S&P Global
Market Intelligence

Dow Inc. NYSE:DOW

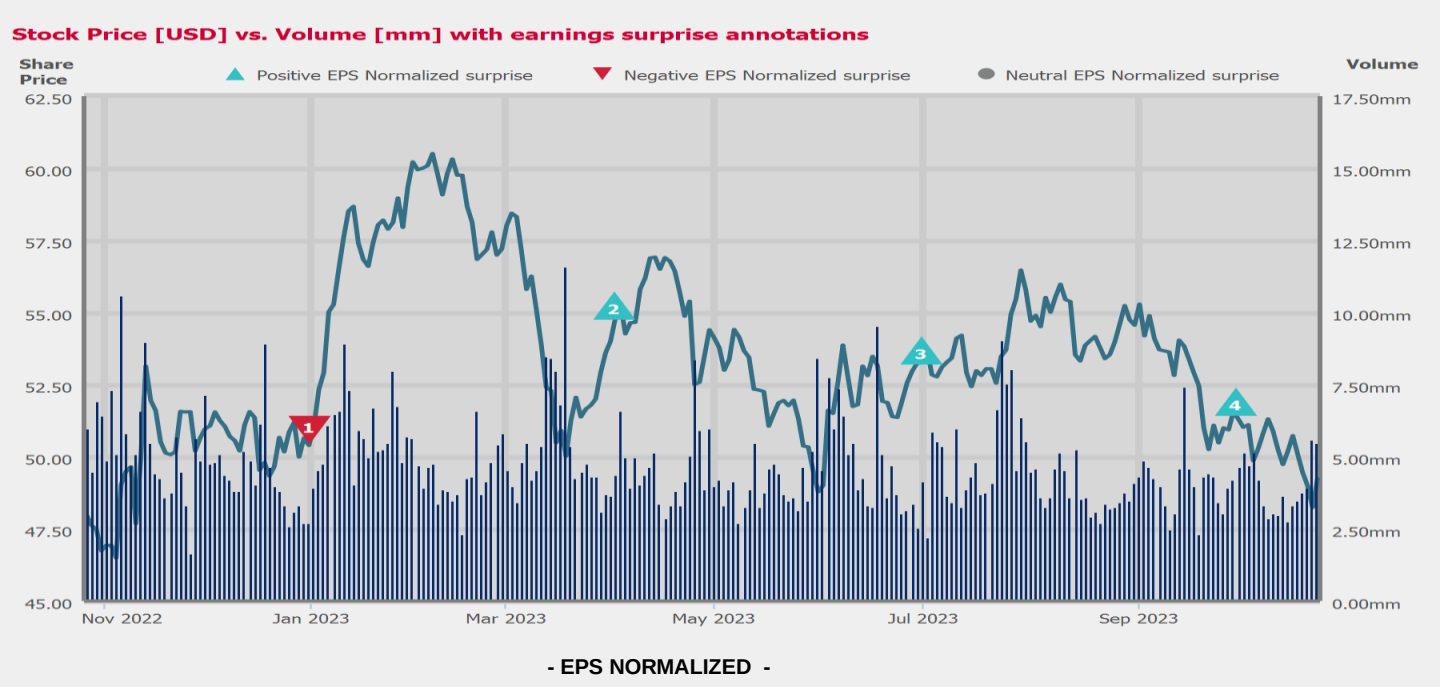
FQ3 2023 Earnings Call Transcripts

Tuesday, October 24, 2023 12:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2023-			-FQ4 2023-	-FY 2023-	-FY 2024-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.45	0.48	6.67	0.48	2.33	3.72
Revenue (mm)	10413.83	10730.00	3.04	10669.34	44356.77	46101.55

Currency: USD
Consensus as of Oct-24-2023 12:53 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2022	0.57	0.46	1 (19.30 %)
FQ1 2023	0.37	0.58	2 56.76 %
FQ2 2023	0.71	0.75	3 5.63 %
FQ3 2023	0.45	0.48	4 6.67 %

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved

Table of Contents

Call Participants 3
Presentation 4
Question and Answer 10

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved

Call Participants

EXECUTIVES

Howard I. Ungerleider
President & CFO

James R. Fitterling
Chair & CEO

Pankaj Gupta
Vice President of Investor Relations

ANALYSTS

Aleksey V. Yefremov
KeyBanc Capital Markets Inc., Research Division

Arun Shankar Viswanathan
RBC Capital Markets, Research Division

David L. Begleiter
Deutsche Bank AG, Research Division

Frank Joseph Mitsch
Fermium Research, LLC

Hassan Ijaz Ahmed
Alembic Global Advisors

Jeffrey John Zekauskas
JPMorgan Chase & Co, Research Division

John Patrick McNulty
BMO Capital Markets Equity Research

Joshua David Spector
UBS Investment Bank, Research Division

Kevin William McCarthy
Vertical Research Partners, LLC

Laurence Alexander
Jefferies LLC, Research Division

Michael James Leithead
Barclays Bank PLC, Research Division

Patrick David Cunningham
Citigroup Inc., Research Division

Patrick Duffy Fischer
Goldman Sachs Group, Inc., Research Division

Richard Garchitorena
Wells Fargo Securities, LLC, Research Division

Stephen V. Byrne
BofA Securities, Research Division

Vincent Stephen Andrews
Morgan Stanley, Research Division

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

Presentation

Operator

Greetings, and welcome to the Dow Third Quarter 2023 Earnings Conference Call.

[Operator Instructions] As a reminder, this conference is being recorded. I will now turn the call over to Dow Investor Relations Vice President, Pankaj Gupta. Mr. Gupta, you may begin.

Pankaj Gupta
Vice President of Investor Relations

Good morning. Thank you for joining today. The accompanying slides are provided through this webcast and posted on our website. I'm Pankaj Gupta, Dow Investor Relations Vice President, and joining me are Jim Fitterling, Dow's Chair and Chief Executive Officer; and Howard Ungerleider, President and Chief Financial Officer.

Please note our comments contain forward-looking statements and are subject to the related cautionary statements contained in the earnings news release and slides. Please refer to our public filings for further information about principal risks and uncertainties.

Unless otherwise specified, all financials, where applicable, exclude significant items. We will also refer to non-GAAP measures. A reconciliation of the most directly comparable GAAP financial measure and other associated disclosures are contained in the earnings news release and slides that are posted on our website.

On Slide 2, you will see the agenda of our call. Jim will review our third quarter results and operating segment performance. Howard will provide an update on our cost savings actions and financial position and share our outlook and modeling guidance. To close, Jim will outline how our long-term growth and sustainability road map continues to enable value creation as we navigate challenging short-term dynamics. Following that, we will take your questions.

Now let me turn the call over to Jim.

James R. Fitterling
Chair & CEO

Thank you, Pankaj. Beginning on Slide 3. For the third quarter, we continued to advance our long-term strategy while also taking action to reduce costs and maximize cash generation in the face of slow global macroeconomic activity and higher sequential feedstock costs. In particular, we continue to implement targeted actions to deliver $1 billion in cost savings in 2023 and delivered a sequential improvement to operating cash flow of more than $300 million.

Net sales were $10.7 billion, down 24% versus the year ago period reflecting declines in all operating segments due to slower global macroeconomic activity. Sales were down 6% sequentially as volume gains were more than offset by lower local prices. Volume decreased 6% year-over-year, mainly due to lower merchant hydrocarbons and energy sales. Volume was up 1% sequentially, led by gains in Industrial Intermediates & Infrastructure and Performance Materials & Coatings. Volume was up 3% sequentially, excluding merchant sales in Hydrocarbons & Energy with gains across all operating segments.

Local price decreased 18% year-over-year with declines in all operating segments and regions, primarily due to lower feedstock and energy costs. Sequentially, price was down 7%, primarily in Europe, the Middle East, Africa and India or

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

EMEAI.

Operating EBIT for the quarter was $626 million, down from $1.2 billion in the year ago period and $885 million in the prior quarter. Our consistent focus on cash flow generation and working capital management enabled team Dow to generate cash flow from operations of $1.7 billion, resulting in a cash flow conversion of 129% for the quarter and 103% on a trailing 12-month basis.

We continue to invest in our long-term strategic priorities while also returning $617 million to shareholders in the quarter through dividends and share repurchases. Year-to-date, we've returned nearly $2 billion to shareholders. Our cash flow generation continues to enable Dow to fully cover its capital allocation priorities. And our balance sheet remains the best it has been in 4 decades, supported by strong investment-grade credit ratings with no substantive long-term debt maturities due until 2027.

Now turning to our operating segment performance on Slide 4. In the Packaging & Specialty Plastics segment, operating EBIT was $476 million compared to $785 million in the year ago period. Local price declines were driven by lower polyethylene and olefin prices in all regions, primarily as a result of lower global energy costs. Volume declined as increased polyethylene demand across all regions was more than offset by lower volumes in merchant Hydrocarbons & Energy sales. Sequentially, operating EBIT decreased by $442 million, driven by lower integrated polyethylene margins, increased planned maintenance activity and lower licensing revenue.

Moving to the Industrial Intermediates & Infrastructure segment, operating EBIT was $21 million compared to $167 million in the year ago period. Results were driven by lower prices and demand in both businesses as well as reduced supply availability due to an unplanned event in Industrial Solutions at our Louisiana operations. Sequentially, operating EBIT was up $56 million driven by volume gains and lower costs, which were partly offset by the Louisiana event.

And in the Performance Materials & Coatings segment, operating EBIT was $179 million compared to $302 million in the year ago period, driven by local price declines in both businesses. Volume was down as gains in commercial building and construction end markets were more than offset by lower demand for personal care and coatings applications in residential construction. Sequentially, operating EBIT increased $113 million, driven by higher operating rates and cost savings.

Next, I'll turn it over to Howard to review our outlook and actions on Slide 5.

Howard I. Ungerleider
President & CFO

Thank you, Jim. We expect the challenging macroeconomic dynamics to continue through the fourth quarter, including sluggish industrial activity. Global manufacturing PMI has declined for the 13th consecutive month in September. It also includes weak demand in Europe and a slower-than-expected recovery in China. While inflation continues to moderate, it remains at elevated levels, resulting in a continuation of a tighter monetary policy.

In the U.S., we're seeing some mixed indicators as September manufacturing PMI improved to 49.8. Retail sales growth remains positive, while consumer confidence has declined for the last 2 months. In Europe, industrial and consumer demand remains weak despite sharply lower inflation. PMI has contracted for 15 consecutive months through September, and consumer confidence remains low. With that said, automotive demand is showing signs of resilience.

In China, while manufacturing PMI remained in expansionary territory in September, China exports fell for the fifth straight month. Automotive sales and production are a bright spot, rising both sequentially and over the prior year in September. Around the rest of the world, India's manufacturing PMI remains expansionary, while in Mexico, industrial production rose for more than 20 months in August. However, ASEAN manufacturing PMI contracted for the first time in

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

2 years in September. Against this macroeconomic backdrop, we will continue to take a disciplined approach to managing our operations while leveraging our diverse global portfolio and our cost-advantaged assets.

Turning to Slide 6. Our commitment to financial and operational discipline continues to be reflected in the proactive actions we are implementing to lower our costs and maximize cash flow. We achieved $700 million in cost savings year-to-date and remain on track to deliver our $1 billion commitment in 2023. In addition, we are further enhancing our financial flexibility as we execute on our capital allocation priorities across the economic cycle. For example, we're implementing continued actions to improve our working capital to maximize cash flow. As a result, our cash conversion cycle has improved by approximately 8 days from pre-COVID levels, and we have unlocked approximately $600 million of cash from working capital in the third quarter.

Since Spin, we have taken actions to strengthen our balance sheet, ensuring ample liquidity while reducing net debt and pension liabilities, and we are continuing to take actions to further derisk our pension plans. Dow pension-funded status has greatly improved, driven primarily by changes in the discount rate and the $1 billion voluntary contribution we made in 2021. Our decision to freeze the U.S. deferred benefit plans at year-end '23 further reduced the pension liability.

We expect to pursue additional derisking opportunities for our pension plans in the fourth quarter, including annuitization and risk transfer of some pension liabilities. If these transactions are executed, we expect to record a onetime noncash and nonoperating settlement charge in the range of $500 million to $1 billion in the fourth quarter of 2023. All in, our targeted actions have given us the ability to continue investing in growth while delivering more than 80% of operating income back to our shareholders, well above our 65% target.

Turning to our outlook for the fourth quarter on Slide 7. In the Packaging & Specialty Plastics segment, industry data shows a continued decline in U.S. Gulf Coast inventory levels, driven by resilient domestic demand and export market strength. Higher polyethylene prices and elevated oil to gas spreads continue to favor our cost advantaged footprint and are expected to generate $100 million tailwind in the quarter. Additionally, we expect a $25 million tailwind as we complete planned maintenance activity at our cracker in St. Charles, Louisiana. We also expect a $50 million headwind to equity earnings due to a planned turnaround at our joint venture in Thailand.

In the Industrial Intermediates & Infrastructure segment, we expect seasonal demand increases in deicing fluid to offset seasonal volume declines in building and construction end markets. Additionally, we expect a headwind of $25 million due to elevated energy and feedstock costs, particularly in Europe impacting our Polyurethanes and our Construction Chemicals businesses.

In the Performance Materials & Coatings segment, we expect the current macroeconomic conditions to limit consumer discretionary spending in nonservice areas. We also expect margin pressure to continue in upstream siloxanes from competitive supply additions, which will result in a $25 million headwind. Additionally, the seasonal decline in building and construction demand is expected to contribute an approximately $50 million headwind in the quarter.

All in, we expect fourth quarter earnings to be in line with the third quarter.

Next, I'll turn it back to Jim.

James R. Fitterling
Chair & CEO

Thank you, Howard. Moving to Slide 8. We continue to make progress on both our Decarbonize & Grow and Transform the Waste strategies, which by 2030 position us to deliver more than $3 billion in underlying earnings, while reducing greenhouse gas emissions by 5 million metric tons and commercializing 3 million metric tons of circular and renewable solutions annually.

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

Starting with Decarbonize & Grow. In September, we achieved startup of a new MDI distillation and pre-polymers facility at our manufacturing site in Freeport, Texas. This new facility replaces Dow's existing capacity in La Porte, Texas and expands supply by an additional 30% at the site to support high-value demand growth in polyurethane systems while also reducing our greenhouse gas emissions by more than 45% compared to the La Porte asset.

Our Path2Zero project in Alberta remains on track. We expect the final investment decision by year-end, pending completion of our subsidies and incentives with the Canadian federal government. Additionally, we recently announced a solar power purchase agreement with MSU Green Energy in Bahía Blanca, Argentina, which will drive the site to source 75% of its electric power supply from renewable sources by 2025.

In Terneuzen, the Dutch government informed us that they need more time for adjustments to certain rules and regulations critical to enabling carbon capture and clean hydrogen. The public-private partnership is a crucial element of our Path2Zero effort at Terneuzen.

Dow investment and timing will depend on the level of collaboration, subsidies available and a clear regulatory framework. We will continue to engage with the Dutch government to advance these efforts. And we continue to advance our Transform the Waste strategy. In the third quarter, we successfully leveraged our U.S. Gulf Coast assets for bio and circular feedstock processing, accomplishing a key milestone to utilize existing assets to quickly scale production of recycled and bio-based products. This was a direct enabler to the commercial launch of our sustainable SURLYN Ionomers, which support high-end applications like perfume and cosmetics packaging.

In addition, Valoregen in France and Mura Technology in the U.K. remain on track to start up their respective mechanical and advanced recycling facilities by year-end. All in, we expect that our initiatives to develop a circular ecosystem will generate more than $500 million of incremental run rate EBITDA by 2030. Altogether, we remain confident in our long-term growth with continued focus on a more sustainable future while maintaining a disciplined and balanced approach to capital allocation.

Next, an update on our Path2Zero project in Fort Saskatchewan, Alberta, on Slide 9. The project will enable Dow to capture sustainable growth opportunities while also delivering on our 2030 greenhouse gas emissions reduction targets and advancing our long-term goal of carbon neutrality by 2050. Construction is planned to begin next year with Phase 1 start-up expected in 2027 and Phase 2 expected in 2029. We expect to spend an average of $1 billion of CapEx annually on this key growth project with total enterprise CapEx ramping above depreciation and amortization levels in the 2025 to 2027 time period as we implement the first phase.

We remain fully committed to keeping our CapEx within D&A across the economic cycle and expect to return to those levels as we complete the project. We are expecting bottom line returns on our Alberta Path2Zero project equal to or better than our Texas-9 investment.

Turning to Slide 10. We are partnering with brand owners and leaders across the value chain to strategically enable and scale waste management transformation through mechanical recycling, advanced recycling and bio-based solutions. This allows us to lead the way to a more circular economy and become a major off-taker of circular feedstock while also minimizing capital outlay for Dow. Robust industry demand for these solutions is expected to outpace supply through the end of this decade. We expect Dow's differentiated innovation portfolio to create opportunities that will result in more than $500 million in incremental earnings by 2030.

Continuing on Slide 11. Our actions to commercialize 3 million metric tons of circular and renewable solutions annually are driven by a robust pipeline of strategic partnerships. These collaborations enable us to deliver innovative solutions to meet increasing brand owner demand. For example, our partnership with P&G China to enable recyclability of air capsule e-commerce packaging delivers an effective and efficient way to protect products while avoiding excessive

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

packaging.

Dow's SPECFLEX CIR foam system uses recycled waste from the automotive industry to produce circular polyurethane-based materials matching the performance of existing products as seen in the recent launch of the Mercedes-Benz E-Class. And our collaboration with LVMH Beauty is pioneering circular feedstocks for sustainable packaging in the cosmetics industry. This has enabled Dow's first sales of bio-based and advanced recycling polymers in the third quarter.

Closing on Slide 12, since Spin, we have executed against our strategic priorities and consistently demonstrated financial and operational discipline. As a result of our proactive actions, our underlying earnings and cash flow generations are well above pre-COVID levels, and our balance sheet is the strongest it's ever been, especially in this part of the cycle.

Our global scale and leading positions across key value chains paired with our cost-advantaged assets and industry-leading feedstock flexibility positioned Dow well to respond quickly to evolving market trends and capture above GDP demand growth across our attractive market verticals. These distinct competitive advantages will continue to enable us to execute our capital allocation priorities while also driving long-term value growth for our shareholders.

Finally, before we move to Q&A, I would like to speak to the announcement this morning that Howard has elected to retire from the company following 33 years of dedicated service. I want to personally thank Howard for his significant contributions to Dow over the last 3 decades. He's been an incredible business and strategic partner, created a financial and leadership team that guided our company through numerous challenges and accomplishments and most importantly, he's been a tremendous colleague and friend.

In addition to recognizing and thanking Howard, we are pleased to share that the Board has elected Jeff Tate to the role of the CFO effective November 1, 2023. As we thank Howard for his years of service, and there will be time to honor and recognize him for that. We're excited to welcome Jeff back to Dow. Many of you will remember, Jeff, who also previously led Dow's Investor Relations team. He returns to us following a 4-year stint as the CFO of Leggett & Platt. Prior to that, Jeff had 27 years with Dow in various finance roles, including VP of Finance for Packaging & Specialty Plastics and was our lead auditor.

Jeff is joining us here today, and we'll look forward to him joining our next earnings call in his formal role. In the meantime, more to follow as we all work together through this transition. As I noted, this change will become effective November 1, and Howard will stay on to support the handover through early January when he will formally retire from Dow.

Howard, I'll now turn the mic over to you for a few comments.

Howard I. Ungerleider
President & CFO

Thank you, Jim. I really appreciate those comments and thoughts. And I would like to share a few personal thoughts of my own. I've had the good fortune of being Dow's CFO for nearly a decade and President for the last 5, and they have truly been the best roles of my career. Jim, it was an absolute honor to serve with you and the rest of the leadership team. We have accomplished a great deal together, and I am extremely proud of not only what we have delivered for all of our stakeholders, but also how we have done it.

Dow is a great company. Our Decarbonize & Grow strategy is absolutely the right path forward, and our balance sheet, as you've said, is in the best shape it's been in 4 decades and that's as a direct result of our disciplined and balanced capital allocation approach. The Dow culture and the incredibly smart hard-working people, who embrace it each and

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

every day all over the world, are absolutely second to none.

After more than 33 years at Dow, this is the right moment for me to move on to my next chapter, and I could not be more excited to hand the finance reins over to Jeff Tate. Jeff and I have known each other for more than 25 years. We have worked alongside each other, and I consider him to be a great professional as well as a friend, and he is absolutely the right leader to help take Dow to the next level of performance together with Jim and the leadership team. And while I'm retiring from Dow, I am not heading to the beach or the golf course, I'm excited about my next chapter and the opportunities that lie ahead.

With that said, I bleed Dow, Red Pantone 185 for those of you checking the color wheel, and I will always be a supporter, a fan and a friend of Team Dow.

With that, I'll turn it to Pankaj to open the Q&A.

Pankaj Gupta
Vice President of Investor Relations

Thank you, Howard. Now let's move on to your questions. I would like to remind you that our forward-looking statements apply to both our prepared remarks and the following Q&A. Operator, please provide the Q&A instructions.

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Hassan Ahmed of Alembic Global.

Hassan Ijaz Ahmed
Alembic Global Advisors

Howard, sorry to see you leave. But obviously, wishing you the best wishes for your future sort of endeavors. In terms of my question, you guys obviously talked about $100 million worth of tailwind -- EBIT tailwind on the P&SP side of things. And you cited expanding oil to natural gas ratios. I just want to sort of delve a little deeper into that. What sort of pricing regime for polyethylene are you baking into that? What sort of pricing regime for ethane are you baking into that?

James R. Fitterling
Chair & CEO

Yes. As we mentioned, we guided for the fourth quarter, in line with the third quarter. It will obviously be a different mix. I expect Packaging & Specialty Plastics to be up. They had obviously, the weight of the St. Charles turnaround on them in the third quarter. And they also had the fact that we were out of the merchant ethylene market. When you look at the core underlying volumes, polyethylene volumes were up in all regions year-over-year, and they were up sequentially 3% in Asia, Latin America and EMEAI. So those are good signs.

Things that you should take into account is we obviously don't have the St. Charles turnaround in the fourth quarter. We do have a little bit of a headwind from the Thailand turnaround. We're expecting -- we saw prices up in September. I'm expecting Q4 integrated margins to be up about $0.02 in P&SP, and that's mostly on the back of pricing. The outlook right now is for ethane to be flat. It could be slightly better than that. But I think for right now, we've got it in as flat.

We've got inventories down for 3 consecutive quarters in the United States in plastics, and U.S. Gulf Coast exports were up 7% versus the previous quarter, and the previous quarter was up about 3.5% versus a quarter before. So I think all in all, I would expect volumes to be good, we'll be back in the merchant ethylene market for some extent. Pro-nap spread in Europe is positive at about $120 a ton, and our assets are the lowest cost in Europe. And I think when you factor all that in, the guide for the fourth quarter is heavily on the back of P&SP delivery.

Operator

Your next question comes from the line of David Begleiter of Deutsche Bank.

David L. Begleiter
Deutsche Bank AG, Research Division

Again, Howard has been an absolute pleasure and best of luck. Jim, Howard, second half EBITDA is running around $5 billion annualized, maybe a little bit more than that. How do you grow -- if the macro stays the same as it is today, how does EBITDA increase materially next year?

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

James R. Fitterling
Chair & CEO

David, good question. Obviously, we're about 12 to 15 months into this economic slowdown, and typically, when we see a slowdown, like we saw starting mid last year, about 12 to 18 months, we start to see things turn to a positive direction. Inflation is the thing that's weighing on people's minds right now. We're continuing to invest in our organic growth, while at the same time, manage our costs. We've got investments in all 3 segments, both incremental investments as well as new plant investments. They will start up through this year. This year, we expect those and an underlying $400 million to $500 million of EBITDA mid-cycle run rate to the bottom line.

On top of that, we're continuing to see strength in areas like telecommunications and data centers, automotive, even in the face of the strikes is holding up relatively well. And our view is that it should bounce back once the agreements are made between the UAW and the auto workers. Our cost positions are good. And so I think that we're positioned that once the weight of inflation starts to moderate that things start to turn back in a positive direction. And our view is that we could be in a better shape for 2024. Additionally, we've taken $1 billion of cost out since Spin.

So if you think about where we're operating today, we're able to meet all of our capital allocation requirements, be free cash flow before financing breakeven, you saw a $300 million improvement this quarter in operating cash flows, and we were still able to opportunistically buy back some shares in the third quarter. So we've done our best to really manage to be able to get through the bottom of the cycle, and it's the right time for us to continue to make our organic investments to get the benefit in the next up cycle.

Howard I. Ungerleider
President & CFO

And David, this is Howard. Look, thanks for your comments, Hassan, same to you as well. The only other thing I would add, David, to your question is don't forget about cash, right? So I mean Jim laid out our EBITDA improvements, but we have equally been doing cash flow improvements really every year since Spin, if you think about it. So the last 5 or 6 years, every year, we've been able to increase cash flow. We'll see if we can do that this year. But a couple of things. We are able to cover all of our capital allocation priorities inclusive of continuing to buy stock back even at these low EBITDA levels. And every year, we've had between $1 billion and $3 billion of what we like to call unique to Dow cash levers. And I would expect that to continue into next year.

When you think about the $500 million plus judgment that we will likely get finally from Nova on the last tranche, continued structural working capital improvements, additional cash that we can pursue out of our joint ventures, and other projects that we currently have in the pipeline. So you should expect at least another $1 billion of unique to Dow cash flow levers coming out of next year on top of the organic investments that Jim talked about.

Operator

Your next question comes from the line of Vincent Andrews of Morgan Stanley.

Vincent Stephen Andrews
Morgan Stanley, Research Division

And let me also echo the prior remarks and congratulations to you, Howard. Very exciting for you. If I could ask just looking at Slide 9 on the CapEx, I just want to make sure I understand -- I mean, obviously, we know where '23 is, it looks like '24 is going to go to that D&A line. And then that '25 to '27, it looks like there's quite a -- there's sort of a zone there. Could you speak to a little bit of maybe a range that you could give us to make sure we have that right in our models and sort of what would define it at the lower end or the upper end of the range? Because I see you do have Alberta at about $1 billion a year, but is it maybe going to be a bit chunkier in some of those years? Or just how should we be thinking about the cadence and the range of CapEx during that period of time?

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

James R. Fitterling
Chair & CEO

Vince, yes, as we get into the Alberta project, it will be '25 to '27 that is the peak construction of that project. Phase 1 starts up in '27. You would expect that we would get to somewhere in the 3 to 3.5 range for CapEx during that '25 to '27 time frame. That's very similar to where we were during the Gulfstream project, we peaked at kind of that same level. Obviously, we're in a little bit different spot than we were at Gulfstream. We're just doing Alberta Path2Zero, but we're also funding growth in Industrial Solutions, which is high-value growth and downstream incremental growth in our Consumer Solutions business. So I think it will be very manageable. And as we get closer to those dates, we'll try to titrate more specifically so that you have some year-over-year expectations on what CapEx is going to look like.

Operator

Your next question comes from the line of Jeff Zekauskas of JPMorgan.

Jeffrey John Zekauskas
JPMorgan Chase & Co, Research Division

In your $1 billion cost-cutting program, how much of that comes out of SG&A and R&D? And in your slides, you say that your share count in the fourth quarter is 710 million and in the third quarter, it was 707.5 million. Are you rounding? Or is the share count going up?

James R. Fitterling
Chair & CEO

Yes. Jeff, on the cost, about half of the costs come out of our structural operating cost model, which would include obviously, making sure that we're controlling SG&A during this time period. It also includes things like contract labor and what we've been doing there to reduced headcount. On our operating cost side, it's things like purchase raw material and logistics costs, utilities costs being down, our turnaround spend, which is down about $300 million. And while SG&A is down both in cost and as a percent of sales, we're obviously still continuing to invest in research as we go forward.

Howard, do you want to touch on the share count?

Howard I. Ungerleider
President & CFO

Yes, Jeff, I was smiling. So yes, it is just purely rounding. The share count actually went down about 2 million shares quarter-on-quarter. Year-on-year, it went down 11 million shares. And I would say 2 things. We are going to continue as long as we have the free cash flow before financing to continue to buy at dilution, and we will also continue to be opportunistic when we have cash available, and/or we believe it's a great investment. And so we're continuing to buy shares on a regular basis, and you should expect that to continue in the fourth quarter.

Operator

Your next question comes from the line of Frank Mitsch from Fermium.

Frank Joseph Mitsch
Fermium Research, LLC

Howard, congrats. Thanks for all the help and friendship over the years and certainly looking forward to your next chapter. This -- the third quarter was the third quarter in a row of sequentially higher volumes. I was wondering what your expectations are as we finish the year and into 2024? Is this a trend that we can continue to see?

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

James R. Fitterling
Chair & CEO

Yes. Frank, I think on volumes in P&SP, I would still be positive around what we see on polyethylene demand in all the regions, also mentioned telecommunications, and the fact that we've seen a lot of demand in infrastructure, data centers, et cetera. And so the wire and cable business is one which is very positive. I would say Industrial Solutions will be limited a bit in fourth quarter because of the outage in Plaquemine. But the demand -- other than that, the demand is there once that plant is back up and running.

In PM&C, for Consumer Solutions for coatings, you're going to see fourth quarter slowdown, which we typically see with architectural coatings. But other than that, the silicones downstream demand has been holding up pretty well. This is the first quarter that we've seen core underlying volumes in all 3 segments better year-over-year. I mean, if you take away merchant ethylene sales in the third quarter because we were -- we had the cracker down in St. Charles, the underlying downstream demand for all 3 segments was better in the third quarter than it was last year. That's the first time we can say that in several years.

So I'm optimistic with that. We can see the automotive strike resolved. I think we'll see a tick up in that demand as well. China continues to be good. We saw a good quarter-over-quarter demand in China in P&SP, slightly up in polyurethanes quarter-over-quarter, up in Consumer Solutions. And flat to just slightly down in the other 2.

Operator

Your next question comes from the line of Mike Sison of Wells Fargo.

Richard Garchitorena
Wells Fargo Securities, LLC, Research Division

This is Richard, on for Mike. I was just wondering to follow up on that, if you could give us some color on where your operating rates are across your segments? Where do you see them for the industry, specifically for polyethylene? And how should we think about the potential improvement in EBITDA if we do get a stronger demand environment next year, and you can ramp those operating rates up to optimal levels?

James R. Fitterling
Chair & CEO

Yes. Just taking a look at -- I'll take a look at it both by segments, but I think you also have to take a look at it by regions. In P&SP, you're going to see operating rates substantially north of 80%. And obviously, when you think about Canada, the U.S. Gulf Coast, Argentina, our Middle East assets, all cost advantaged positions, even Terneuzen and Tarragona with pro-nap spreads of greater than $100 -- $120 a ton, that advantages them versus their competition within Europe.

So I think you'll see all those operating rates continue to be strong. And we're not building inventory. We're obviously able to meet that and move into the export market. Where you see things a little bit softer, obviously, construction-related segments, so in polyurethanes, which has a pretty heavy European footprint. We see lower operating rates there. We see that as well even on the Gulf Coast.

In Industrial Solutions, operating rates have been good. Our own issue in Plaquemine is the thing that has that capacity out. And then in Consumer Solutions, on silicones, we tend to see good operating rates in the quarter above 80%. And if you take a look at PM&C, those are slightly down because of the typical year-end slowdown in demand in coatings.

So all in all, I feel good that we're positioned to be able to ramp up to meet demand as it comes up our cost advantaged regions are continuing to run strong, as you would expect. And we're watching closely for the demand signals that will

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

pull us into 2024.

Operator

Your next question comes from the line of Kevin McCarthy of Vertical Research Partners.

Kevin William McCarthy
Vertical Research Partners, LLC

Jim, I'd appreciate your outlook for Dow's construction-facing businesses heading into 2024. Some of the companies that we cover are pointing to meaningful benefits from infrastructure and reshoring-related investments, basically fiscal stimulus. On the other hand, we've got rising rates, and that typically has a chilling effect. So how do you see those countervailing trends netting out for Dow and affecting the way you're planning for the future?

James R. Fitterling
Chair & CEO

Yes. Kevin, the things we watch on construction, obviously, on commercial construction just the completion rates on existing builds and the permit work that's going on, on new builds. I would say this has been a relatively strong year on commercial because there have been a lot of projects that were in flight. We're starting to see, obviously, some tick up in applications for pyramids on residential for the noncommercial side of things, which is good. But I think as long as there's a question out there on rates and will rates continue to rise, that's going to put a lid on what we'll see on residential construction.

In terms of infrastructure, we are seeing some movement in that space. I would say the biggest rate-limiting step on infrastructure is permitting. So the speed at which people can get permits, whether that's for -- it could be for pipelines, it could be for transmission cabling, you name it, but there could be some limitations there, and we keep an eye on that. Overall, I feel good about the fact that we're moving through the toughest phase of it right now. And if we could see some positive growth come back in the construction markets in China and the U.S., that will be a nice upside for us in '24.

Operator

Your next question comes from the line of Steve Byrne of Bank of America.

Stephen V. Byrne
BofA Securities, Research Division

Yes. The inventory chart you have on Slide 6 is intriguing. What I'm curious about is, for each of your businesses, do you have a view as to how much your customers have destocked your products relative to their end market demand. And thus, how much of this sequential decline that you've seen 12, 15 months is destocking versus just end market underlying demand weakness? You showed some sequential improvement in each of your businesses in the third quarter. Is that just destocking coming to an end? Or do you think that this is really some firming demand by your customers?

James R. Fitterling
Chair & CEO

Steve, it's a good question. Obviously, we get industry data that we published on the chart that you see there. When it comes to downstream when we get into the consumer brands and the retailer space, we have to go on reported data that we glean out of their public reports. But just a few things to keep in mind. We know in the auto sector, for example, that with the OEMs, it's been pretty much hand to mouth because there have been other rate-limiting steps like the

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

ability to get computer chips.

We haven't seen a big restocking with the OEMs. We've seen the OEMs continuing to run because they want to be in a position to ramp up when the strikes get settled. So I would say I don't feel like there's a lot of restocking going on there. I would say on the consumer brands and the pharma companies lately seen them, obviously, watching inventory levels. I don't get any sense of any stocking or big destocking going on there. I think it's running more to meet demand.

And then the other thing we take a look at is obviously what's going on with the construction segments, as I just mentioned. But it's a little bit harder. It's a little bit fuzzier when we get into the downstream. We don't have as much published data to rely on. So we look more at PMI. We look more at retail sales. We look more at what they comment on in their public filings.

Operator

Your next question comes from the line of John McNulty of BMO Capital Markets.

John Patrick McNulty
BMO Capital Markets Equity Research

And Howard, again, congratulations. You've been a huge help over the years. So the question would just be on the II&I segment. It came in -- it looks like solidly better than kind of what you were expecting when you gave the outlook on the 2Q call. So curious what the factors were that drove it? And I guess, if we back out the operations problem, you're kind of at a $250 million run rate in terms of EBITDA. Is that a reasonable way to think about how you start out looking at 2024?

James R. Fitterling
Chair & CEO

Yes. On II&I, we obviously saw a strong demand in the energy side, which is Industrial Solutions and the mobility side, which is more the polyurethane side. Durable goods are still lower than they were in the year ago period. We also had a little bit better because Sadara had had some lower operating rates from some maintenance time, and it's coming back out of that. So I think that will continue to be a positive upside. There's price pressure obviously on polyurethanes. We're going to see some positive impact from the new isocyanates capacity down in Freeport, which will be there.

The business also did a lot of work on their costs. So their EBITDA was up because they're also managing their costs. I don't think in fourth quarter, you'll see any higher impact on Plaquemine unplanned event. We saw about $100 million in the third quarter, you'll see that kind of flat to the fourth quarter. And then the target is to try to get that asset up and running in the second quarter next year.

Operator

Your next question comes from the line of Josh Spector of UBS.

Joshua David Spector
UBS Investment Bank, Research Division

I want to echo my congrats to Howard and [indiscernible]. So I just wanted to ask on the siloxanes side within PMC, made some comments on kind of some increased pressure there. I mean you've been under pressure in that business all year from added supply. Has anything changed in the last few months? Or is that just a reiteration of what you've seen? And as you think about next year, how much did things have to improve for that business to get back to a normal healthy level?

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

James R. Fitterling
Chair & CEO

Josh, obviously, in siloxanes, there was significant new capacity in 2022 and 2023, and we expect that to moderate in 2024 and beyond. That's put pressure on siloxanes prices, primarily in Europe or in Asia, which are at the lowest levels that they've been at in quite some time. They're starting to move up a bit in the fourth quarter, some demand related, some obviously related to higher silicones pricing, upstream silicon metals pricing, which is kind of moving things up. But I think what you're going to start to see is that you're going to have less capacity coming on, and the downstream market continues to grow at good rates, and we'll start to absorb some of that and we'll start to see operating rates improve '24, '25.

Operator

Your next question comes from the line of Patrick Cunningham of Citigroup.

Patrick David Cunningham
Citigroup Inc., Research Division

On the long-term decarbonization strategy, given the weaker macro and what seems to be some deceleration in appetite to tackle the green transition, how do you think about the risk to public-private partnerships, subsidies, incentives in North America and abroad?

James R. Fitterling
Chair & CEO

Yes. Good question. Obviously, our view on the Alberta project is we're working in an environment that's supportive of decarbonization. There's a price on carbon in Canada. There's existing carbon capture infrastructure. And there's obviously some investment credits for the hydrogen portion of the project. And so those are all positive. As we mentioned, though, we have to keep in mind that this is also going to be a very low-cost asset from an ethane supply capability standpoint. So that's why we say our expectation is the returns will be at or above our Texas-9 cracker, which is the best project that we've ever had in our history.

Having said that, we always have to keep our eyes wide open to what's going on, on the incentive space. We're not going to build just on the back of incentives. We've got to make sure that we make investments that are long-term, low-cost operating investments where we have advantaged feedstocks, and we have access to market. That's -- the same thing is true when we get into circularity projects.

And when we talk about our advanced and mechanical recycling projects, we've got to make sure that the partnerships that we have are looking long term and where they're going to access the waste, will they be the low-cost position and will they have the right access to market. So we're looking at them project by project. We're absolutely convinced that our timing is right on the Alberta project. We get this 1 final issue nailed down with the Canadian federal government, we should have FID before the end of the year.

Operator

Your next question comes from the line of Arun Viswanathan of RBC Capital Markets.

Arun Shankar Viswanathan
RBC Capital Markets, Research Division

I'll add my congrats to you, Howard, definitely a pleasure working with you over the years. I appreciate your insights. Yes, I guess I just had a question on China. Maybe you could just update us on what you're seeing there. Obviously,

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

very important for most of your markets. You noted that volumes were up across the 3 businesses year-on-year if you remove your merchant ethylene sales. But I guess what are you seeing in China? Maybe if you could characterize kind of polyethylene demand, maybe some impacts from -- on the consumer side as well as construction that would be great in your outlook?

James R. Fitterling
Chair & CEO

Yes. Good question. I mean obviously, GDP growth this year is expected to be about 5%, that's been on the back of consumer demand, and that's really been the government's position as consumer-driven recovery from the slowdown. Our expectation is because of what's going on in the housing construction markets, there will be some pressure on the government for some stimulus activity to get things moving there. Manufacturing PMI in September was up. It's the second consecutive month up, which is good. Automotive sales were up about 9.5% year-over-year in September. EV sales are up about 38% year-to-date. Retail sales were up 5.5% in September, and we saw a rise in the sale of clothes and textiles as well as some refined oil products.

I would say one of the things that we've always looked at in terms of coming out of a slowdown is the price of MEG. And one of the things that drives the price of MEG is the operating rate on the polyester plants, which are above 70% right now. We haven't seen that in quite some time. I think it's a little bit early to call that as the turn, but it's something to keep an eye on. And the volume moves quarter-over-quarter are good. Packaging has held up really well. And it typically does in an economic slowdown because of the nature of food packaging, medical packaging, day-to-day consumer nondurable items.

Operator

Your next question comes from the line of Duffy Fischer of Goldman Sachs.

Patrick Duffy Fischer
Goldman Sachs Group, Inc., Research Division

In both PMC and [i-Cubed], if you could walk through, pricing you called out is down sequentially in each of the SBUs, but yet EBITDA was up in both segments sequentially. So could you walk through and just tell us like where was the spread getting better because raw materials were falling more than price was down? And how much of that was kind of the structural costs that you guys are trying to take out that we would put in as kind of permanent?

James R. Fitterling
Chair & CEO

Yes. So if you look at II&I, the Louisiana outage was obviously a headwind. And then you had some turnaround tailwinds and cost savings, about $40 million. Variable costs on the benzene and propylene side really compress there. And then equity earnings from Sadara were a little bit better. So those were the moving parts. In PM&C, you had tailwinds of about $60 million from the turnaround in cost savings. So that's to the positive. You had some seasonality and lower siloxane prices to the negative, and we had also improved supply availability of siloxanes and some opportunistic monomer sales in the coating side of the business, acrylates were strong in the quarter. So that was -- those were the things that net-net made the swing in those 2 segments.

Operator

Your next question comes from the line of Aleksey Yefremov of KeyBanc.

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

Aleksey V. Yefremov
KeyBanc Capital Markets Inc., Research Division

Howard, congratulations. Just wanted to follow up on PMC. I would say a pretty healthy number. Is this a good level that we can use for thinking about next year? It sounded just in the previous answer, there were some opportunistic sales. So that's sort of where the question is coming from. Is this a real sustainable number to think about going forward earnings in the segment?

James R. Fitterling
Chair & CEO

Yes. I think as siloxanes improve, you can see some positive uptick in Consumer Solutions and silicones. The downstream demand has continued to be strong. So that hasn't been the primary issue. And we're seeing still continued good positive signs in the downstream demand sector, things like EVs and battery production. We'll have to watch the commercial construction markets. I think residential will start to improve somewhat, but household and personal care, consumer products, health and beauty, I would say, are going to continue to be positive in that space.

Coatings has been slow due to construction. I think there are some signs starting that applications for permits are starting to pick up on construction. That's kind of a U.S.-centric view. And in China, we'll have to watch if there's any stimulus to get the construction markets going there.

Automotive, I would say, is a bright spot globally, even Europe, in spite of a slow GDP has seen pretty strong automotive builds through the year. And I would say, once we get the strikes resolved here with the UAW and the big automakers, I think you'll see a step-up in demand because they'll start to be competing again for that market share.

Operator

Your next question comes from the line of Laurence Alexander of Jefferies.

Laurence Alexander
Jefferies LLC, Research Division

I just want to revisit the inventory level. If you think about lessons learned from this cycle, where do you see inventory days in working capital days shaking out at the next mid-cycle? And separately, Howard, just thank you for your help getting ramped up on Dow.

James R. Fitterling
Chair & CEO

Yes. Maybe Howard, do you want to touch inventories. You got the working capital team, and there's been pretty focused on this all throughout.

Howard I. Ungerleider
President & CFO

Yes. Sure, Jim. And Laurence, thanks and I appreciate everything you've done to cover Dow over time, and hopefully, we'll continue. Yes, we've been -- look, I've been very proud of the whole organization and how we've really -- if you think about one of the big changes that we've made, I think as a leadership team as an organization in the last 5 or 6 years is really a big step change on cash and managing cash just as well as we're managing margins and EBITDA and operating rate and AU.

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

We have structurally taken out about 8 days. When you think about it on a cash conversion cycle since Spin, 8 days has been structural and the other improvements have been more around the cycle. So obviously, that will continue as we head into -- as we've headed into this down cycle period, probably we've taken out about $1 billion of cash just on the releasing revenue from working capital as we head into a normalized macro and eventually a cyclical peak out into the future, you could expect $1 billion use of cash.

But overall, 8 days out, cycle to cycle, I think, is a good target so far. And I would expect that under Jeff's leadership, together with Jim and the leadership team, I would expect at least another day, maybe another 2 days in the next year or 2 will come out structurally. So I think a nice target is 10 days cycle to cycle from a structural standpoint. We've been really -- we've implemented OMP or in the process of implementing OMP in almost all of our businesses now and really thinking about it end to end from the customer back, the team is still working on it, but that's -- that gives you a good range.

James R. Fitterling
Chair & CEO

Jeff is going to make me cut you off before you set any more to targets for him.

Howard I. Ungerleider
President & CFO

Just 1 more day, maybe 2. That's it.

Operator

Your last question comes from the line of Mike Leithead of Barclays.

Michael James Leithead
Barclays Bank PLC, Research Division

Great. Appreciate you squeezing me in here. Just briefly on packaging. I think sequentially, EBIT was down about $440 million on $480 million lower sales, almost 100% drop through. Can you help us better understand the moving pieces in the quarter there?

James R. Fitterling
Chair & CEO

Sure. The lower sales were primarily due to being out of the merchant ethylene market, and so that obviously had an impact. We had the cost of the turnaround in the third quarter for the St. Charles cracker. And that was a drag, that drag becomes a positive as we go into the fourth quarter. We had some stronger equity earnings, which were up from the previous quarter. But then pricing and the impact of really a surge in feedstock and energy costs that happened in the third quarter were the big delta. Prices ran up on us in the third quarter. And then the pricing came in September, which kind of lagged the increase in the feedstock and the energy cost.

And so you saw that margin squeeze. I think we're back to even with that, and we'll get a little bit ahead of that. And like I said, I expect about $0.02 integrated margin improvement as we go into the fourth quarter.

Operator

There are no further question at this time. I will now turn the call over to Mr. Gupta for closing remarks.

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

Pankaj Gupta
Vice President of Investor Relations

Yes. Thanks, JL. Thank you, everyone, for joining our call today, and we appreciate your interest in Dow. For your reference, a copy of our transcript will be posted on Dow's website within approximately 48 hours. This concludes our call. Thank you very much.

Operator

You may now disconnect.

COPYRIGHT © 2023 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

Copyright © 2023 by S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

These materials have been prepared solely for information purposes based upon information generally available to the public and from sources believed to be reliable. No content (including index data, ratings, credit-related analyses and data, research, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of S&P Global Market Intelligence or its affiliates (collectively, S&P Global). The Content shall not be used for any unlawful or unauthorized purposes. S&P Global and any third-party providers, (collectively S&P Global Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Global Parties are not responsible for any errors or omissions, regardless of the cause, for the results obtained from the use of the Content. THE CONTENT IS PROVIDED ON "AS IS" BASIS. S&P GLOBAL PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Global Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages. S&P Global Market Intelligence's opinions, quotes and credit-related and other analyses are statements of opinion as of the date they are expressed and not statements of fact or recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P Global Market Intelligence may provide index data. Direct investment in an index is not possible. Exposure to an asset class represented by an index is available through investable instruments based on that index. S&P Global Market Intelligence assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P Global Market Intelligence does not act as a fiduciary or an investment advisor except where registered as such. S&P Global keeps certain activities of its divisions separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain divisions of S&P Global may have information that is not available to other S&P Global divisions. S&P Global has established policies and procedures to maintain the confidentiality of certain nonpublic information received in connection with each analytical process.

S&P Global may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P Global reserves the right to disseminate its opinions and analyses. S&P Global's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription), and may be distributed through other means, including via S&P Global publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.
© 2023 S&P Global Market Intelligence.