

Significant Events

Coronavirus pandemic

Due to the lingering coronavirus pandemic, fiscal 2021 is expected to remain a challenging year for the global economy. The growing availability of vaccines and increasing options for fighting the pandemic are having a positive effect, however. In parallel, we are observing a significant recovery in demand compared with the prior-year quarter. The steps taken by Covestro early on last year to protect the health of all employees will stay in place, so far-reaching health, safety, and hygiene measures are still in effect at our sites. Depending on the local situation in each case, some of our staff, particularly employees in administrative departments, are working from home. Production at our sites was not affected by the pandemic in the first quarter of 2021.

Covestro is monitoring the development of the coronavirus pandemic worldwide on an ongoing basis to ensure that we can react quickly when necessary. Existing measures are modified and continually expanded as required in line with recommendations and instructions issued by the relevant governments and committees of experts.

Other events

On February 25, 2021, Covestro signed an agreement on the sale of its 51% equity investment in subsidiary Pearl Covestro Polyurethane Systems FZCO, which operates the systems house business in Dubai (United Arab Emirates), to current co-shareholder Pearl Industries Overseas Ltd. The proceeds of the sale total an amount in the mid-single-digit millions of euro. The sale is part of an ongoing effort to optimize the portfolio and represents another step toward strategically refocusing the Polyurethanes segment. Subject to approval by the responsible authorities, the transaction will close in the second quarter of 2021.

See "Divestitures."

On April 1, 2021, Covestro completed the acquisition of the Resins & Functional Materials (RFM) business from Koninklijke DSM N.V., Heerlen (Netherlands). Completion of this acquisition of RFM in the Coatings, Adhesives, Specialties segment makes Covestro one of the world's leading suppliers of sustainable coating resins.

See "Acquisitions."

Results of Operations and Financial Position of the Covestro Group

Results of Operations

Business picked up again considerably in the first quarter of 2021 after the initial effects of the coronavirus pandemic led to a decline in demand in the prior-year quarter, particularly in the APAC region. As a result, the Group's core volumes sold increased by 5.3%. In the automotive and transportation industry and the electrical, electronics and household appliances industry, growth was particularly significant. This is attributable mainly to a strong resurgence in demand in the APAC region, where a massive drop in volumes was recorded in the prior-year quarter due to the coronavirus pandemic. However, our growth opportunities in the quarter under review were limited due to unplanned weather-related production stoppages in the NA region and raw material bottlenecks, which led to an overall reduction in product availability. Core volumes sold in the Polyurethanes and Polycarbonates segments rose by 2.5% and 11.6%, respectively. In the Coatings, Adhesives, Specialties segment, core volumes sold were up by 7.1% over the prior-year quarter.

In the first quarter of 2021, Group sales were up by 18.8% to €3,307 million (previous year: €2,783 million). The main factors contributing to this result included a rise in average selling prices, which had a positive effect on sales amounting to 20.2%. This development was mainly driven by the advantageous competitive situation in the Polyurethanes and Polycarbonates segments. Total volumes sold had a positive effect on sales of 3.4%, while exchange rate movements had a negative impact amounting to 4.8%.

In the Polyurethanes segment, sales rose by 30.7% to €1,665 million (previous year: €1,274 million), and the Polycarbonates segment's sales grew by 21.3% to €889 million (previous year: €733 million). In the Coatings, Adhesives, Specialties segment, sales increased by 4.0% to €595 million (previous year: €572 million).

The Group's EBITDA in the first quarter of 2021 improved to €743 million (previous year: €254 million), largely on account of a considerably higher selling price level. Also contributing positively to earnings were the effect of total volumes sold and lower selling and general administrative costs, which were achieved mainly by implementing cost-cutting measures. Higher provisions for variable compensation and a temporary increase in cost of goods sold, mainly due to unplanned production stoppages, reduced earnings.

In the Polyurethanes segment, EBITDA rose to €443 million (previous year: €50 million), and the Polycarbonates segment's EBITDA grew to €222 million (previous year: €109 million). In the Coatings, Adhesives, Specialties segment, EBITDA decreased by 12.3% to €114 million (previous year: €130 million).

The Covestro Group's EBIT increased to €556 million in the first quarter of 2021 (previous year: €67 million).

Financial Position

At €428 million, cash flows from operating activities were up from the prior-year quarter (previous year: €–110 million), largely due to an increase in EBITDA. At the same time, lower income tax payments and an overall reduction in funds tied up in working capital compared with the prior-year quarter had a positive effect.

Free operating cash flow rose to €318 million in the first quarter of 2021 (previous year: €–249 million). This is attributable to the increase in cash flows from operating activities and reduction in cash outflows for additions to property, plant and equipment compared with the prior-year quarter.

Net financial debt

	Dec. 31, 2020	Mar. 31, 2021
	€ million	€ million
Bonds	1,990	1,990
Liabilities to banks	227	226
Lease liabilities	672	691
Liabilities from derivatives	9	18
Other financial liabilities	1	1
Receivables from derivatives	(13)	(15)
Financial debt	2,886	2,911
Cash and cash equivalents	(1,404)	(2,106)
Current financial assets	(1,126)	(710)
Net financial debt	356	95

In comparison with December 31, 2020, the Covestro Group's financial debt increased slightly by €25 million to €2,911 million as of March 31, 2021.

Cash and cash equivalents rose in comparison with the figure on December 31, 2020, by €702 million to €2,106 million. In addition to positive cash flows from operating activities of €428 million, this was the result of short-term bank deposits totaling €355 million maturing and the sale of money market fund units totaling €61 million. In contrast, cash outflows for additions to property, plant, equipment and intangible assets at €110 million reduced cash and cash equivalents. This led to an overall drop in current financial assets by €416 million to €710 million.

The increased balance of cash and cash equivalents at the end of the quarter is earmarked for financing the price of acquiring the Resins & Functional Materials (RFM) business from Koninklijke DSM N.V., Heerlen (Netherlands).

See "Acquisitions."

Net financial debt declined by €261 million compared with the figure on December 31, 2020, to €95 million as of March 31, 2021.

Performance of the Reportable Segments

Polyurethanes

Polyurethanes key data

	1st quarter 2020	1st quarter 2021	Change
	€ million	€ million	%
Core volume growth¹	-3.6%	+2.5%	
Sales	1,274	1,665	+30.7
Change in sales			
Volume	-2.5%	+0.2%	
Price	-10.8%	+36.1%	
Currency	+0.7%	-5.6%	
Portfolio	-1.1%	0.0%	
Sales by region			
EMLA	589	804	+36.5
NA	395	357	-9.6
APAC	290	504	+73.8
EBITDA	50	443	>700
EBIT	(51)	340	.
Cash flows from operating activities	(86)	202	.
Cash outflows for additions to property, plant, equipment and intangible assets	84	71	-15.5
Free operating cash flow	(170)	131	.

¹ Reference values calculated on the basis of the definition of the core business effective March 31, 2021.

In the first quarter of 2021, the core volumes sold in the Polyurethanes segment increased by 2.5% over the prior-year quarter. Contributing factors here primarily included the positive volume development in the electrical, electronics and household appliances industry and in the automotive and transportation industry, chiefly due to greater demand in the APAC region. The prior-year quarter was marked by the effects of the coronavirus pandemic, particularly in the APAC region. At the same time, unplanned weather-related production stoppages in the Polyurethanes segment's NA region in the current quarter led to reduced product availability and limited potential growth.

The Polyurethanes segment's sales were up by 30.7% to €1,665 million in the first quarter of 2021 (previous year: €1,274 million). The key driver here was the higher selling price level, mainly due to an advantageous competitive situation. This increased sales by 36.1%. The development of total volumes sold had a positive effect on sales of 0.2%. Exchange rate movements, however, had a negative effect of 5.6%.

In the EMLA region, sales grew by 36.5% over the prior-year quarter to €804 million (previous year: €589 million) on account of a sharp increase in average selling prices. A decline in total volumes sold there and the change in exchange rates each had a slightly negative effect on sales. In the NA region, sales dropped by 9.6% to €357 million (previous year: €395 million). The key factors here were the development in total volumes sold and in exchange rates, each of which put significant downward pressure on sales. In contrast, an increased selling price level had a strong positive effect on sales. Sales in the APAC region climbed by 73.8% to €504 million (previous year: €290 million). This was due to factors including a rise in average selling prices and higher total volumes sold, both of which gave sales a significant boost. In contrast, exchange rate movements had a considerable negative impact on sales.

EBITDA in the Polyurethanes segment was up over the prior-year quarter to €443 million in the first quarter of 2021 (previous year: €50 million). The key drivers here were the higher selling price level and lower selling and general administrative costs, which were achieved mainly by implementing cost-cutting measures. In contrast, higher provisions for variable compensation and a temporary increase in cost of goods sold, mainly due to unplanned production stoppages, reduced earnings.

In the first quarter of 2021, EBIT jumped to €340 million (previous year: €-51 million).

Free operating cash flow rose to €131 million in the first quarter of 2021 (previous year: €-170 million), mainly on account of the increase in EBITDA and lower cash outflows for additions to property, plant and equipment.

Polycarbonates

Polycarbonates key data

	1st quarter 2020	1st quarter 2021	Change
	€ million	€ million	%
Core volume growth¹	-4.8%	+11.6%	
Sales	733	889	+21.3
Change in sales			
Volume	-2.6%	+12.5%	
Price	-9.6%	+13.8%	
Currency	+1.0%	-5.0%	
Portfolio	-3.6%	0.0%	
Sales by region			
EMLA	262	292	+11.5
NA	181	147	-18.8
APAC	290	450	+55.2
EBITDA	109	222	>100
EBIT	54	168	>200
Cash flows from operating activities	35	105	>200
Cash outflows for additions to property, plant, equipment and intangible assets	29	16	-44.8
Free operating cash flow	6	89	.

¹ Reference values calculated on the basis of the definition of the core business effective March 31, 2021.

In the first quarter of 2021, core volumes sold by the Polycarbonates segment increased by 11.6% over the prior-year quarter. The key driver of this development was a strong resurgence of demand that had begun in the second half of 2020. Demand had declined substantially in the prior-year quarter as a result of the coronavirus pandemic, particularly in the APAC region. The upsurge in demand led to an increase in core volumes sold in the electrical, electronics and household appliances industry and in the automotive and transportation industry, especially in the APAC region. At the same time, unplanned weather-related production stoppages in the Polycarbonates segment's NA region led to reduced product availability and limited our growth potential.

In the first quarter of 2021, sales in the Polycarbonates segment were up by 21.3% to €889 million (previous year: €733 million). Higher average selling prices due to an advantageous competitive situation as well as an increase in total volumes sold led to positive effects on sales of 13.8% and 12.5%, respectively. Exchange rate movements reduced sales by 5.0% in contrast.

In the EMLA region, sales were up by 11.5% to €292 million (previous year: €262 million). The change in total volumes sold had a significant positive impact on sales, while higher selling prices lifted sales slightly. However, exchange rate movements were neutral overall in terms of sales. In the NA region, sales dropped by 18.8% to €147 million (previous year: €181 million). Contributing factors here were the decline in total volumes sold and exchange rate movements, both of which had a considerable adverse effect on sales. The average selling price level remained stable in this region compared with the prior-year quarter. In the APAC region, sales climbed by 55.2% to €450 million (previous year: €290 million). The changes in selling prices and total volumes sold each contributed to very strong sales growth. However, exchange rate movements reduced sales considerably.

EBITDA in the Polycarbonates segment grew over the prior-year quarter, amounting to €222 million in the first quarter of 2021 (previous year: €109 million). The increase in selling prices and decrease in raw material prices led to significantly higher margins, which bumped up earnings. Growth in total volumes sold also had a positive effect on EBITDA. However, higher provisions for variable compensation reduced earnings.

In the first quarter of 2021, EBIT increased to €168 million (previous year: €54 million).

Free operating cash flow was up, amounting to €89 million in the first quarter of 2021 (previous year: €6 million), largely due to the improvement in EBITDA. The year-over-year increase in funds tied up in working capital was offset by decreased cash outflows for additions to property, plant and equipment.

Coatings, Adhesives, Specialties

Coatings, Adhesives, Specialties key data

	1st quarter 2020	1st quarter 2021	Change
	€ million	€ million	%
Core volume growth¹	-5.2%	+7.1%	
Sales	572	595	+4.0
Change in sales			
Volume	-7.1%	+5.6%	
Price	-3.9%	+2.4%	
Currency	+1.1%	-4.0%	
Portfolio	+1.1%	0.0%	
Sales by region			
EMLA	279	268	-3.9
NA	139	127	-8.6
APAC	154	200	+29.9
EBITDA	130	114	-12.3
EBIT	100	85	-15.0
Cash flows from operating activities	40	45	+12.5
Cash outflows for additions to property, plant, equipment and intangible assets	25	23	-8.0
Free operating cash flow	15	22	+46.7

¹ Reference values calculated on the basis of the definition of the core business effective March 31, 2021.

In the first quarter of 2021, core volumes sold in the Coatings, Adhesives, Specialties segment rose by 7.1% over the prior-year quarter, which had been adversely affected by the coronavirus pandemic, especially in the APAC region. Volumes grew in all main customer industries, especially the furniture and wood processing industry. The main contributor to this trend was positive volume growth in the APAC region. At the same time, raw material bottlenecks in the Coatings, Adhesives, Specialties segment in the quarter under review led to reduced availability of products and curtailed growth opportunities.

In the first quarter of 2021, sales in the Coatings, Adhesives, Specialties segment rose by 4.0% to €595 million (previous year: €572 million). An increase in total volumes sold and higher selling prices had a positive effect on sales of 5.6% and 2.4%, respectively. This stood in contrast to a change in exchange rates, which reduced sales by 4.0%.

Sales in the EMLA region were down by 3.9% to €268 million (previous year: €279 million), chiefly due to a slight decrease in total volumes sold. In contrast, higher average selling prices modestly improved sales. Exchange rate movements were neutral overall in terms of sales. In the NA region, sales dropped by 8.6% to €127 million (previous year: €139 million). Changes in exchange rates, which put significant downward pressure on sales, was the main contributor to this development. In addition, a slight negative effect was exerted on sales by the decline in total volumes sold. The development of the selling price level lifted sales somewhat in contrast. Sales in the APAC region rose by 29.9% to €200 million (previous year: €154 million), mainly because of a considerable increase in total volumes sold. Moreover, higher average selling prices caused sales to rise slightly. However, the change in exchange rates brought down sales substantially.

EBITDA in the Coatings, Adhesives, Specialties segment declined by 12.3% from the prior-year quarter to €114 million in the first quarter of 2021 (previous year: €130 million). Higher provisions for variable compensation and a temporary increase in cost of goods sold, mainly due to unplanned production bottlenecks, resulted in a reduction in earnings. In contrast, a higher selling price level and a positive volume effect contributed to increasing earnings.

In the first quarter of 2021, EBIT dropped by 15.0% to €85 million (previous year: €100 million).

Free operating cash flow grew by 46.7% to €22 million in the first quarter of 2021 (previous year: €15 million). The decrease in funds tied up in working capital compared to the prior-year quarter and lower cash outflows for additions to property, plant and equipment had a positive effect on free operating cash flow. This stood in contrast to a decline in EBITDA, which had a negative effect.

Forecast

Economic Outlook

Global economy

The lingering coronavirus pandemic is likely to make the year 2021 another challenging one for the global economy. Likewise, the spread of coronavirus variants raise the possibility of new waves of the pandemic, which could affect growth negatively. However, as a result of the increasing availability of vaccines and the start of a controlled approach to fighting the pandemic, we continue to expect a return to positive growth rates in all regions. In contrast to the outlook we published in the 2020 Annual Report, we now anticipate a faster recovery of the global economy and a resulting greater increase in economic performance of 5.3%.

We revised our estimates for all regions upward, principally due to expected higher production volumes and consumer spending. In the NA region, we anticipate a significant increase in expected economic growth compared with our outlook published in the 2020 Annual Report. This is attributable to factors including the increase in the U.S. economic stimulus package to USD 1.9 trillion. In contrast to the projection in the 2020 Annual Report, the overall economic situation in the EMLA and APAC regions appears to be improving somewhat, which led to an upward revision of the expected growth there.

Economic growth¹

	Growth 2020	Growth forecast 2021 (2020 Annual Report)	Growth forecast 2021
	%	%	%
World	-3.7	+4.4	+5.3
Europe, Middle East, Latin America², Africa (EMLA)	-5.9	+3.4	+3.8
of which Europe	-6.2	+3.2	+3.8
of which Germany	-5.3	+2.8	+3.5
of which Middle East	-4.2	+4.5	+4.4
of which Latin America ²	-7.5	+3.7	+3.5
of which Africa	-2.6	+2.4	+3.2
North America³ (NA)	-3.9	+4.0	+6.1
of which United States	-3.5	+4.0	+6.2
Asia-Pacific (APAC)	-1.2	+5.7	+6.2
of which China	+2.3	+7.6	+7.9

¹ Real growth of gross domestic product; source: IHS (Global Insight), Growth 2020 and Growth forecast 2021 as of April 2021.

² Latin America (excluding Mexico).

³ North America (Canada, Mexico, United States).

Main customer industries

In all main customer industries, we continue to forecast positive growth for the year 2021. However, we expect the pace of growth to differ in the individual industries.

Growth in main customer industries¹

	Growth 2020	Growth forecast 2021 (2020 Annual Report)	Growth forecast 2021
	%	%	%
Automotive	-15.9	+17.3	+15.7
Construction	+2.0	+0.6	+1.1
Electrical, electronics and household appliances	+4.5	+6.3	+8.7
Furniture	-6.8	+4.6	+4.5

¹ Covestro's estimate, based on the following sources: LMC Automotive Limited, B+L, CSIL (Centre for Industrial Studies), Oxford Economics. We limited the economic data of our "automotive and transportation" and "furniture and wood processing" main customer industries to the automotive and furniture segments (not the transportation or wood processing segments). As of: April 2021.

Growth in the automotive industry is projected to be 15.7%, down from the outlook presented in the 2020 Annual Report. The growth expected for the furniture industry was also corrected slightly downward. In contrast, we anticipate an increase in the growth rate of the electrical, electronics and household appliances industry to 8.7%, up from our forecast in the 2020 Annual Report. At 1.1%, growth in the construction industry will likely exceed the projection in the 2020 Annual Report.

Forecast for the Covestro Group

The analysis of the development of our key management indicators is based on the business performance described in this Quarterly Statement, the economic outlook outlined above, and consideration of our potential risks and opportunities. There have been no fundamental changes in the risk situation from the presentation in the 2020 Annual Report. At the time this Quarterly Statement was prepared, there were no risks that could endanger the Group's continued existence. The acquisition completed on April 1, 2021, and the integration of the Resins & Functional Materials (RFM) business of Koninklijke DSM N.V., Heerlen (Netherlands), into the Coatings, Adhesives, Specialties segment has been factored into this forecast. One-time costs that could arise in conjunction with the LEAP transformation program have not been considered.

Covestro adjusted the forecast presented in the 2020 Annual Report on April 13, 2021, as a result of business development that has been better than expected to date. We now expect the following changes in our key management indicators over the course of the rest of fiscal 2021:

Forecast for key management indicators

	2020	Forecast 2021 (2020 Annual Report)	Adjusted Forecast 2021
Core volume growth	-5.6%	Between 10% and 15%	Between 10% and 15%
Free operating cash flow (FOCF)	€530 million	Between €900 million and €1,400 million	Between €1,300 million and €1,800 million
Return on capital employed (ROCE) ¹	+7.0%	Between 7% and 12%	Between 12% and 17%

¹ ROCE: The return on capital employed is calculated as the ratio of EBIT after taxes to capital employed. Capital employed is the capital used by the company. It is the sum of noncurrent and current assets less noninterest-bearing liabilities such as trade accounts payable.

We still anticipate that core volume growth for the Covestro Group will be between 10% and 15%, with around 6 percentage points attributable to the acquisition of the RFM business. We also continue to project growth for the Coatings, Adhesives, Specialties segment significantly above the corridor expected for the Group. For the Polyurethanes and Polycarbonates segments, our growth projection remains in the mid- to high-single-digit percentage range.

This year, FOCF is forecast to fall between €1,300 million and €1,800 million. Owing to one-time expenses in conjunction with the RFM acquisition, we continue to expect FOCF in the Coatings, Adhesives, Specialties segment to be significantly below the prior-year value. In contrast, FOCF in the Polyurethanes and Polycarbonates segments is still anticipated to come in well above the prior-year levels.

For fiscal year 2021, we now expect a ROCE of between 12% and 17%.