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DuPont Specialty Products USA, LLC

1Q 2023 Earnings

TOTAL PAGES:27

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

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DuPont Specialty Products USA, LLC

1Q 2023 Earnings

PRESENTATION:

Operator^ Ladies and gentlemen, thank you for standing by. Welcome to the DuPont First Quarter 2023 Earnings Call. I would now like to turn the call over to Chris Mecray, Head of Investor Relations. Please go ahead.

Christopher Mecray^ Good morning. Thank you for joining us for DuPont's first quarter 2023 financial results conference call. Joining me today are Ed Breen, Chief Executive Officer; and Lori Koch, Chief Financial Officer. We have prepared slides to supplement our remarks which are posted on DuPont's website under the Investor Relations tab and through the webcast link.

Please read the forward-looking statement disclaimer contained in the slides. During this call we will make forward-looking statements regarding our expectations or predictions about the future.

Because these statements are based on current assumptions and factors that involve risks and uncertainties, our actual performance and results may differ materially from our forward-looking statements.

Our Form 10-K, as updated by our current and periodic reports includes detailed discussion of principal risks and uncertainties, which may cause such differences. Unless otherwise specified, all historical financial measures presented today exclude significant items.

We will also refer to other non-GAAP measures. A reconciliation to the most directly comparable GAAP financial measure included in our press release and presentation materials and have been posted to DuPont's Investor Relations website. I'll now turn the call over to Ed.

Edward Breen^ Good morning. Thank you for joining our first quarter 2023 financial review. This morning we announced quarterly results with operating EBITDA in line and revenue and adjusted EPS slightly better than our previously communicated guidance.

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

This performance reflects our team's continued strong execution while facing short-term volume pressure in select consumer-driven short-cycle end markets, including electronics and construction.

First quarter organic revenue declined 3% versus the year ago period, despite double-digit declines from electronics lines of business of interconnect solutions and semiconductor technologies, mitigating the weakness in electronics and construction markets, was ongoing broad demand strength in areas, including water, automotive, aerospace and health care, along with the carryover benefit of pricing actions taken last year to offset inflationary pressure.

Adjusted EPS was up 2% as we continue to realize benefits from our ongoing capital allocation strategy. As expected, operating EBITDA declined versus the year ago period driven by lower volumes. Given the near-term slowdown in short-cycle end markets, we continue to be proactive in taking actions within our control to minimize volume pressure while also focusing on optimizing cash flow generation. As a result, we expect to continue to show the resiliency of the new DuPont portfolio and expect that our financial results will generate returns commensurate with top tier multi-industrial assets.

In addition to our commitment to generating value through delivery of consistent operating performance, we also continue to focus on accretive and value-added capital deployment. This morning, we announced a definitive agreement to acquire Spectrum, a leading manufacturer of critical components and devices for medical end markets for \$1.75 billion or \$1.72 billion after certain tax attributes.

This deal fits with our strategy to focus on the Industrial Technologies growth pillar expanding our offerings into the fast-growing health care market. Turning to Slide 4. We have had our eye on Spectrum which is a current DuPont customer for a long time, and our team is extremely excited for this opportunity.

Spectrum is a recognized leader in advanced manufacturing of specialty medical devices and components serving 22 of the top 26 medical device OEMs with relationships that date back decades and a strategic focus on fast-growing therapeutic devices and components. Their business is predominantly North American focused and has

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

demonstrated consistent growth over many years. We expect them to generate revenues of about \$500 million in 2023.

As you can see on Slide 5, DuPont's existing health care portfolio is quite strong today. As a reminder, our current health care portfolio is comprised of Liveo medical device and biopharma consumables business, which is a key part of the Industrial Solutions line of business and our Tyvek Healthcare Packaging business reported through Safety Solutions.

Together, these businesses represent \$800 million of total revenue and grow at rates exceeding the company average and well above GDP at solid rates of profitability. The Spectrum business fits nicely with our existing Liveo franchise and will complement our established position in biopharma consumables, bringing world-class manufacturing capabilities and deep OEM customer relationships.

On Slide 6, you can see the addition of Spectrum to our portfolio is impactful and the combined presence in healthcare will now represent approximately 10% of DuPont's total sales. The transaction adds higher growth while further reducing cyclicity in the portfolio.

Also worth noting the transaction significantly increases the total addressable market we serve within health care devices. These businesses are expected to grow at high single-digit rates over time and even faster in 2023 due to specific business wins in place.

This transaction has compelling strategic rationale, as you can see on Slide 7. The Spectrum business expands DuPont's growth strategy of customer-centered innovation and strengthen our existing stable position in fast-growing health care end markets. We are excited by the complementary fit and specifically, our ability to leverage the strengths from each side to generate incremental growth opportunities on top of already growing core markets.

As an example of this on the biopharma side, DuPont Liveo has extensive direct relationships with leading OEMs in the biopharma space and has a proven design and build co-development model. The added advanced manufacturing capabilities enabled

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

by Spectrum will expand its product and capability set to meet stringent customer specifications essentially adding a new pipeline for the Spectrum side by adding new customer relationships.

On the medical device side, as an example, Spectrum has extensive direct relationships with leading OEMs including with 22 of the top 26 players, adding Liveo silicone offerings and DuPont's material science technology will enhance Spectrum's depth of cooperation with customers and expand its product offerings. Spectrum is expected to accelerate top line growth for Industrial Solutions and DuPont as a whole.

Regarding deal terms, the net purchase price of \$1.72 billion after certain tax adjustments, represents a 15.6x EBITDA multiple based on 2023 estimates, or 13.2x after moderate expected cost synergies of \$20 million.

In line with our return hurdles for capital deployment, the acquisition is expected to deliver high single-digit ROIC by year five, excluding revenue synergies that we described, we believe the combined growth opportunities I just mentioned, can add incremental value to the business combination. We expect this transaction will close by the end of the third quarter this year, and we do not anticipate significant regulatory hurdles. We plan to finance the transaction with cash on hand.

Given a lot of moving parts on our capital allocation over the last six months, let's briefly review our status on Slide 8. From closing of the M&M sale in November through today, we have deployment actions and plans in place to account for the full \$11 billion of gross cash received from the sale through a disciplined capital allocation process.

In the fourth quarter of last year, we announced a \$5 billion share repurchase authorization and took actions to deleverage our balance sheet by paying down \$2.5 billion in senior notes and reducing commercial paper from \$1.3 billion to 0 at year-end and remaining undrawn through the first quarter.

Regarding share repurchases, we still expect to complete the \$3.25 billion accelerated share repurchase program launched last November, in the third quarter of this year and remain committed to completing the remaining \$2 billion of authorization as an ASR shortly thereafter.

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

Today's announcement to acquire Spectrum with cash on hand, essentially completes the deployment of any remaining excess cash from the M&M transaction. In terms of additional cash sources, I will note that we are progressing with our plans to sell the Delrin business and continue to expect the planned transaction to close by year-end 2023.

Our current capitalization remains very sound with no significant debt maturities until November 2025. Looking through all currently communicated deployment actions inclusive of the Delrin sale, we expect net leverage to finish the year around 2x. We are comfortable with that leverage point which is more in line with our multi-industrial peers, and we expect to remain at that level as an equilibrium target going forward. With that, let me turn it over to Lori to review our financial performance and outlook.

Lori Koch^ Thanks, Ed, and good morning. Our first quarter financial results reflect our team's ongoing strong focus on execution and operational excellence as we began 2023. In a pressured volume environment within consumer electronics and construction, we are focused on the operational levers within our control to drive solid operating EBITDA and minimize margin impact despite volume decrements in some of our most profitable lines of business.

Turning to our financial highlights on Slide 5. First quarter net sales of \$3 billion decreased 8% as reported and 3% on an organic basis versus the year ago period. Currency resulted in a 3% headwind from dollar strength against key currencies most notably the Yen, Yuan and Euro, and we also saw a 2% headwind related to portfolio changes. Breaking down the 3% organic sales decline. 4% pricing gains were more than offset by a 7% volume decline.

Pricing reflects the carryover impact of actions taken during 2022 to offset broad-based inflation related to raw materials, logistics and energy. Volume decline reflects weakness in consumer electronics, resulting from decreased consumer spending, channel inventory destocking and softness in construction. Lower volume in these consumer-driven short-cycle end markets was partially mitigated by ongoing strength in water, automotive, aerospace and healthcare markets.

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

Taken in combination, volume within electronics and construction end markets during the quarter was down high teens in the aggregate versus the year ago period while our remaining businesses were up low single-digits. From a regional perspective, Europe and North America sales in the quarter were up 5% and 1%, respectively, on an organic basis while Asia Pacific was down 10% versus the year ago period. China sales were down nearly 20%, driven principally by the electronics weakness.

First quarter operating EBITDA of \$714 million decreased 13% versus the year ago period, driven by lower volumes and the impact of reduced production rates in electronics as we scale back production to better align with demand. Currency was also a headwind.

Operating EBITDA margin during the quarter of 23.7% was down 130 basis points driven by volume pressure and inclusive of mixed headwinds related to lower volumes within the high-margin semi business. Decremental margin for the quarter was 41%. Given the high teens volume declines in our electronics portfolio, our overall decrements were disproportionately impacted as these businesses are some of the most profitable within the DuPont portfolio.

Adjusted EPS in the quarter of \$0.84 per share increased 2% versus last year, which I will detail shortly. Looking at cash performance. Cash flow from operations during the quarter of \$343 million less cash paid for CapEx of \$241 million resulted in adjusted free cash flow of \$102 million.

Included within free cash flow are transaction cost headwinds of about \$75 million related to those cash payments associated with the M&M deal closing and ongoing Delrin Divestiture Cost. Turning to Slide 10.

Adjusted EPS for the quarter of \$0.84 per share increased 2% compared to \$0.82 in the year ago period. Headwinds related to overall volume declines were more than offset by the low the line benefits, including an \$0.11 benefit related to lower net interest expense and a \$0.09 benefit due to share repurchases including the upfront benefit of our ongoing ASR program initiated last November.

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

Our tax rate for the quarter was 23.4%, up from 21.8% in the year ago period resulting in a \$0.02 headwind to adjusted EPS, driven primarily by geographic mix of earnings. Turning to segment results, beginning with ENI on Slide 11.

ENI first quarter net sales of \$1.3 billion decreased 16% as organic sales declined 13%, along with currency headwinds of 2% and unfavorable portfolio impact of 1%. The organic sales declines reflect a 15% decrease in volume, partially offset by a 2% increase in price. The organic sales decrease for ENI was driven by Interconnect Solutions, which was down 21% and in Semiconductor Technologies, which was down mid-teens.

The decline in interconnect was driven by weak smartphone, PC and tablet demand along with channel inventory destocking. Our PCB customers in China operates in the first quarter with utilization rates in the mid-40s, which is an expected cycle low. The decline in semi tech resulted from reduced semiconductor fab utilization rates due to weak end market demand as well as downstream destocking of finished chip inventories.

[Semi chip fab utilization] rates in the first quarter averaged around 80% which we expect to dip somewhat in the second quarter as these customers work down inventories. We expect recovery in fab rates began during the third quarter.

Sales for Industrial Solutions were up low-single-digits on an organic basis as pricing and ongoing strength in Vespel aerospace products and in healthcare for applications such as biopharma consumables were partially offset by lower demand in largely consumer-driven areas, such as advanced printing and lighting applications.

Operating EBITDA for E&I of \$362 million was down versus the year ago period primarily due to the drop-through impact of volume declines, which correspond to the lower customer utilization rates just referenced and our lower operating rates, as also mentioned. Turning to Slide 12.

W&P first quarter net sales of \$1.45 billion increased 1% as organic sales growth of 4% was mostly offset by a 3% currency headwind. Organic growth reflects a 6% increase in price resulting from the carryover impact of pricing actions taken last year, partially offset by a 2% decrease in segment volumes. Organic sales growth was led by Water

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

Solutions, which was up low-double-digits on strong pricing and continued demand growth for water filtration led by reverse osmosis product lines.

Safety Solutions sales were up mid-single-digits on an organic basis on pricing and volume gains. Volume growth was driven by Kevlar and Nomex demand in aerospace and automotive markets, especially for EVs coupled with Tyvek strength in healthcare. Shelter Solutions was down mid-single-digits on an organic basis on greater than 10% volume decline due to softness in construction markets, partially offset by pricing.

Operating EBITDA for W&P of \$344 million increased 1% as pricing and disciplined cost control were largely offset by inflationary cost pressure, primarily related to higher raw material and energy costs currency headwinds and lower volume. Before I turn it back to Ed, I'll close with a few comments on our financial outlook and guidance for second quarter and full year 2023 on Slide 13.

As we look at the current demand environment, we continue to expect ongoing strength throughout the year in areas such as water, automotive, aerospace and healthcare. Within electronics markets, we continue to see weakness in channel inventory destocking in the near term. Based on recent customer feedback, echoed by their public commentary and third-party market forecast.

We expect customer utilization rates to bottom relatively near term and to improve during the third quarter, which is about a quarter later than previously expected. To highlight these assumptions, we've included current market forecasts for semiconductor and smartphone market on Slide 14.

For semiconductors, third-party research now suggests MSI will be down 13% for the full year 2023 compared to estimates last quarter, indicating down mid-single-digits, with fab utilization expected to ramp back up above 80% beginning in the fourth quarter. For both of these end markets, you can see the expected improvement beginning during the third quarter, which reflects a later and somewhat more gradual pace than the assumptions last quarter.

Due to the delay in the near-term recovery, we are adjusting the high end of our full year guidance ranges for net sales, operating EBITDA and adjusted EPS. We now expect

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

full year net sales to be between \$12.3 billion and \$12.5 billion, operating EBITDA to be between \$3 billion and \$3.1 billion and adjusted EPS to be between \$3.55 and \$3.70 per share.

For the second quarter 2023, we expect similar results for the first quarter as overall market conditions are anticipated to be generally consistent. On a longer-term view, historical data suggests downturns in these markets are short, lasting about three to four quarters which gives us confidence in the longer-term growth for electronics as we get through this year. With that, I'll turn it back to Ed.

Edward Breen^ Thanks, Lori. Before we take your questions, I'd like to highlight that we published our annual sustainability report yesterday, highlighting the ongoing work of our employees across the globe to meet our commitments across all aspects of ESG. As a reminder, our sustainability strategy is grounded in three pillars, innovation, protecting people on the planet and empowering employees and customers. I continue to be proud of the progress we are making on our 2030 goals and remain impressed at the speed in which we are advancing.

On climate change, we exceeded our 2030 acting on climate goal to reduce Scope 1 and 2 greenhouse gas emissions by 30%, well ahead of schedule and we have set a new goal, which has been validated by SBTi to reach a 50% reduction in emissions by 2030.

Regarding innovation, 80% of our top innovation programs deliver sustainability value for customers. Within water, we've helped to enable seawater to be used as a source of potable drinking water with our reverse osmosis technology. We are also helping reduce carbon emissions through building materials innovation and protection.

In auto markets, we're making electric vehicle battery safer with our materials for thermal management. And within electronics, we directly enabled increased performance requirements in semiconductor manufacturing.

In our community, we engaged over 500 community projects with over 300 nonprofit partners across 30 countries focused on STEM education. From a DE&I standpoint, many aspects of our inclusive culture continue to be recognized. 2022 marked our second year on Forbes Magazine's world's top female-friendly companies list as one example.

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

There are many great examples and stories in the report of how our teams are delivering on our purpose and driving sustainability. Overall, our teams have done a tremendous job. With that, we are pleased to take your questions, and let me turn it back to the operator to open the Q&A.

Operator^ (Operator Instructions) Our first question comes from Steve Tusa from JPMorgan.

Charles Tusa^ Could you just help level set us on where you stand as far as the amount left -- you have left to buy back for the rest of the year and the pace on that? And then when the -- when Delrin closes, just remind us of the proceeds you're expecting there and what you'd expect to do with that cash?

Lori Koch^ Yes, I'll take the share repurchase. So we still have \$2 billion left to complete, which we will do on the back of the completion of the current ASR, which is expected sometime in the August, September time frame. We'll get started on the second program and be able to take 80% of the shares out upfront and then it usually will take us about six months to complete the full \$2 billion authorization. Turning to Ed for Delrin comment.

Edward Breen^ Yes. So Delrin, we're expecting to close by the end of the year. We've been doing all the carve out work. So we're very far along on accomplishing all that. I'm not going to talk about what we sell it for. But the EBITDA is about \$180 million on the business. So you kind of figured out the ZIP code on that as we move forward. Again, that cash should be somewhere kind of end of the year, beginning of next year.

Charles Tusa^ Got it. And then just lastly, on price cost. What's your outlook for pricing for the non-electronics businesses in the second half? And any update on your -- on the spread for the year, if there's any positive benefit there? I think it was \$100 million or something in prior guide.

Edward Breen^ Yes. We have not changed that, Steve. Maybe we're being conservative, obviously, as we've said before, we've worked very hard with our teams on how we're going to handle this as we move forward.

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

The timing is -- we're seeing a little bit of it, by the way, because of logistics and shipping rates being down -- but the big bulk of it will be on the raws. It will be more on the W&P side. And remember, by the time we renegotiate contracts and then you've got like a four-month window to get it through our supply chain into a finished good that's sold.

The kind of figure out timing of it, but we have not changed the assumption, which is very little of the \$800 million that we raised pricing. And we'll just update everybody as we get to next quarter on that, and we'll have a clearer picture of what that potentially is.

Lori Koch^ And on the pricing side, so we saw 4% total in Q1. It was 6% in W&P. We see that decelerating as we lap the 2022 benefits. And so in the second quarter, we expect overall about 1% price lift, really 2% in W&P and flat E&I.

Operator^ Our next question comes from the line of Jeff Sprague from Vertical Research Partners.

Jeffrey Sprague^ Ed, maybe a little color on how active you are on the buy side of M&A. The -- what the pipeline looks like -- I don't think you responded to the potential use of Delrin proceeds. When that happens, should we expect kind of more M&A like this or some combination of even additional repo plus M&A?

Edward Breen^ Yes, Jeff, our leaning right now is nothing else on the radar screen over the next year on the M&A side. We want to get the Spectrum deal done. Focus on that. By the way, the Laird acquisition we did the other year is going extremely well. So I think there's nothing that we're excited about that we see out there.

This one, by the way, we've had our eyes on for quite a period of time. As I think we said in our comments, they are actually a customer of ours. So -- this is really where we've been focused for the last kind of one year, 1.5 years with our thinking. If I had to say right now with any extra proceeds, I think we would lean towards additional share repurchase but remember to Lori's comments, it's still going to be about over the next year that we're still taking shares out of the market.

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

The existing ASR as we said, -- and then we'll -- as soon as we finish this one, we'll launch the new ASR for \$2 billion, and that will take us till back the end of the first quarter of 2024. So any excess cash we'll deal with at that point in time. But it depends on the environment, obviously, but if the environment were like it is now, where the multiple is for the company, my good as we lead towards share repurchase.

Jeffrey Sprague^ Could you speak to, I guess, for lack of a better term, kind of contingency planning. On the electronic stuff, as you said, I think you tried to triangulate between your own intel and third parties and what your customers are telling you. But it does look and feel like some of these customers are chasing a ball down the hill here on some of this stuff.

So there's things you can't control, but the question is and things you can control kind of cost actions that you might be taking or considering -- and I wonder if also a part of that answer, you could kind of speak to maybe the opportunity to unlock some additional cash from working capital as we work through this kind of cycling down in the electronics markets.

Edward Breen^ Yes. Just as an overall comment, though, Jeff. It's interesting. The semi -- you go back and study all the other downturn, remember, semi is a great industry by the way. It's going to go up the next couple of decades, but you always do hit these pockets of some destock and some softness. So -- but this actually for us, when you look at our sales rates, semi started coming down at the beginning of the fourth quarter. So we're two full quarters into the downturn.

Now we think the quarter we're in now is the bottom, just slightly down more from the first quarter. When you look at them, there are usually three to maximum four quarters of a destock. Remember, a lot of this is destock on top of some consumer softness, obviously, so we're pretty deep into it. It would appear.

Having said that, to your direct question, though, we've got a couple of other layers of actions we would take on the cost side to protect ourselves. And then back to the conversation we just had with Steve Tusa. Obviously, we're going to work this price cost thing real hard and haven't made that time in at this point in time. So that would be where the two levers would be.

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

Lori Koch^ Yes. I think on the inventory piece, too, so we did take action in the first quarter that was a headwind to E&I margins of about \$40 million to \$45 million to be able to better align inventory and production rates. And so we saw a headwind there. We'll continue to see that headwind in the second quarter as well as we try to get inventory more in line with where the demand signal is -- but to Ed's point, to just reiterate on the discretionary side, we are doing a fair amount of actions.

You can see on the face of our P&L that we took about 10% out of our total SARD that was really a function of the restructuring that we did in the tail end of 2022 as well as really tensioning backfills, and travel and expense, and we'll continue in that mode as we go into -- as we said in 2Q as well.

Operator^ Our next question comes from the line of Scott Davis from Melius Research.

Scott Davis^ Can you guys talk -- I know it's not giant, but it can't move the needle if you do it right, on Spectrum. What -- can you make it better? You commented just that it's more North American-based? Is there an opportunity to take it globally? Is there anything that you can do? Synergies look fairly modest, maybe you're just being conservative. But -- is there anything you can do with that asset to perhaps drive those returns up a little higher than the deal model?

Edward Breen^ Yes. Well, Scott, we didn't take into account any revenue synergies. So let me just talk to the cost piece of the [segment]. We only put in \$20 million of cost synergies, which, by the way, is only 3% to 4% of revenue, which is obviously low compared to -- you know what deals normally are on the synergy side.

So I think our net 13.2x is pretty conservative based on just that \$20 million. The real opportunity here is going to be on the growth side. Remember, our relationships at DuPont are namely -- and by the way, they're very deep relationships with the biopharma OEMs.

Spectrums are more with the medical device OEMs, but a lot of our technology actually goes through companies like Spectrum into that industry. So when we look at the ability for DuPont to move its technology and material science into the medical device market

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

with spectrum and (inaudible) the opposite of that Spectrum moving into the biopharma space.

And when we look at the joint opportunities we could have together we could drive some nice incremental growth there. And by the way, we've been talking to them and looking at this opportunity that I'm talking to for a very long time. So I think that's the big benefit.

Can we get some more cost synergies? Probably 10, but we haven't counted on it yet. But -- it will be the growth that this business has been growing, as you can see in our charts kind of right around 10% over the last four years. It's going to actually grow faster this year. They've got a couple of big new wins from OEM customers. And then we can broaden it out a little bit more globally because of our footprint on the Liveo side. But remember, a lot of the medical device players are U.S.-based companies that sell globally.

The other opportunity, Scott, the other big one we have is we have a path to get the margins of Spectrum up about 300 basis points. They -- very recently, I say, in the last year, put in a fair amount of new production capacity that's getting filled up because just the growth rate, Davis, you think about four years in a row of 10%.

So they have a fair amount that they're just completing on the factory expansion side. And as we fill up those assets and get them utilized will drive the margins up another 300 basis points. So that would back to me, would even be a bigger lever than the cost one, to be more of that margin expansion and then the revenue opportunity.

Scott Davis^ Okay. Interesting. And then just as a quick follow-on. The price comments that you just made, Lori, the sequential kind of drop down. Is that mathematically, is that more just that we're getting to the tougher comps on when you jacked prices up a year ago? Or is there -- okay. So there's no sequential weakness?

Lori Koch^ There's no sequential price declines of any magnitude baked in it's more just lapping. Last year, the bulk of the raise was in like February, March time frame. So...

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

Operator^ Our next question comes from the line of Christopher Parkinson from Mizuho.

Christopher Parkinson^ Thank you so much. Your performance in WP specifically on the water and the safety side has been pretty solid. -- depending on, obviously, where the macro takes us, which is natural out of your control, can you speak to the potential resiliency of those two businesses in terms of your expectations can you speak to the potential resiliency of those two businesses in terms of your expectations for the second half embedded in guidance?

Lori Koch^ Yes. So we still expect continued strength in water. So we had a nice organic growth in the first quarter on both a price and volume basis, and we expect that to continue as we head into the rest of the year. There's a lot of secular trends favoring our water portfolio right now.

And on the safety side, we're seeing strength as well in most areas, especially what we highlighted with respect to the Spectrum acquisition on our health care portfolio. So we've got about a \$500 million medical packaging business in tie back that's performing very nicely. So we have secular trends continuing throughout the rest of 2023.

One other area, too, that we can highlight of growth within the safety portfolio is the EV piece. So there's a nice application for Nomex paper within the e-motor that we're seeing nice growth in the first quarter, and we look for that to continue as well.

Christopher Parkinson^ That's very helpful. And just given the results on the margin front, Lori, for the first quarter, can you just give us a real quick update on your expectation for the intermediate to long-term outlook to 27%, 28%. Is that still roughly in line with your expectations in terms of your progression back to those levels?

Lori Koch^ Yes. I mean that's still our expectation with three big tailwinds between now and then. One is obviously the volume recover in E&I and getting those margins back into the low 30s. So we dipped in Q1. That was really a reflection of the volume and the actions we took to align production with demand. So that \$40 million to \$45 million created a headwind in the first quarter. So that is not permanent that will resolve itself.

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

Another tailwind is the price cost piece. So as we can see a potential future benefit there that will be margin accretive for us. And so those are the two biggest levers. And then obviously, the final piece is the mix component. So as you get E&I back on its growth trajectory, obviously, is the highest margin piece of our portfolio. So there's a favorable mix lift there as that market starts to recover.

Operator^ Our next question comes from the line of Mike Leithead from Barclays.

Michael Leithead^ First question, just on Spectrum. Apologies if I missed this, but in the materials, but is it possible to provide the 2022 revenue and EBITDA for the business?

Lori Koch^ Yes. So 2022 revenue is about \$450 million and EBITDA was about \$95 million.

Michael Leithead^ Great. And then secondly, can you just talk about the lower leverage target now -- about kind of 2.0 instead of 2.75. Is this just more conservatism in the current rate environment? Or just kind of help frame the pivot there.

Edward Breen^ Yes. It's exactly what you said. It's more a higher interest rate environment we're in. And I think it's just prudent to set there. By way, not the number one reason, but another reason is the premier multi-industrial companies are all, if you look at it kind of centered around a 2x leverage we were kind of targeted up at that 2.75.

So we think that this environment, interest rate environment, it's just a prudent place to be -- and so that's where we'll end the year about there, maybe actually a little slightly below 2x, depending on the proceeds that we get. And then we always have -- we preserve our strategic flexibility there, but that's kind of where we'd like to target ourselves moving forward. But really, the interest rate environment is the key reason.

Operator^ Our next question comes from the line of Aleksey Yefremov from KeyBanc.

Aleksey Yefremov^ I wanted to follow up on your 300 basis point margin expansion opportunity for Spectrum to clarify -- is this opportunity in your high single-digit ROIC number? Or it could push the number higher?

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

Edward Breen^ No, it's in there. We have a -- I mean just the growth rates they're on right now, if you look at it, they're going to be -- I won't get into specific knowledge that there'll be north of 10% growth this year.

So just adding that leverage into the system really moves the needle for us, especially when they built new capacity in place, and you're sitting there with it, you're hiring people on -- you're just kind of going through that digestion period as you're ramping up. So as we said, their revenues this year, Lori just mentioned 2022 to the revenues this year will be like \$500 million. So nice growth trajectory, and you just play those numbers through the system, that's where you get to.

Lori Koch^ And even if you back into the numbers that I had mentioned for 2022, that's about a 21% EBITDA margin. 2023 is expected to be 22%, so already 100 basis points of improvement. And they had a really nice first quarter ahead of their management plan actually. So they're on a very nice trajectory to achieve that average \$110 million of EBITDA in 2023.

Aleksey Yefremov^ And as a follow-up, in semis and interconnect clearly, it's a challenging market. Can you discuss your outgrowth? Are you continuing to gain content in these markets this year?

Lori Koch^ Yes, we would expect to see that, and we actually are seeing some share gains in the Litho in the packaging space still underneath the numbers that we're reporting. So what is clouding our performance versus the MSI is the destock piece. So the destock is pretty significant. That's going on in the first half, it would be another headwind on top of the MSI numbers that we have presented in the deck. And so that's what's clouding the story a little bit, but we still expect that content and exposure to advanced nodes to be able to give us outperformance in total.

Aleksey Yefremov^ Our next question comes from the line of Vincent Andrews from Morgan Stanley.

Vincent Andrews^ Ed, point taken on the sort of historical electronic cycle, the three- to four-quarter downturn, just curious if there's any sensitivity to that -- and what I mean

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

by that is -- and you're looking for the recovery in the third quarter. If for some reason, it doesn't come in the third quarter, can it still come in the fourth quarter? Or is there some seasonal reason why it might get kicked into the first quarter, if that were to play out?

Edward Breen^ No, there's no seasonal reason, Vincent. It's hard to tell exactly what month it is in there. But we've modeled all the other downturns. And remember, this downturn is pretty significant now. The 13% down is correct. You're hitting it pretty quickly on the destocking. And then by the way, there's one other factor here to kind of pushed it out a lot a little bit.

One of the very large semiconductor players kept running hard on their fab utilization through the first quarter, and that's public knowledge. I'm not going to mention the name, but one of the big players. So that is creating also the fact that they got to take their utilization down pretty rapidly here. And I think they just talked publicly about that a week or so ago. So that was one of the other reasons that just kind of pushed it out a little and they got to go through a destock also.

Vincent Andrews^ And can I just ask on Spectrum. I don't know if you mentioned this before, I didn't see it. But what polymers and materials are critical to their products and are there any particular folks that they tend to compete against?

Lori Koch^ Yes. So they compete against TE, Nordson and Integer are some of their larger competitors. As far as on the input side, they are -- they use their specialty polymers and design expertise to manufacture very high complexity materials for the large med device players.

And so that's as I had mentioned earlier, where we see a really nice sweet spot of being able to leverage the two portfolios. They've got really nice positions with the medical device guys, and we've got really nice positions with the biopharma guys. And so being able to bring our two portfolios leverage our expertise in material science across the broader portfolio is where we see the opportunity for us ahead.

Operator^ Next question comes from the line of Josh Spector from UBS.

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

Joshua Spector^ Just when I look at your E&I guidance for 2Q. I mean you're basically flat to slightly up sequentially on the sales line. I mean pretty clear how you're guiding towards semis and utilization rates come down, some interconnect is kind of a push as well. So is industrials doing better sequentially? And is there anything you note there that's maybe different than what you expected?

Lori Koch^ No, you had walked through the pieces. So industrial, we still expect continued strength overall within industrial. There's a little bit of a flip between interconnect and semi sequentially. So you'll start to see a little bit of the seasonal build that happens normally and interconnect primarily within the smartphone space.

And then we actually see a little bit of sequential deceleration in semi from Q1 to Q2 really a function of what Ed had mentioned earlier, on one of the larger customers. Overbuilding in Q1 and then pulling back in Q2. But net-net, there's not a material change in revenue for the total company or E&I from Q1 to Q2.

Joshua Spector^ Okay. I appreciate that. And I guess kind of following up on a prior question. Is this all -- this recovery in semis pushes out again another quarter, you had \$200 million sales, \$100 million EBITDA cut. You talked about some production kind of realignment, if this were to push forward again or push out again, would there be any difference in the decrement that we should expect, either due to price cost or anything else that would maybe be an additional lever you consider?

Lori Koch^ Yes. I mean we would -- so right now, we expect that, that headwind that we'll see in the first half of around \$90 million from pulling back production in E&I not being there in Q3 and Q4 in the second half. And so if this recovery extends into the fourth quarter, then you would expect that \$45 million to recur again in the third quarter.

The one caveat that we will make that we don't have baked into the guide to that could offset any decremental weakness if the recovery is pushed out, is that price cost piece. So we don't have anything material baked in that could become a tailwind to the second half based on what we see right now versus what we see right now.

Operator^ Our next question comes from the line of John Roberts from Credit Suisse.

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

John Roberts^ Health care alone now is going to be almost the same size as Shelter Solutions. So do you create a reportable health care segment and move the rest of safety into industrial? Or do you put Spectrum into a larger safety segment where healthcare will be about 40% of the safety segment?

Edward Breen^ Yes, John, it's something we've been looking at how to report it. It's interesting. Yes, healthcare will be 10% of the portfolio now. The water business, by the way, is developed into 10% of the portfolio. I think both really nice good secular end markets for us over the coming years at higher growth rates, obviously, both of those. So we'll take a look at that. We don't -- we'll probably look at it as we enter 2024 to see if we do anything, but no decision on that yet.

John Roberts^ Okay. And then on the delay in electronics, do you have any long lead time orders that actually show an inflection in demand yet?

Edward Breen^ No, because it's a short cycle business. So you can't really -- we'll have a little bit of lift as Lori said in the ICS business. And that's typical for us. As you said, you're going into the holiday season later in the year, so we start our shipments. And you can see one of our charts. Just the smartphone piece of alone picks up in third, fourth quarter there. So we begin shipments there. But past that, it's first cycle business, and we'll see it and we'll ship it pretty quick.

Operator^ Our next question comes from the line of Steve Byrne from BOA.

Stephen Byrne^ Yes, I just wanted to ask about your water treatment growth. Would you say that it's being driven more by the treatment of water for consumption or for wastewater discharge. And are you seeing any increased demand for both of those buckets due to foreignated compounds, either from EPA drinking water standards that are underway or EPA scrutiny on any company that's using a (inaudible) material?

Lori Koch^ No. I mean, so the growth we have seen would be more on the industrial side. The business is about 70% behavior towards industrial wastewater treatment. So that's what's driving the growth. There's nothing material that we're seeing with respect to any groundwater remediation that's coming out from the [EPA].

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

Edward Breen^ 70% of that business is recurring. We're replacing membranes and all at these industrial sites. And -- it's just a secular trend that should continue because including DuPont, we're all working on that for our ESG targets. And it's besides greenhouse gas emissions, it's the other big one.

Stephen Byrne^ And then one on shelter. Clearly, it's going through a cyclical downturn, but just curious about your longer-term view on Shelter Solutions. Is it likely to remain a core business for you?

Edward Breen^ No, it's a core business for us. I remember a very key component of that is our Tyvek franchise, which is a very nice margin business for us against all of the end markets that we service with Tyvek including the construction market. Obviously, Lori mentioned a really nice market for that is medical packaging. So it's definitely part of the portfolio.

Operator^ Our next question comes from the line of John McNulty from BMO Capital.

John McNulty^ So on the topic of raw materials, I know what you said is in the guide. I guess I'm curious, in terms of the raw material basket that you're buying today, acknowledging it takes some time to work through the P&L. Can you help us to understand how much that might be down from the peak and how we should be thinking about that?

Lori Koch^ Yes. So we saw around the \$800 million of escalation last year. It was about 60% raws and the rest, roughly between logistics and energy. We are seeing deceleration on the logistics and the energy side. So obviously, you can look at European and U.S. natural gas and see there's been a sizable pullback there and the ocean freight rates we're seeing tailwinds as well.

And so that's where we're seeing most of the deceleration. I wouldn't say we've seen a material amount thus far on the raw material side either on both the bulk buy or on the tail spend. So that's the upside as we head into the rest of the year is when we start to see an inflection in the raw material buy.

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

John McNulty^ Okay. So you haven't -- actually, you're not buying them lower now. So that's to come, and then it still has to work through the P&L, is that right?

Lori Koch^ Yes, yes.

Edward Breen^ I think, John, it's important to note that there are individual raw materials where we would be buying at lower prices, but there are others that have maintained an inflation curve.

And there are a lot of things that we buy are very supply driven in terms of the dynamic, and it could take quite a while to kind of unlock any kind of relief there. Even if you take a really basic benchmark price and suggest that, that could be down already today, so there are puts and takes within the portfolio. But I think the punchline here is that there's well less than \$100 million of net benefit in the model that we have today.

And that's inclusive of some of the savings that Lori reference from logistics and energy, but netting out as we go through the year later, some potential give back that could be necessary. So there really isn't that much in there. And yes, I suppose that could present an opportunity as we look forward, but we haven't seen a lot of benefit come through today.

John McNulty^ Got it. Okay. Fair enough. And then just one question on the acquisition. So the growth rate from 2019 to 2023 of 12% is a pretty chunky number. But at the same time, if memory recalls, like during the COVID period, medical device demand was actually pretty soft.

You had -- didn't have a whole lot of access to surgical suite. So is that 12% understated in your mind? Or is that kind of a fair run rate in this just -- based on the specific products they make, maybe it didn't have that pressure that maybe some others in medical devices did. How should we be thinking about that?

Lori Koch^ Yes. I mean it wouldn't have had the same magnitude of pressure as some of the other providers into the elective surgery. So it's selling into the nonelective types, so kind of more the essential surgery. So want have seen that as significant of a COVID

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

headwind. So I would say the 12% CAGR that we saw from '19 to '23 would be too materially awesome where we see it going forward.

We see it a little bit decelerating to the high single-digit range, but still a really nice growth for us. And then, obviously, really nice growth in 2023 on the back of already underlying strong volume as well as they had some sizable new customer wins that are in the process of ramping and really get to a nice clip as we head into the back half of 2020 as well.

Operator^ Our next question comes from the line of David Begleiter from Deutsche Bank.

David Begleiter^ Ed, do you have an update on PFAS and the MDL ahead of the upcoming trial in Florida?

Edward Breen^ Yes. So the trial comes up in about a month out and now, David. And I'll just say, we've been talking pretty regularly with the plaintiff. As I've mentioned last quarter, that the judge did a point in mediator who, by the way, is very actively involved with these regular conversations we're having. So we're feeling positive, but I'll leave it at that right now.

David Begleiter^ And can you provide a little more color on the weakness you're seeing in North American construction, [resi versus non-resi] and any destocking that's still ongoing in that space.

Lori Koch^ Yes. We saw pretty similar volume declines across all 3 end markets. So do it yourself residential and commercial markets. A reminder, just on the exposure in commercial, it's more so on like the healthcare and education side versus large commercial construction in downtown cities.

And so we saw a similar performance from a volume deceleration in all three. We don't have a material pickup in 2023 plan for those markets. So we'll see how they continue to perform, but we don't see an inflection like we do in electronics and construction in general.

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

Operator^ Our next question comes from the line of Arun Viswanathan from RBC Capital Markets.

Arun Viswanathan^ So just looking at the full year guidance of \$3.05 billion of EBITDA at the midpoint and your Q2 of \$7.15, that would imply that your second half is around \$1.62 billion and your first half is around \$1.43 billion. So that \$190 million uplift or \$200 million almost uplift when you look at first half to second half, is that mainly the comps getting easier on the volume side for E&I. Are there any other special items we should kind of consider when we think about that cadence.

Lori Koch^ Yes. I mean it's mostly within E&I that lift, and it's going to be more favored to Q4 versus Q3 as you look at the slides that we presented on both the smartphone and the semi MSI side. So -- most of it is that anticipated second half recovery. There is a little bit of seasonality that would play into a first half versus second half comp, but most of it is the electronics recovery. And as I had mentioned, a little bit more favorite to Q4 versus Q3.

Arun Viswanathan^ Okay. And just one quick one on M&A. So you guys have now reentered the market with the Spectrum acquisition. Would you say that the portfolio transformation is now kind of complete? And -- or are you still considering other opportunities within the five markets that you've been looking at?

Edward Breen^ You're never, I guess, complete, but I would summarize it, yes. We feel like we're complete for a period of time here. We like where we're at. This was the last piece we were looking at -- and so I don't see anything over the next, like, year, just to again state time period. I think we like where the portfolio is at. We just want to operationally run it well.

Operator^ Our final question comes from the line of Mike Sison from Wells Fargo.

Michael Sison^ In terms of spectrum, is there a pretty big runway in terms of other acquisitions there? You sort of exited plastics, you're back in the plastics, and I get it healthcare is so much better on market. But is this an opportunity to build a pretty big plastics health care unit over time?

DuPont Specialty Products USA, LLC

1Q 2023 Earnings

Edward Breen^ There's definitely more you could add to it. And again, we like it secularly, so that's why we've kind of doubled down in this area. But remember, we have a lot of opportunity between what we already had and what they had. So we really like it because of that. So yes, there's other opportunities down the road. But -- it's just like the layer do. We want to get this in. We want to get it synergized. We want to get it really humming with our business. So over the next year, that's what we'll be focused on.

Michael Sison^ Then just a quick follow-up, when I take a look at Slide 14. Thus inventory destocking end in 2Q? And even if the third quarter isn't that much of an improvement sequentially, E&I's results could improve if the destocking is sort of done?

Lori Koch^ Yes. We do see the destocking moderating in Q2, yes. So it peaked kind of in the 1Q, 2Q time frame and then we see it pulling off a bit in Q3, Q4.

Operator^ I would now like to turn the call over to Chris Mecray for closing remarks.

Christopher Mecray^ Yes. Thank you everyone, for joining our call. For your reference, a copy of our transcript will be posted on our website. This concludes the call. Thank you.

Thank you, ladies and gentlemen. This does conclude today's call. Thank you for your participation. You may now disconnect.