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OVERVIEW:

Company Summary

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PRESENTATION

David Begleiter - *Deutsche Bank AG - Analyst*

With us today is Mark Costa, Board Chair and CEO of Eastman Chemical. I'm going to lead off with some questions for Mark, and we'll go from there. So Mark, welcome to our conference.

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

Great to be here. Look forward to the conversation.

David Begleiter - *Deutsche Bank AG - Analyst*

Excellent.

QUESTIONS AND ANSWERS

David Begleiter - *Deutsche Bank AG - Analyst*

Maybe you can walk us around the world from a demand perspective by region, by business, by end market, how are things progressing through the second quarter?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

So I'll start with end markets first, and then I'll come back to regions. On an end market basis, if you look at sort of roughly half of our revenue is exposed to what we call consumer discretionary. So that's autos which is the largest end market. And then building construction and consumer durables and consumer durable parts, which includes a lot of appliances, TVs, things like that, are obviously connected to the state of the housing market because that's a big trigger for purchases of those kind of products.

And in that world, what I'd say is there isn't anything dramatic in its change relative to last year. So the building construction market, we expect to be similar to last year. There's obviously the hope for interest rates dropping and stimulating demand. That's obviously not happening. The auto market, I think, is a bit softer this year. And that's been the one change, I think, for the whole industry from what people thought in January to where we sit today, where that global market will be off low single digits. So it's not a significant change, but it is going to be a bit weaker this year from what we can see so far.

And I'd say on consumer durables, it's a little bit better than last year, but similar. So you could see demand getting a bit better sequentially out of Q4 into Q1. We're seeing seasonal demand that you would expect on those kind of products being purchased to be made into things that show up for Christmas, et cetera, things like that. So put it all together, it's sort of stable when you look at it.

On the what we call the more stable markets, so that's personal care, consumer packaged goods, medical, ag, all those kind of more stable markets, I'd say we're seeing modest sort of low single-digit kind of growth in the market for this year versus last year. We're not seeing any headwinds. We're certainly not seeing any snapback. And that's the whole point of those markets; it's relatively stable. So that is sort of the way it's playing out. Ag, I'd say, is so far looking like a normal year, lots of conversation about what ag will look like next year given the Strait disruption. But this year, I think it's in the normal category.

Geographically, I think it's what you all know. I mean, Europe and China are certainly worse off economically than here. The economy here is obviously not strong. And even though affordability is a big issue, I think what's defied everyone's logic, including mine, is that demand has held up relatively well compared to like consumer confidence. And the biggest way to explain that, I think, it's just employment is still really good, right?

So while people are worried about what's going to afford, they still the job. And so they're still buying things. They're certainly stretched. And we're worried about that as a back half kind of question around where consumer demand goes. But right now, we're seeing demand hold up well in this quarter across the portfolio.

We're not seeing any signs yet of demand destruction associated with what's going on with the Gulf and the impact it's having on prices. But it takes a while for those impacts to actually show up in the final price of a consumer product. So we're just going to have to see how this plays out.

David Begleiter - *Deutsche Bank AG - Analyst*

So relative to your guidance of $1.70 to $1.90 for the second quarter, are we tracking along with those expectations?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

Yes, we feel good about where we are on our guidance. So on the Specialty side, Advanced Materials, we're seeing the sort of sequential improvement in demand that we expected. If anything, it's a little bit stronger than we expected on the consumer durable side, a little softer on the auto side from the comments I just made. But overall, I would say demand is on track and the quality of the demand is good. So the mix value of what we're selling are some of the higher-margin products.

So that's good stability there on the price cost side of it, and the innovation is coming through as we expected. So the ramp-up of the recycled PET, ramp-up of some of the consumer durables using our Renew content is on track. So we still feel good about that 4% to 5% revenue growth this year versus last year for the Advanced Materials segment driven by the circular economy.

And it's not just that, right? You've got the heads-up display interlayers that are very high value that are growing faster than the underlying auto market. You've got some good solid growth in the performance films business. But I'd say that's more in line with the market than growing faster than it because aftermarket products are not exactly a priority. When people can't afford a car, they're not going to put film on it, right? So that's a bit more challenged.

But overall, I think it's in good shape on the price-cost side. You've got the benefits of price increases we put in place. We've got them all in place as we said we would do. I'm feeling confident about that. Because of the speculation that maybe the Strait will open and oil prices come off, raw material headwind is probably not quite as strong as we expected and things like PX, which have moderated a bit. So helpful.

And then when you look at that volume increase, and you put it together with operations running hard to keep up with demand relative to lower -- relatively low utilization we had in the first quarter in Advanced Materials as we are still managing inventory and uncertain about demand. So we got a pretty helpful utilization tailwind going from Q1 to Q2 in Advanced Materials. So that segment is on track.

Additives & Functional Products, it's just rolling along, demand is holding up solid. They have a lot of cost pass-through contracts. Two-thirds of their demand is in stable markets, so it's stable. And then the cost pass-through contracts are working as it should to keep up with raw materials, energy distribution costs. So that business is on track for a good quarter.

Chemical Intermediates is obviously feeling fine. I'm sure we'll come back to that in a more detailed question. So I'll just keep it short here. It's doing fine. And its earnings are probably going to be a bit better than $50 million, which is what we originally sort of estimated with the tightness in the market.

And then I would say fibers is going to be potentially a little bit light. It's -- as we told you, Mid East demand, how to get [Chile] in. And more importantly, cigarettes out is the bigger issue that they're solving. But it just takes time to sort of work our way through it, right? That's about 10% of the fibers demand revenue is the Mid East in tow. And so that was a bit of the challenge.

But overall, the customers are committed to their contracts on a full year basis. We're not seeing any divergence there. We'll come back to that, I'm sure, in another question and what that means for the back half.

David Begleiter - *Deutsche Bank AG - Analyst*

Would you say the bias is to the upper half of the guidance range?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

Well, I would say where I sit today, you could see potentially we're in that zone. But June is an extremely important month. And you just don't know on how demand will play out in June.

The order books in Advanced Materials are solid through July right now, which is good and not typical, right? But at some point, if the Strait opens, people are going to say, oh, maybe if I just hold off buying, the price will get cheaper, right? There's going to be a month like that at some point.

I don't know which month that's going to be. Clearly, none of us do, but I don't think it's going to be June at this point. So I feel good about sort of how volume should be trending. But it's war on multiple continents. I mean, there's a lot going on.

David Begleiter - *Deutsche Bank AG - Analyst*

And just on that prebuy question, you -- there has been some prebuying across the portfolio. Is that fair?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

I don't think there's been much prebuying in Chemical Intermediates, just to start off the easy thing. We can sell whatever we can make because other people can't make it, right? So everyone focuses on oil, but naphtha and methanol and things like that is what you should really be focusing on for this industry at the moment. And it's short, right? A lot of 15%, 20% of the naphtha for the world comes out of the Gulf, it's not coming out.

There isn't a bunch of refineries sitting around empty outside of the Gulf and to be ready for the scenario. So when you're dumping all the strategic reserves into the world, you're depressing oil prices because there's no refineries to use it, right?

And so that's the part that I think people are missing is you got to do the supply-demand balance at every step in the chain. And you've got an artificially depressed price in oil, I think, and it's partly because demand is coming off on fuel. But it's also partly because there's no refineries to turn in India. And so that naphtha situation is going to drag on for a long time. We were just talking about in the last meeting.

I met with the CEO of one of the biggest chemical tanker companies. And they're like, look, there's a clear priority of what's coming out of the Gulf. And it starts with avgas and urea and sulfur because we need transportation and people not starve next year, right? So that gets prioritized, then oil, then chemicals.

So we are not in the priority rank of getting things out of the Gulf. So when you open this thing, if they have -- I don't understand how they do this, but apparently, they can prioritize what goes through it, I'm told. And if that's true, it's going to take a while to reestablish naphtha and other refined chemical products for very good reasons for the state of civilization, right?

So I think things are going to stay tight. Certainly, people who are far more qualified like the Dows and Lyondell can give you a better detailed explanation of it. But I've had conversations with those guys, and they're of this view. Without doubt, China is adding some capacity, but we'll have to see how it plays out.

David Begleiter - *Deutsche Bank AG - Analyst*

There may be some prebuying in AM. Is that fair or at least some --?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

On the AM side, there could be a little bit of prebuying, and there could be a little bit of prebuying in AFP. Certainly not, we have the opposite going on in fibers. You have to keep in mind that the back half of last year, which was brutal, as you all know, involved a huge amount of destocking.

The good news is we saw that destocking come to an end because we saw a very substantial recovery, right? Sequentially, our volumes in AM and AFP came back 10% from Q4 to Q1, which was encouraging.

But the underlying demand hasn't improved a lot. January and February were relatively weak. So no one was ramping up plants, including us, right, for some expectation of growth this year. People are being cautious.

So suddenly, you get to the war where now people can't make things as easily as they used to. People may want to buy forward, but they can't because it's not there to buy. So I think that there's just constraints on what's out there to be prebought because we certainly had stock outs in places as we got to the end of March, constraining what we could actually allow people to build. And we're still running hard just to keep up with demand right now.

So I think that that inventory situation is quite a bit different than obviously when we were in '22 or even in '25. Because in '25, everyone thought the economy is going to get better, it's present. This is all good. People like us, we were building inventory for growth for the year in the first quarter. That did not happen this year.

David Begleiter - *Deutsche Bank AG - Analyst*

Back to the conflict, how long do you think it will take for supply chains to normalize once the conflict ends and the Strait reopens?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

There's two different camps on that out there, and I'm guessing the answer is in the middle. So one camp is China is going to make everything and ramp up their coal assets and this and the other. But 70% is naphtha, 15% to 20% is coal. I can't ramp up the coal that much.

And they certainly have plenty of reserves. But again, they didn't have a bunch of idle refineries sitting around. They're all running relatively hard. So they don't have a lot of swing up in what they can do to solve the gap in the world. So I think I'm in the camp that things are going to be constrained. It's going to take a while to reestablish the supply chain.

Just like shipping explanation, you got to fix the things that are damaged in the Mid East. You've got to reestablish. Just starting these plants are not like light switches, right? It takes a while to start them up. And there's some we know got shut down hard, which never come back well.

And so there's all of that that's going to sort of drive this out at least six to nine months and really getting back to some stability. I don't think we're ever going back to where we were in the back end of last year or the beginning of this year. Whether it's oil or naphtha or everything else, I just think it's going to be structurally short for quite a long time.

But it's not going to stay as extreme as it is here, right? So our expectation is there's some moderation of spreads in the back half of the year, and we'll see how it plays out.

David Begleiter - *Deutsche Bank AG - Analyst*

And just the ACC, the American Chemistry Council annual meeting. What was the mood in Colorado? And maybe what's the divergence of opinions if you mentioned them a little bit on the reopening?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

What I just said is there's -- things will remain tight versus it's going to loosen up faster than people think. And normally, at ACC, by the way, you have all these meetings like this, back-to-back meetings. And by the time you get to the end of yesterday, everyone has the exact same point of view about the world. And that is not the case right now.

People have very divergent views about how this is all going to play out. And as I said a moment ago, I think the answer will typically end up being somewhere in the middle of the extremes. But I would say uniformly, the opinion is what I said, demand is holding up. We're not seeing any signs of demand destruction.

I think that's sort of a consistent point of view out there. Everyone is worried about inflation impact on consumer demand in the back half of the year. It's only rational. But the consumer continues to defy that concern every year and holding -- to be clear, it's not like markets are good. Let's just not overstate, right? End market demand is bad, but it hasn't gotten worse. But we're -- housing is 20% lower than 2019, right? Same in Europe, 20% lower. China, total disaster. There's nothing good about that.

It's just not getting worse. But there's a huge amount of pent-up demand when you think about just how many housing transactions have not happened now for four years, right? The age of a car is getting 14 to 15 years old on average, right? I mean, that's -- a lot of really old cars that are just going to start hitting end of life.

Appliances, right? They were massively bought in 2020 and '21. Now they last five, seven years, and then you got to replace them, right? So you're getting to replacement cycles at a minimum, let alone maybe some demand recovery. So the area under that curve is significant. It needs to be unlocked, which is, in my opinion, not probably going to get unlocked this year. Unless interest rates come down, you're not going to sort of unlock the housing / consumer durable side of things.

So I'd say demand-wise, everyone is nervous about the future but not seeing it yet in their orders. People aren't seeing a lot of pull forward consistent with the comments I made earlier. So there's maybe a little bit of that going on, but not significant for the reasons I've already mentioned. And the big question about China and what they're going to do, I think, is they're just going to keep doing what they've been doing, which is add capacity and take global market share on the commodity side of the world, where it's just about price and subsidies they have to go do it.

On the specialty side, we still don't have a lot of direct Chinese competition yet. I mean, we always assume we're going to have it. That's why we have an innovation-driven company to innovate and stay ahead of that challenge. Circular economy should be a regional business. And so that's another way to sort of disconnect from Asia if we're going to have actual circular economy.

So we're always looking for all the moats that we can build around that threat. And so far, everything is holding up reasonably well.

David Begleiter - *Deutsche Bank AG - Analyst*

And longer term, you're thinking and the group is thinking about benefits to US suppliers, your heavy US asset base. Is there a premium on US supply, security of supply? Is there less dependence on virgin Gulf supply, or the long-term benefits beyond 6 to 12 months of this conflict to you and your US-based peers?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

Yes. Without a doubt, that's true. On the commodity side, we can sell whatever we make, right? So that's clear as markets are shorted from what I said earlier about naphtha and everything else around the planet. On the specialty side, I think, for sure, part of the reason orders are holding up as they have is we're viewed as much more secure supply.

Most of our competition is not in China, but it is in Asia. It's typically Japanese or Korean competitors who are in the best spot right now on the specialty side of things. And so that's holding up reasonably well. They're under more cost pressure than we are when it comes to pricing.

I think that being a North American asset-based company, 80% of our volume is made in the US. 60% of our revenue is outside the US. We're highly levered to North America always have been. And now it's a really good thing. So our energy costs are advantaged.

Obviously, our olefin cost structure with ethane and propane are advantaged. And we're viewed as having a much better position to be secure in our supply and reliable supply to customers. And that's always a good thing.

We will come -- the North American chemical assets will be winners in this long term. The Mid East is -- it's going to be hard to recover the Strait being safe completely, I think, forever at this stage because the Iranians now know they have a huge leverage point. And while the Chinese are certainly adding massive amounts of capacity and massively subsidizing it and getting discounted oil to run it, one, they're not getting the discounts anymore. And two, all their assets from a cost position point of view are in the third quartile.

So you can add it, but they're not cost advantaged in doing it, right? So if they want to subsidize forever, then that's a long-term problem for the industry. But there's also just a limit on how long you can do that.

David Begleiter - *Deutsche Bank AG - Analyst*

Segue into Chemical Intermediates, which has been the biggest beneficiary for you guys in this conflict. Where are spreads today versus where they were pre-conflict, expectations for the back half of the year? And longer term, the role of this asset in your portfolio and the company?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

So there's two elements of what's going on in Chemical Intermediates before you get to the war, right? There is a structural element and there is a cyclical element to what's going on. The cyclical side is North American markets are far more attractive than the export markets for anyone who makes these kind of products, whether it's acetyl or olefin.

So demand came off because that also goes into housing and goes into consumer durables and cars and everything else for the intermediates that we make. So that has that same sort of market exposure. So we had a mix hit when that demand is lower than normal. And so -- and those margins are much better than export, right?

And then on the export side is where the structural part showed up because that's -- the Chinese aren't really penetrating our market because we have tariffs and things like that. And logistically, it's easier to go to Latin America and Europe for them or Southeast Asia than it is to come here. So that export market got crushed in '24 and '25 by all the exporting done by China, right? So those values basically got down to very low values.

Those values are not very high, right? So that benefit on the export side of thing is obviously helping us. So while that comes off, if there's stability that comes back in the North American market, you can offset some of the decline in export values with higher value mix in North America and some demand recovery. Those can stabilize out a little bit. That will be helpful.

But the margins right now are certainly higher than what I would call normalized in the world that we now live in, given the structural dynamics out of China. But I also think because of everything I've already said, it's not going back to where we were last year, somewhere in the middle. I mean, anyone guess on where that is.

David Begleiter - *Deutsche Bank AG - Analyst*

And long term, its importance and role in the Eastman portfolio?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

Look, the olefin business -- first of all, acetyls is part of the integrated complex in Tennessee. That's not going anywhere. It's all big pile of spaghetti there, right? So you can't disassemble anything with cellulosics or polyester from that side. But when it comes to the Texas side, we've been clear that's not a strategic asset to us.

It carries a lot of cost. A lot of cost is spread by revenue, and it has a lot of revenue. So it carries a lot of cost structure. So you got to keep that in mind when you're trying to think about its own portfolio for its assets.

It provides -- half of the output does go into our specialties. That gives us a nice secure raw material position that's made in Americas. So that's a good thing to have. So -- but at some point, does it fit the portfolio as we're growing the specialties and building up the circular economy? Probably not. But right now, it's doing its job.

And it's providing some earnings stability, right? The nice thing is it's a small percentage of the portfolio. But when raws go really up like '21 or now, where you have pricing trying to chase it on the specialty side, the margin expansion here actually offsets that. It gives you a bit of a stability hedge. But you don't want to be too big. Otherwise, you're going up and down with it.

But it's small enough where it just helps offset some of that and gives you more stable margins. So there's this thing going on with our stock where people know how to trade this, right? I want to trade on the commodity side, or I want to trade on the specialty side. So you can see that word debate in the investment community going on daily.

The reality is it provides stability, which is a good thing in this world, stable cash, stable growth. That's what you get out of this portfolio.

David Begleiter - *Deutsche Bank AG - Analyst*

Talking about stability, fibers acetate tow, we have seen some destocking in the last few quarters. Where we stand on that journey? And where we stand on that destocking journey in tow?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

So the destocking is not a few quarters. It's -- unfortunately, I have to think about this in years. So tow is a critical part of a cigarette. It's about 5% to 10% of the price of a cigarette. If you run out of tow, that is super bad when you have 65% gross margins, right?

So security of supply is always the priority in history for this industry. When we had all the shortages and we had some operational problems in the beginning of 2022 with our site, the customers became -- especially the big multinationals who are very well-run built inventory because they want to secure supply. They built it in '21, they built it in '22, they built in '23, a little bit every year because we have these volume band contracts that they stay in.

They don't buy a lot extra each year, but they bought a bit extra each year. So they accumulated a lot by the time they got to the end of 2024. And of course, no one ever tells you when they're building inventory ever. Because they're worried to put them on allocation and not give it to if the market is relatively tight. So you just don't know what's happening. That's what happened across so many marketplaces in '21, not just tow but everything, right?

But they didn't -- and everyone else started to destock right away in the end of '22. These guys, because they're so worried about secure supply, didn't start destocking anything until last year. And they're all under contracts, especially the big ones that have a min and max. So they went to their minimum commitment, which allows them to chip away at the destocking, but they can't solve it in a year because we hold them to the minimum contract to keep stability in the business on the volume side.

So it's just -- it started last year. It's going through this year. It's going to keep on going to some degree into next year. By then, it will be done. I mean, there's an age limit on this tow, right? So it will sort of resolve itself, but it's a journey.

But that's the primary drop in demand. I mean, why it got enabled was a Chinese player came on with some capacity that made it available to the Western world. Historically, they've just been selling into like Russia, Venezuela, and Iran, places that we can't sell. But they added some capacity so they could actually take some of the risk out of the marketplace about supply, which is what enabled the destocking.

The asset that's being shut down by Celanese is pretty much equivalent to what they added. So that helps sort of on the balance side. But there's still a lot to go. And the margins are very highs. People get tempted into chasing volume because the value is so high. So that's why you get these dynamics where prices come off. And we had really high prices in some places, really high. And so it was not a surprise that they were going to come off.

David Begleiter - *Deutsche Bank AG - Analyst*

Underlying decline rate is still the same 1% to 2% or --?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

It was 0% to 1% between 20 -- it turned out between 2014 and 2024. It's moved more into that 1% to 2% range. There's some more excise taxes in places like India and this, that, and the other that's going to impact demand to some degree. But historically, demand despite all the drama around cigarettes has just not changed a lot over time. But it will definitely decline a little bit more than the last decade.

David Begleiter - *Deutsche Bank AG - Analyst*

And the non-tow portion of fibers, is that still progressing?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

So the textile business was a great opportunity to keep the assets running full. The margins were actually pretty good. I mean, not exactly tow margins, but not that far off. So as that business was growing, it offset some of that tow market decline.

As we told you, about 40% of the earnings decline has nothing to do with tow from '24 to '25. And this was about a $30 million decline in '25 relative to '24 with all the drama of the trade war, the retaliation tariffs on our products going into China that slowed sort of demand for us.

And I'd say that we thought demand would be coming back meaningfully this year at the beginning of the year. It's a lot slower than we thought because of all the economic drama going on right now. So there's still that $30 million recovery out there, but it's more in the future than it is this year at this stage. I mean, it's coming back a little bit, but not a lot. So that will help.

David Begleiter - *Deutsche Bank AG - Analyst*

I want to touch on M&A. It's been picking up in the space here and there. You've been one of the least acquisitive companies in chemicals. I think you've earned a right to do something, but you've chosen to focus organic internally. What role does M&A play in the growth of Eastman Chemical?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

Yes. So historically, by the way, we're one of the more acquisitive companies in a different time frame. So we went through this huge portfolio optimization, if you know our history from 2006 to 2011, where we got rid of a lot of commodities and really upgraded the quality of the portfolio through a series of divestitures. And then we flipped around in 2012 through '14, we did $9 billion of acquisitions, right? So we were very acquisitive, right?

So we bought Solutia, we bought Taminco. We bought a bunch of bolt-on businesses, all of which have delivered great returns. And very successfully integrated into our company. But yes, when we hit 2014 after we bought all this stuff, we went into an organic phase, say, well, we have all these products, all these specialty businesses. The ones that we bought had a lot of potential, but had not been properly invested in from an R&D point of view.

So we were working on that and ramp that up successfully and built a pretty good business. And through all that, and we had a lot of leverage that came with it, the economy wasn't exactly great. So the rate of delevering wasn't quite as fast as we'd like.

And so it took us a while to get to the balance sheet back to where we want it to be. And then you had COVID hit and then you had supply chain crisis. And then you had a complete another drop of manufacturing consumer-related demand, right? So it's been a little chaotic in the last --

Yes, it just never stops. And by the way, I joked a year ago that we're running out of terrestrial problems. So we'll have an alien invasion. And apparently, that's true, too. So who knew?

But the good news is they've been walking among us for decades, and so they must be peaceful. So maybe we don't have to worry about a disruption, but maybe he'll tax other galaxies as well for inputs. We have to think about all that chaos and being responsible, your balance sheet and your cash flow and being stable and reliable. So running around doing M&A didn't seem like a great idea. But the real choice that we made getting your question, but I think history is important.

The real choice we made in 2021, which is we could go really aggressive with the strength of our balance sheet at that point and the strength of earnings right back then on the M&A side or we could go on the circular economy side.

We couldn't do both. And we decided that the circular economy had far more upside and organic growth gets a far better valuation if done well, that, that was the right choice because we're unique in what we could do in something at that scale of platform level relative to anyone else in the industry. And we still believe there's a lot of value there, right? Go look at PureCycle, right, negative $140 million of EBITDA, $2 billion valuation, right? And we've got very significant revenue.

We actually have a significant profit, and it's not in our stock at all because people are worried about the core. You stabilize the core and you start getting that valuation on top of the portfolio creates a lot of value. So we still believe our organic strategy has a lot of value despite all the chaos.

Having said that, the world is going to speed up on M&A, as you said. The world is definitely going to, I think, in our industry, consolidate to some degree. Certainly, that seems to be the going theory. And so we're looking at all options at this point. But there's nothing, just to be clear, going on at the moment.

But you have to realize the world is changing and change with it, right? So M&A probably play a role in our portfolio too, both ways, both things you could divest or things that you could buy or et cetera. So we're starting to consider those things, but there's nothing imminent.

David Begleiter - *Deutsche Bank AG - Analyst*

The pipeline filling small bolt-ons at least? Or how is the pipeline today?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

The pipeline -- I mean, there's always the bolt-ons out there. But the thing about bolt-ons is they take a lot of effort relative to the value they bring. And so if you've got a machine going like Rohm and Haas did a long time ago where they're rolling up like competitors in coatings, it's really compelling. And we've done that well in performance films where we rolled up competitors and built that business to be more robust than what it was. And we're always open to doing it. But it's not as robust as any of us would like it to be.

David Begleiter - *Deutsche Bank AG - Analyst*

Right. Okay. You mentioned methanolysis organic growth. Where do we stand in that journey today?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

Well, certainly, it's a little slower than what we thought in 2021. So the current status is the plant is running great. The yields are fantastic. We've got clear insight on how we can debottleneck to at least 130% of design rate, right, to stretch the asset and give us time before we have to have the next big capital spend. On the specialty side, the volumes are growing with some of the recovery in the market, but you're going into blenders.

You're going into reusable water bottles. You're going into those products that are discretionary, right, where the market conditions aren't great. So it's going to grow with the rate of the market because people don't want to just add recycled content in an existing product. They want to put it in a new product launch, right, where they get people paying attention, you get the value for it, et cetera. So if you're not launching products, then you're not growing a lot of Renew.

So we are seeing half our revenue growth, which would be that 4% to 5% I mentioned on AM is in the specialty, where they are starting to launch some products, they are picking up some volume there. The other half, which is the rPET, demand has improved considerably for that side of the business in the last nine months, as we've talked about on the calls, principally because the mechanical is degrading faster than they thought. And then we blend it with the mechanical and make it look good again. So there's more recognition of our value proposition about how our product is identical to virgin where mechanical really is not and going to be less so every year. So that's creating a lot of opportunity for us.

At the moment, we're capacity limited, not demand limited. So it's -- our assets are flexible, but they're not that flexible, right? You have to take some effort to sort of swing them back to making PET, which is what they originally did before we turned them into specialty assets. And so we're in the middle of sort of making some of those adjustments. We told you about one line we're switching over, and we're looking at another one right now.

So things are good on the demand side. Premiums are holding.

David Begleiter - *Deutsche Bank AG - Analyst*

And what's Pepsi? Pepsi is a big customer for you guys. What's been their feedback on the material and what do they want from you going forward?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

They've been extremely happy with the product. They actually have a whole thing on their website around Eastman and how we're enabling them to sort of address the environmental challenges of packaging. So they've been great and a few other big package companies are engaged as well. So they're pulling forward the volume even in this economic environment.

And you think about the stress test and the value proposition, things are not good if you're in the consumer package world, right? They have demand challenges because pricing got so high. They're lowering pricing right now to rebuild volume and they're still buying our material it's a good value proposition to us in this context, right?

They could easily just say, I really care about the environment. I'm going to care a lot more about it in 2027 than '26. And a number of the brands are doing that, right? That is certainly happening. But the ones who really take the environment seriously like Pepsi, like P&G as two examples, are very much sticking with their plans.

David Begleiter - *Deutsche Bank AG - Analyst*

Then you have your home state, California putting in place recycling laws, that can only help matters, I presume.

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

Depends on how the rules get written. So there's always two camps out there in the environmental community. One is they really want to solve the problem, which is recycling and supporting all those types of initiatives, whether it's recycling or the biodegradable cellulosic polymers we have that we're taking into foodservice now. But there's also a contingency that just wants the world to have no oil on it ever, right? And so the only way to get rid of oil is you have to get rid of combustion engines, you have to get rid of plastic.

So that group, the more extreme NGOs just want to ban everything, right?

So there's that war going on, which is totally unrealistic. It sounds good, raises money, but they can't actually ever accomplish their goal. But -- so that creates a lot of policy volatility. But yes, in general, the recycling rates being required, EPRs, which are enhanced producer responsibility, also known as a tax on packaging waste, those drive behavior. Colorado, I would say, is the best example of a pretty thoughtful design that I wish more countries -- or not countries, but states would adopt.

Of course, California is going to be more extreme about everything. So we'll see how it plays out.

David Begleiter - *Deutsche Bank AG - Analyst*

So what's next here for methanolysis? Texas has obviously didn't work out initially, but what's next from a capacity standpoint?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

So the Texas project was a very capital-intensive design because we're building everything new, right? Polymer line new, methanolysis new, all the infrastructure around it new. And that's led to what the capital cost was so high and also helped us when we got that DOE grant of $375 million to bring the number back down to sort of more targeted rational range. So when we lost that grant, it actually forced us to step back and say, well, is there a different way we can approach this to be a lot more capital efficient. And at the same time, you have so much stress in the commodity markets, including PET, a lot of assets being effectively abandoned.

That creates the opportunity to leverage existing facilities and infrastructure and focus really the capital down to the methanolysis unit, right? So we've been looking at multiple options of how to do that. I believe we have a couple of different pathways. But we haven't finalized exactly what we're going to do. And so we're not going to talk about the details until we've got it all sorted out. But there is a capital-efficient way to go forward.

David Begleiter - *Deutsche Bank AG - Analyst*

Could we hear about that in 2026 or --?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

We could not start in CapEx but a pathway more clarity and precision in '26.

David Begleiter - *Deutsche Bank AG - Analyst*

Would that be only US or Europe as well?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

Be both. The issue -- we're in a tough environment. We're going to be very disciplined about our capital allocation, and we're not going to be ramping CapEx up a lot until we feel like the economy is stable, certainly not the moment. And because we can debottleneck the first plant, it buys us, let's say, two years of grace and how we want to sort of build out this facility and stretch its capacity and then add on the next plant. So -- and that allows us to be capital efficient, allows us to be disciplined about the market demand, making sure it's building as strong as we believe it will, and therefore, higher confidence around a good return on investment for the second plant.

David Begleiter - *Deutsche Bank AG - Analyst*

My last question is you've always been hard to value, peg, what is Eastman Chemical. And I think people default to a lower valuation they can't really figure out what you are and where you're going. How do you address those concerns and issues? You have Greg here as well. The age-old question, why is Eastman and how do you value Eastman Chemical?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

Well, look, the core of Eastman is it is a specialty chemical company, right? It's not a commodity company. Yes, it has a little commodity tail on it, which actually stabilizes earnings and cash. And we can debate how it impacts the valuation. But the reality is Advanced Materials and as the Functional Products business are the sort of the core of where all the capital goes and where the growth happens or where the acquisitions will occur or whatever else.

Circular economy is completely not valued in the current stock price, right? I think we can 0. I agree. But we have a company that can't make any profit that has a $2 billion value.

So as a reference point, I'm feeling pretty good that we're worth a lot more than that on the circular economy since we've got the largest asset in the world that's doing chemical recycling. It's up and running. It's up and running at high yields, right? So the technology is totally proven. We have an established customer base with a reasonable -- a serious amount of revenue now.

We were paying premiums in the worst economic environment we could imagine, right? So I think that platform has value, right? So I think that what's being missed is the margin challenges, the earnings challenges are all volume driven. It's not about some sort of collapse in margins in the specialties. It's just asset utilization, right, because demand is low. So you've got all this pent-up demand on the upside in the core business. You've got circular -- not just on the polyester side, but on the cellulosic side.

So we got the Aventa products and things like that coming on foodservice. Obviously, we got to stabilize fibers and take that uncertainty off because I think that's a bit of a hang up. But we're in an earnings known range now where it's going to start stabilizing. I mean, it's not stabilized yet, but we're working on it.

And then I think CI gets back to a more stable level, right? So call it $150 million, $200 million of EBIT on a normalized basis. And you've got the E2P investment that adds $50 million to $150 million of earnings depending on the market conditions on the ethylene propylene investment that will be online in the summer of '28 that further strengthens that, which is just great cash flow. Now whether it stays in the portfolio or not is debatable based on how we're growing the specialties.

But I think that people are missing about the quality of the portfolio and how well it's holding up in this context because so much of our demand is exposed to discretionary consumers. So that is the issue, right? We are going to have exposure to discretionary demand. That is the one demand volatility on that side is real, but we're at the bottom of the market when it comes to consumer discretionary demand. So there's never a better time to get into the stock because the incremental margins are at least 30% to 40% of Advanced Materials when that volume comes back, if not higher.

So it really hurts on the way down. It's really good on the way back, not just on the earnings, but on the cash flow, right? Because the margins on those products are high. And AFP is really holding up well through the things. So you got a nice stable base there, and then you've got all the upside in AM. I just -- I think they obsess too much on the tail risk, which is a very small part of the company.

David Begleiter - *Deutsche Bank AG - Analyst*

Do we get a circular segment at some point to highlight its value relative to the company you mentioned, your own circular segment?

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

We've had that debate. I mean, with the first plant, that's not going to happen because it's so integrated into making all the specialties. As you scale up to a second and third plant, that's more stand-alone, if there's -- we perceive value to making sure that's called out as a separate segment, we'll do that. But that's a problem for a different year. Right.

David Begleiter - *Deutsche Bank AG - Analyst*

Our time is up. Mark, Greg, thank you very much.

Mark Costa - *Eastman Chemical Co - Chairman of the Board, Chief Executive Officer*

Thank you. Thank you all.
