'll move to Jonas Oxgaard with Bernstein.

Jonas Oxgaard (Analyst - Sanford C. Bernstein & Co.):

Hi. Congratulations. One comment first. I would stay away from the troika. I would suggest respectfully a triumvirate. Much better (laughter).

Andrew Liveris (Chairman & CEO):

Thank you, Jonas. You may have saved the headline for me.

Jonas Oxgaard (Analyst - Sanford C. Bernstein & Co.):

So that said, I was curious, on the ag side have you already started discussions with potential partners, other owners, or where are you on that timeline?

Andrew Liveris (Chairman & CEO):

Yes. So Jonas, really, literally, since the Monsanto Syngenta conversations began in May, you could imagine that every player talks to everyone. And on a previous call, I think it was the last quarter's earnings call, I basically said Dow will have a seat at the table. So, yes, we're all talking to everyone. There's no imminent deal. I want you to obviously listen to the questions that were asked a couple times about, is this a good time, is this the right value, dah-dah-dah. All that is very key questions that we have to answer for our shareholders. But look, the answer is, everyone is talking to everyone.

Operator:

And next we'll move on to Vincent Andrews with Morgan Stanley.

Vincent Andrews (Analyst - Morgan Stanley):

Thanks, and I unfortunately have another follow-on question on the ag situation. It sounds like you're considering either a sale or keeping it internally. And I'm just wondering, are you also considering intermediate options such as a spin-off or a sub-IPO tracking stock, those types of things? Particularly in the event if the timing or the bid/ask spreads would suggest it might make sense to wait a little bit longer before complete monetization?

Andrew Liveris (Chairman & CEO):

Thank you, Vincent for allowing my shortest answer. Yes.

Vincent Andrews (Analyst - Morgan Stanley):

Okay. And if I could just follow up on the price declines and crop chemistry vis-a-vis the inventory levels. How much of that do you think is just a function of weather-related demand issues? How much of it is a
function of, maybe in Brazil, the financing issues, and are you extending more credit to farmers on their bartering or those types of things? And how much of it is just sort of the dollar has made, maybe in the past made purchasing power and pricing power higher and now that tides gone out a bit? How do you shuffle the deck between those buckets?

Howard Ungerleider (EVP & CFO):

Yes. I would say it's really -- you literally answered the question, because it really is a little bit currency, it's a little bit lower crop prices, which you look at a rented piece of land and the farmer's not able to make money in Brazil on that basis. And there has been -- you throw some weather in there and you mix it all together and it makes for a really challenging environment after three years of pretty high yields with high inventories.

Operator:

And next we'll move on to Jim Sheehan with SunTrust.

Jim Sheehan (Analyst - SunTrust Robinson Humphrey):

Thank you. Regarding your flame retardant technology, you're gaining some new license revenue there. I was wondering if you could just comment on where you see that technology going in the future? Do you think you can grow it outside of Europe?

Howard Ungerleider (EVP & CFO):

I would say, yes, the medium- to long-term plan is that's going to be global technology. So we're seeing nice licensing income. It plays right into our technology material science strength. And, boy, talk about EVA and ROC, it really has been a nice tailwind for building and construction. And we see that continuing to expand over time.

Operator:

And next we'll move on to Aleksey Yefremov with Nomura Securities.

Aleksey Yefremov (Analyst - Nomura Securities Co. Ltd.):

Thank you. What is the EBITDA associated with the (inaudible) global stake being sold? And also, could you comment on the magnitude of the [equate] stake sale as well? How does it compare in terms of proceeds and EBITDA?

Andrew Liveris (Chairman & CEO):

We don't look at it on an EBITDA basis, do we, Howard?

Howard Ungerleider (EVP & CFO):

I would say this. Phase one. This is the beautiful thing, and why I would differentiate in terms of JV consolidation, deconsolidation, it's hidden EBITDA. Remember, because of 20-50 equity accounting, you don't see the EBITDA of our joint ventures. You only see our percentage ownership of the net income after tax of the joint ventures in our EBITDA. So when you look at Phase 1 that we announced today, you're talking about probably in the range of $30 million to $50 million of lost Dow EBITDA in exchange for the $1.5 billion of proceeds. So it's a pretty nice EVA positive.

Operator:

And that will be all the time we have for questions. I would like to turn the call back over to Mr. Broodo for
any additional or closing remarks.

**Jack Broodo** (VP of IR):

Thank you, everyone, for your questions. Andrew, did you have some closing remarks?

**Andrew Liveris** (Chairman & CEO):

Yes, I do. We packed a lot into this call. We appreciate your questions. You've got our earnings release. You've also got our pathway for the next two or three years release as well. We have a Company that's closing out one year early from its goals that we announced in 2013. Our divestment targets were exceeded. We are in the position now of talking about the next two or three years with great clarity, and that clarity has been provided on the call.

This is a Company that has delivered on its promises. There's no gap between what we've said and what we've done, and we intend to continue that. We're getting little to no help from a consistent economy. Witness all the questions on volatility.

Look at the proof points of our portfolio performing in this economy, which we now have got quite a few quarters in a row. Those who worried about low oil, look at our results. Those who worried about China going away, look at our results. The results of the Company and the consistency of performance enables us as a Board and management team to continue to deliver that growth in terms of earnings and cash flow. We are strong cash flow machine, getting stronger back to you.

There is no big M&A. We will consolidate JVs where it makes sense. There is no need to think about this Company directing itself to anything in terms of big CapEx. We've got the big projects starting up. We have done this the last five years with your perseverance, and we are now in the throes of starting up some of the biggest industrial chemical complexes of all time, the one in Saudi Arabia, and of course the big expansion on the US Gulf Coast. We're advantaged on the inputs and we're advantaged on the outputs. That's a structurally hedged portfolio that's very unique to this enterprise.

We commit to you consistent return to shareholders, consistent return of that cash over these last five years. And last but not least, I'm very proud of the team announcements we've made today. We have the team to drive this Company for the next 5 to 10 years in place. It's a team that has consistently grown and delivered for you, the shareholder, and I'm very proud of that. Thank you.

**Jack Broodo** (VP of IR):

Thank you, Andrew. As always, we appreciate your interest in the Dow Chemical Company. For your reference, a copy of our prepared comments will be posted on Dow's website later today. This concludes our call for today. We look forward to speaking with you again soon.

**Operator:**

And that will conclude today's call.

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