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EMN.N - Q4 2025 Eastman Chemical Co Earnings Call

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OVERVIEW:

Company Summary

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PRESENTATION

Operator

Good day, everyone and welcome to the fourth quarter and full year 2025 Eastman conference call. Today's conference is being recorded. This call is being broadcast live on the Eastman website at www.eastman.com.

I will now turn the call over to Mr. Greg Riddle, Eastman Investor Relations. Please go ahead, sir.

Gregory Riddle - *Eastman Chemical Co - Vice President, Investor Relations*

Thank you, Becky, and good morning, everyone, and thanks for joining us. On the call with me today are Mark Costa, Board Chair and CEO; Willie McLain, Executive Vice President and CFO; and Jake LaRoe, Senior Manager, Investor Relations.

Yesterday after market closed, we posted our fourth quarter and full year 2025 financial results news release and SEC 8-K filing, our slides and the related prepared remarks in the Investor Section of our website, eastman.com.

Before we begin, I'll cover two items. First, during this presentation, you will hear certain forward-looking statements concerning our plans and expectations. Actual events or results could differ materially.

Certain factors related to future expectations are or will be detailed in our fourth quarter and full year 2025 financial results news release, during this call, in the preceding slides, and prepared remarks and in our filings with the Securities Exchange Commission, including the Form 10-K filed for a full year 2024 and the Form 10-K to be filed for a full year 2025.

Second, earnings referenced in this presentation exclude certain non-core and unusual items, reconciliations to the most directly comparable GAAP financial measures, and other associated disclosures, including a description of the excluded and adjusted items are available in the fourth quarter and full year 2024 financial results news release.

As we posted the slides and accompanying prepared remarks on our website last night, we will now go straight into Q&A. Becky, please, let's start with our first question.

QUESTIONS AND ANSWERS

Operator

Josh Spector, UBS.

Joshua Spector - UBS AG - Analyst

I wanted to ask two things on Fibers here to start. First, can you talk a bit more about the actions you're taking, how the shutdown impacts earnings through the year? And second, if you could talk about cellulosic a little bit and your ability to pass through costs there if prices go up due to changes in supply behavior.

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

Sure. Josh. So Fibers obviously is a top priority for us as we've been focusing on how we manage that business and stabilize it after what happened last year. Before I get into some of the actions we're taking in context of matters, and so I'm going to just remind you something we said before, where tow is certainly the largest driver in the drop in the volume and we held prices actually relatively well in spreads last year.

But that -- about 40% of the EBIT drop is actually not tow, right? So you've got about a \$30 million decline that was tariff-driven in the textile business. While normally that's growing to offset market decline in tow and said it reversed in the negative direction with all the tariff pressure and consumer pressure.

The second was the overall stream slowed down because of reduced demand across the company using cellulosic and that was about a \$20 million headwind. And utilization and energy costs for about \$15 million higher. So there are multiple levers tow plus everything else in this portfolio that matter.

When it comes to the tow side of things, we feel good that we've stabilized the volume situation this year relative to last year in our contracts with our customers. It did include a bit of a modest price decline to make that happen. And what that price decline really is about is, there were some customers that had higher prices in the marketplace, and they pulled in to be more in line with the broader market into where we are today.

So stable and the volume we're assuming when we say stable is assuming our customers are at their contract minimums because we do expect destocking will continue through this year like it did last year. As a reminder, we have contracts last year, too and we started the year thinking people will be buying in their normal range of the contract. And then as we told you through the year, they moved to their contract minimums, but we held them to that.

That's why they have to continue destocking this year to get to where they want to be. And so -- and Q1 is starting out a little bit light. The contract commitments are annual contracts, but they have some ratability flexibility around the quarters, and we expect the first quarter start off a little soft, hence our guidance and then they will ramp up as you go through the year.

And normally, the back half is a little bit stronger anyway as they load channels ahead of the tax increases that normally happen every January. So we feel good about that.

Obviously, there are a bunch of actions in addition to stabilizing that business directly that we're taking. So the cost reduction actions across the company, that significant cost reduction goal that we have this in the \$125 million to \$150 million range to build on \$100 million last year, a decent portion of that goes towards Fibers with some of the actions we're taking specifically on how to optimize how we operate our assets more efficiently.

The growth in textiles, we're seeing growth start to come back slowly, but it's coming back. We expect that to build through the year. We are expanding our efforts. So today, we've mostly focused on selling Naia filament, which is a very high-value product in the textile market. There is another product which is Staples, short fibers that you use. It's a more economic product. It typically goes into things like denim and fleece and it's a huge market.

And so the margins are not as good, but they're still reasonably attractive. And so we're ramping up our effort, already got sales for this year, and we're going to try and ramp that up as another way to drive asset utilization.

And then on the broader stream question around cellulose. We have the Aventa product, currently lives in corporate other, but that product is moving forward. We're going through a lot of product qualifications last year, and we expect volumes to build this year, especially in food trays and cutlery and straws. And so that will drive stream utilization as well.

So a lot of different actions that we're taking. They will build through the year. So how we get to the number this year and stabilize it, will sort of build through the year so we build on all the different actions we're taking.

When it comes to price on the tow business, most -- some of the prices do have CPTs in them and allow for adjustment for changes in raw material and energy costs. So a number of those contracts will adjust, a few won't and the textile prices are market-based. So we can raise prices.

But in this weak environment, I would not assume we're raising prices a lot outside of the CPTs managing some of the headwind. So that's sort of where we're at. We're pulling every lever we've got. This is incredibly important source of earnings and even more important source of cash flow, and we take this business very seriously in what we're going to do.

Operator

David Begleiter, Deutsche Bank.

David Begleiter - Deutsche Bank AG - Analyst

Mark, looking at Chemical Intermediates, are there other actions or options you're looking at to reduce the earnings volatility of this business?

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

Absolutely, David. And first of all, the biggest action we're taking, we've already told you about, which is the E2P project. So we have a project to take our bulk ethylene, which is the biggest driver of earnings challenge in the segment, given how that ethylene market is challenged. And that's not a new topic. It's been a topic for us for a long time.

We have a project where we can take the ethylene and turn it into propylene and that dramatically improves the earnings in the segments. It allows us to not sell bulk ethylene, allows us to replace higher cost purchased propane -- I'm sorry, propylene and so we improve a loss

as well as reduce and eliminate the loss on the bulk ethylene, and we also improved the margins on the propylene side of the equation at the same time.

So that's worth, if you look at all the different ranges and scenarios of how the industry spreads can change, it's similar to \$50 million to \$100 million improvement in earnings and the payback on that is less than two years from a capital point of view. So that project we're driving forward as one that will definitely structurally improve the business.

When it comes to how the business also, it thrives and improves, frankly, is there's a cyclical nature of this, which is more demand-driven in the business. So the North American market is much more profitable than the export market, especially with all the Chinese dumping going on that's really impacting the market outside the US. The tariffs are helping to some degree, protect the North American markets.

So as demand comes back within the segment in North America and building construction durables, et cetera, that's a big mix upgrade. Also remember, more than half of the product we make in this segment goes into our specialty. So as demand recovers there, you're replacing very low-value exports on the margin with much higher value specialty sales. So that also helps improve the stability in the earnings when we get back to a more normal demand situation in the core CI business.

Of course, there's the broader question around the overall market and how it gets better with the current pricing and a lot of the products out coming out of China right now, the cost models we have, they're at their variable cash costs. We don't know how long that's sustainable, that's certainly impacting high-cost assets around the world, especially in Europe, South Korea, Japan.

So you see assets are going to get rationalized. I'm not about to guess what the time frame is on that relative to how China is adding capacity. But I do think the market structure around the world will continue to get better over the next few years. We're not banking on any of that this year, to be clear, with the uncertainty that's in the current market situation. But there are a lot of actions we're taking to improve this business in long term.

David Begleiter - Deutsche Bank AG - Analyst

No, very helpful. And just on Q1, can you help us with the bridge versus the prior year to get to that decline you're forecasting on an EPS basis?

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

Could you repeat that question again? You were just broken up a little bit.

David Begleiter - Deutsche Bank AG - Analyst

Can you help us with an earnings -- an EPS bridge from Q1 last year to Q1 this year for that decline that you are forecasting?

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

Year-over-year decline. I just want to make sure I understood the question correctly. So as we look at where we are today, obviously, we went on a journey through last year, right? Q1 was relatively strong, and then it evolved over time to where we finished Q4. In Q1, it's important to remember, as we told you on the third quarter call, that was actually a year-over-year growth scenario, right?

So the end markets and the consumer discretionary, for example, were up 2% to 4%. And so if we had that year, we would have had growth -- normal seasonality for the rest of the year we had growth for the year. So the evolution of the market after the April Liberation Day, causing

markets to sort of go from being modestly up to down in meaningful ways, changed and altered the rest of the year. So Q1 is a tough comp because it was actually a growth quarter.

Now where we are today, I think it's much more important to think about the progression of how we've gone through the year and how we come out of the back half of this year into Q1 and build from Q1 through this year. And so when I look at where we are now, we feel good about how Q1 is progressing. I think that we wanted to and are seeing a return in volume from fourth quarter to first quarter.

So you're seeing strong improvement in volumes in AM with seasonality sort of coming back to some degree, although I'd say customers are still being cautious. We're definitely seeing the lack of destocking of pre-tariff inventory that we told you about in the third quarter call, which obviously was a big driver of the volume decline in Q4 relative to Q3, I think most of that's abated. So we're seeing good recovery in the volumes there, seeing good recovery in the volume seasonally in AFP, as you would normally expect.

We've already talked about volume recovery being a bit modest in Fibers and we'll build through the rest of the year. And even CI is going to have volume recovery as a function of just less shutdowns, so more volume to sell as well as some of the seasonality and destocking that was pretty aggressive in CI abating.

So overall, we feel like we've got a meaningful amount of volume recovery coming our way. I wouldn't -- it's by no means taking us back to last year, Dave, but it's making good progress from where we were in Q4.

On top of that, you've got utilization benefits that come with the volume and some of the cost benefits and actions we're taking that continue to build as we go from the fourth quarter to the first.

There will be some offsets. Obviously, energy costs are higher even in a normal period before we get to the winter storms. We expected energy headwinds in our guidance. And we expect prices to be a bit off in CI with some contract resetting. And then Fibers, as we already told you, we'll have a modest decline in price.

So when you put it all together, we feel good about that guidance and starting the road to recovery. But all the things we're doing that we've talked to you about build over time, right? The innovation builds over time, circular builds over time, cost reductions build over time. We're assuming we get back to normal seasonality, which will certainly help Q2 and Q3.

So while Q1 is not where we want to be relative to what we think is possible for the full year, we're really encouraged to see the strength of the recovery out of Q4, and we see a lot of levers on how we can build and improve and deliver a strong meaningful earnings growth for the year.

Operator

Patrick Cunningham, Citigroup.

Rachael Lee - Citigroup Inc - Analyst

This is Rachel Lee on for Patrick. So the earnings contribution from methanolysis seems to imply maybe less than 25% incremental margins on additional volumes this year. So is this the right way to think about incrementals for some of these noncore applications? Or is there any additional fixed cost or mix drag impacting 2026?

William McLain - *Eastman Chemical Co - Chief Financial Officer, Executive Vice President*

Thanks for the question. What I would highlight is, obviously, as we think about the benefits of our circular solution for the packaging model as well as the combination of the specialties with Tritan Renew and the end markets that we're going to into those applications. To your point, Rachel, there's a, I'll call it, a spectrum of drop-through margins.

As we think about 2025 to 2026, volume growth is a key aspect of that, and we've highlighted that with the contracts that we have across a spectrum of key brands that we're growing with in the packaging space and that being the substantial driver.

So as you think about that growth rate, what I would say is, for the fixed or I'll call it the -- the model that we've talked about for packaging, where we have volume commitments as well as cost pass-through, we believe that, that is reasonable outcomes and delivers the returns that we've been talking about.

What we will also have is upside to that as we have additional mix upgrade and sell into our specialty markets. And as we get momentum in the consumer discretionary markets over the long term to drive those returns that we've committed to previously in the circular economy.

Rachael Lee - *Citigroup Inc - Analyst*

Great. And I know you haven't guided to fiscal 2026 for the full year, but given your expected growth across AM, staple, and AFP. Can you help size your latest view on your price cost trends for your specialty businesses in 2026? And just one follow-up there, you often talk about defending your value of your products, but now it seems like you're giving some price back in AM. So I guess what's driving that?

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

Sure. So it's -- there's a lot of that question, right? So I'm going to try and answer as best I can. Just to start off with around sort of how we look at 2026 and think about it, we're very clear that the macroeconomic scenario is highly uncertain. I think everyone is pretty much in the same bucket.

And so we're not trying to call the macro economy. The biggest driver of our company in earnings and performance and cash is volume. And that's been true for the last four years and it will be true for this year. But right now, we're assuming the markets and our planning scenario are relatively stable to last year. And then what are all the different things that we can do to drive value.

And so we start with the focus on cost reduction since that's immediately in our control. And as you've seen, we delivered \$100 million, which was \$25 million over our target. Last year, great momentum and that we think we can get another \$125 million to \$150 million on top of that. That's \$225 million to \$250 million in two years, which for our size of the company is pretty significant and really demonstrates our accountability to our shareholders with a great value in challenging times.

But the biggest thing is around growth, right? So we have lower costs and a lot of that cost will flow into Advanced Materials, then it's how do we grow volume. And on the volume front, there are several things that we're doing that are more in our control than waiting for the macro economy to get better.

First and foremost is always innovation to create growth above your underlying markets. The cellulosic -- I'm sorry, the circular economy in polyesters is a key example of that, that incremental \$30 million of improvement over '25 is significant with a revenue growth of 4% to 5%. A lot of it being driven by the rPET customers that we talked about in the third quarter that are already ordering and ramping up with us in the quarter.

So we feel very good about that and building -- starting to build in Q1 will create more value as we go into the rest of the year. You've got the classic innovation in the films business with HUD in luxury cars and EVs growing around the world. You've got the EastaPure, ultra high-purity solvents in semiconductors in AFP.

We have all the cellulosic growth I just talked about and how we're trying to drive growth in the Fibers business. We're also expanding our aperture and how we think about volume growth across the company, but especially in Advanced Materials and in Fibers is how do we target these applications that are outside of our normal core specialty businesses.

You don't really want to aggressively go after market share in your high-value products because you just erode your value in those applications in a weak market, that's a bad choice. You want to win on your value proposition, you want to maintain your margin. So we're targeting areas where we can grow, that adds volume and utilization to the overall cost structure of the company.

One we've already done, which is we gained some of our architectural interlayers where we lost some share last year. As I talked about, we're doing the staple product in fiber to drive growth. We have the Aventa. We also in polyester, just with the actions we're taking in our core business have a lot of volume growth already but there's still space to look for more volume.

So we're expanding some efforts in some markets like heavy gauge sheet and shrink packaging, where the margins are not as high as Tritan, but they're still attractive and allow us to drive asset utilization.

So how do we really ramp up volume and utilization and leverage that cost reduction altogether. And the segment that will for sure benefit the most from these actions is in AM. Now to your question around prices, there are some price declines. We already mentioned Fibers and CI. In Advanced Materials, we do expect some modest decline in there too, as we share our raw material costs advantages.

We can't offset energy headwinds in this market condition and our competitors are outside the US, but we certainly have done a phenomenal job of managing our price relative to our costs over the last four years. But after you get it in four years of doing a great job, you have to start sharing some of that raw material benefit with your customers. And so we're doing that.

But in the context of the volume growth we're getting, the overall variable margin is increasing. So those are all the actions that we're taking to try and drive value and create very meaningful earnings growth for the year.

Operator

Vincent Andrews, Morgan Stanley.

Turner Hinrichs - *Morgan Stanley & Co Ltd - Analyst*

This is Turner Hinrichs on for Vincent Andrews. I'm just wondering if you could help with some of the bridge items for advanced materials ex methanolysis? I believe that you've commented that innovation reversal of the asset utilization headwind from last year and FX or tailwinds, while you should see some price cost headwinds. Curious if you could provide some more color or help put a finer point on what you might see on a year-over-year basis in that segment?

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

Yes. I think I just hit on a lot of it just in the last answer, but the great thing about Advanced Materials this year is it's got a lot of leverage to work with, right. So, to grow earnings this year relative to last year. The first and foremost is that volume growth, right? It's volume growth delivered by circular, which is one of the bigger drivers. It's finding volume growth in weak markets through our innovation and on the levers that we're trying to pull there.

So you've got some core recovery and you got circular. On top of that, you have a good portion of the cost reduction flowing into AM that is part of that overall corporate program. You've got the largest amount of utilization headwind last year with the aggressive inventory actions we took in managing Advanced Materials. And so as these volumes come back, we start getting a meaningful tailwind on utilization in this segment. And then you do have some FX tailwinds and benefits as well.

So when you put all those four levers together, they're quite material. Now there are some offsets like a bit of higher energy costs this year, that modest price decline I just mentioned, relative to the energy cost. And then you've got the -- I just forgot what the other part was, -- the other headwind is -- that's it. I don't think there's another headwind. Oh, variable comp. That was it, variable comp is the other headwind.

Operator

Aleksey Yefremov, KeyCorp.

Aleksey Yefremov - *KeyBanc Capital Markets Inc - Analyst*

Just looking at various bridge items you provided for this year was sort of crudely came up with about \$5.50 to \$6 in EPS. So I wonder if you could comment if that range is close to what you were thinking?

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

So I never imagine getting that question. So look, as I already said, the macro economy is incredibly complicated right now. There's a lot of uncertainty. In that context, we're taking a huge amount of actions that are in our control from costs to trying to create our own volume, leveraging asset utilization and certain things like FX, that's a tailwind. So there's a lot that helps.

Clearly, there's a few headwinds. The rate at which CI recovers from last year and how we moderate and stabilize the Fibers business as well as things like variable comp going back to 1x. So when you put it all together, we've said there's a meaningful improvement in earnings that's possible.

What I would say is when you think about the sort of upper end of what you're talking about around \$6 a share, that's very much in the range of what we're thinking as possible. But I have to emphasize there's a wide range here around what could happen. And it is macroeconomic that we're talking about and where the uncertainty is.

If you look at GDP and everyone's talking about how great GDP is and it's growth last year were expectations of this year. If you back out data centers, AI, health care, GDP is sort of flat. And the consumers, I think, has been well understood through last year, especially the 80% of our consumers out there are really struggling with the economic challenges they have and the affordability, the fear of what tariffs are going to do, fear about can I get a new job if I lose mine, et cetera.

So there's a lot of caution out there that's been there for the year, all last year. I don't think it's materially changed. That's why we think the economy could be stable. But it's challenging out there. And there's any number of things, geopolitical works, et cetera, that could make things worse.

On the flip side, there's a lot of potential upside here too relative to sort of that \$6. Right now, demand has been incredibly weak since 2019. We've told you housing, and you all know, total home sales down 20%, not just here, but in Europe, China is worse. You've got consumer durables down 5% to 15%. You've got cars barely getting back to 2019 levels.

A lot of pressure in accessories in the auto market because people can barely afford the car. There's a lot of pent-up demand since 2019 to now, not to mention normal market growth being missing, that can recover at some point when consumers get confident and stable.

And especially for the US economy, more than China and Europe, I think the current administration is very focused on getting the economy to grow for the consumers, not just data centers and health care because the midterms are coming up. And so lower interest rates, obviously, will help a lot of the tax policy may get more money into the pockets of that 80%. There are a bunch of housing policies that they're considering that could be helpful. So I'm very hopeful that they take those actions and the consumers get healthier and buy more, and that would be upside.

So we're very focused on controlling what we can control, very aware that the economy could go any direction, so we're not going to take our eye off the ball and everything that we can control. But there's just a lot of uncertainty. And right now, we're just focused on making sure we get a good start to Q1 and build from there.

Operator

John Roberts, Mizuho.

John Roberts - Mizuho Securities USA LLC - Analyst

It wasn't very long ago that you had a young chick featured on the cover of your slides. What's going on with the ag products you're just continuing?

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

We had a couple of Crop Protection products in Europe that had a regulatory ban going forward so we had to stop selling them. So that's what happened. It's just a European specific thing, but there were profitable products, and we felt the impact. We will see it to impact this year.

John Roberts - Mizuho Securities USA LLC - Analyst

Maybe I could get a second one then. What's going on with the decline that you cited in rPET from mechanical recycling?

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

Decline?

John Roberts - Mizuho Securities USA LLC - Analyst

Decline in quality. I think you cited (multiple speakers) rPET.

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

Yes, yes, absolutely, John. So the decline in mechanical recycling quality. What happens is -- and we've been -- we've known this from the beginning of our platform and why we're so excited about chemical recycling is, mechanical recycling has a major flaw, which is when you melt plastic, you break down the bonds of the polymer chain every time.

And as you do that over cycles, the polymer integrity chains get worse and worse. And so the quality of material degrades, and you get impurities also in the polymer because you have to remember, mechanical cycling has no purification.

So you take waste plastic, you select the cleanest, clearest bottles you can find in the plastic waste stream and then you wash them and then you chop them up and then you melt them back into pellets. So there's no purification.

So also if there's any contaminants in that bottle, it doesn't necessarily get removed from the polymer. So the polymer starts to get yellow, it starts to get gray. You will see that on the bottoms on the shelf that's already starting to show up. You also have some integrity issues around the strength of the polymers. So if you're stacking cases, the bottle will start to collapse a little bit.

And so there was always a belief that in understanding that the mechanical integrity would degrade with mechanical recycling. And they thought it would take many years before that impact would actually show up in the polymer, and it's showing up a lot faster. It's already showing up.

And that really confirms our value proposition because we have none of those problems, right? Chemical recycling, we -- as we told you, before we unzip the polymer back to the building blocks, we have a big purification step.

So the intermediates that we produce out of it that we then turn back into a polymer are perfect. They're exactly the same as virgin. In some cases, we're finding it's actually -- has a little bit better clarity than a virgin polymer. So -- and we can do this infinitely like aluminum.

So we are really the long-term solution in chemical recycling. Mechanical is a good thing to do and it's energy-efficient, but its yield is incredibly low because -- they can only clean up 25% to 35% of the really clear bottles. The rest of it gets downgraded into low end markets or landfill. That's why long term, we're very confident about the value of this whole platform having a lot more demand, and it's already being confirmed with our customers now recognizing how much our quality is better.

And that's why you see some volume being pulled forward with Pepsi and some other brands into buying our bit from us next year -- nothing this year relative to when the second plant was going to come online.

Operator

Frank Mitsch, Fermium Research.

Frank Mitsch - *Fermium Research LLC - Analyst*

Mark, I wanted to get a sense -- I wanted to get your sense of where you think inventory levels are at your customers. Obviously, you spoke a little bit about the volume decline that we saw in 4Q, kind of reminiscent of the great destock back in '22, '23. So I mean you might make the case that inventory levels have to be bone dry at your customers, but I'm curious as to what your thoughts are.

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

So I think that a lot of very painful lessons were learned back in '21 and '22 when customers and the retail channel massively overbuilt inventory. And then demand corrected, obviously, with inflation, interest rates, et cetera, and people got caught holding on a lot of inventory that took a very long time to destock.

I would say this year is very different or 2025 was very different than '23. First of all, people learned their lesson and we're not building inventory for some expected high growth scenario. Everyone was at the beginning of '25, pretty cautious about the economic scenario for the year.

So customers and retailers were being disciplined on that. Now what was different was April changed everything, right? So when the tariff trade sort of situation escalated, that caused everyone to go into action mode to try and mitigate their exposure and they bought more than they needed for the moment where they were trying to get ahead of those tariffs. And then demand slowed down a bit, as we described from Q1 to Q2 with the consumer.

So you ended up with some excess inventory, not just for us because we were doing the same thing, building some volume with the expectation of modestly improving sales in the back half of the year, and obviously, that didn't happen. So we had to do our own destocking in Q3.

Same was true of our customers, right? They were sitting on more inventory than they needed with the consumer demand not improving materially and had to sort of take action on reducing that inventory. But the inventory levels they started with were much lower than where we were back in '23. And the change in end market demand is not significant, right? End market demand has moderated a bit. But it didn't sort of collapse like it did in the back half of '22 and '23.

I think the other test of it, Frank, is back then, we had a huge and difficult Q4, where volume really dropped and then it dropped even more in Q1 of '23, right? Whereas now we see orders picking up in January, February relative to last fourth quarter, right? So that also gives me that comfort that they wouldn't be ordering more right now if they hadn't managed their inventory.

Frank Mitsch - *Fermium Research LLC - Analyst*

Okay. Got you. Okay. And so that feeds into my next question. I'm trying to just reconcile a couple of different items related to this. The asset utilization headwind in 2025 was \$100 million, running your plants lower because of -- because you want to meet demand. So that's \$100 million negative in '25.

Now for '26, you're guiding \$25 million to \$50 million benefit from utilization, lower shutdowns and volume growth. So it's \$25 million to \$50 million for that. Is that directly comparable to that \$100 million negative for 2025 and is also the \$20 million benefit from lower maintenance in '26 versus '25. So if you can reconcile those numbers, that would be very helpful.

William McLain - *Eastman Chemical Co - Chief Financial Officer, Executive Vice President*

All right, Frank. Just at a high level, what I would highlight for you is, as Mark just highlighted, we had to do some of our own destocking. So first half to second half, we basically had \$100 million headwind as we look at the way we run our plants, the demand that we had in the first half and with the tariff, I'll call it, initiated pre-buying ultimately in the back half as things got more cautious, we turned our plants down to deliver the \$1 billion commitment that we made on cash flow.

As you think about on a year-over-year basis, we highlighted in '24, we actually built inventory as we were planning for the strategic transitions to serve our circular economy footprint, including the rPET, and we built inventory in advance of the transition.

I would say our Advanced Materials business did a great job of bringing that inventory back down, but it was really the build of inventory in '24 and the implications. So that's why there's a more modest utilization tailwind as we go into '26 from '25 is it's really those lower planned turnarounds as well as the benefit of not planning to build or deplete inventory. We expect to hold it pretty stable in our baseline assumptions starting the year.

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

The other thing I'd add is, we have plans to drive a lot of volume growth in the things that we can control. We're appropriately cautious like everyone else in the industry right now, but with the underlying market demand is going to be. The demand is stable.

We can deliver on all the volume that we're trying to achieve. The tailwind is going to be more than \$25 million to \$50 million of utilization benefit for this year. But we need to prove all that, right? So we're going to be a little conservative on how we think about that number until we see all the volume come together.

William McLain - *Eastman Chemical Co - Chief Financial Officer, Executive Vice President*

And also, just as we highlighted on Advanced Materials and while we -- the reason to believe, obviously, a large portion of the benefit will show up in Advanced Materials from utilization.

Operator

Kevin McCarthy, VRP.

Matthew Hettwer

This is Matt on for Kevin McCarthy. Could you size the opportunity for your high purity solvents in the semiconductor end market within Additives and Functional products? What does that growth rate look like? And how do the margins compare to the rest of the segment?

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

The high purity solvents is a great business. The margins are definitely above segment average in that business and it's always great to be connected to semiconductors right now and being on that growth. It's not a huge product line and we don't break out those kind of numbers in our portfolio. But it is a meaningful contributor to sort of how to drive earnings growth, how to offset some of these discontinued products as we think about how we keep AFP stable this year.

And the growth rates are higher in the 20%, 30% range and how we're growing it, but it's not a huge number when you apply that 20% to 30%. So don't go overboard in how you think about it. But it definitely is helpful as we think about that lower HTF sales and a couple of the discontinued products being a headwind this year and -- I'm sorry, in AFP and how we offset it.

Matthew Hettwer

And then in your prepared remarks, you mentioned that the EPS guidance you gave for 1Q does not include the impact from winter storms. And I appreciate that's hard to predict, but could you maybe give us an idea of how you're thinking about that, given how the winter has progressed so far?

William McLain - *Eastman Chemical Co - Chief Financial Officer, Executive Vice President*

To your point, it's too early at this point. We still have freezing temperatures here in Tennessee as well as our site in Longview, Texas. And there's more snow that's getting ready to come. We've seen limited impact on our facility so far. As you might expect, I'm sure you've been watching the natural gas markets.

So the main impact is on the energy and natural gas. And where does that actually play out and influence. As Mark highlighted, we expected the higher natural gas in Q1, but this could also be an additional tailwind. Ultimately, we're taking actions to ensure the safety as a headwind in addition to what we had already forecasted.

We're taking actions on sort of the safety of our team members and reducing rates to also limit the amount of natural gas headwind that would come from this event. And obviously, we have a hedging program, and we're -- about half of that is hedged as we go through the quarter. We will provide, I'll call it, more information as we talk to you throughout the quarter.

Operator

Salvator Tiano, Bank of America.

Salvator Tiano - Bofa Merrill Lynch Asset Holdings Inc - Analyst

Yes. So firstly, I wanted to go back to the fibers volume. I know it's been a pretty long discussion, but I still do not really understand getting that, obviously, the textile part was down a lot, how given the volume bands in tow the volume was down 19%, setting aside the EBIT that you addressed in the first question of the call. So what are typically the volume bands in your contracts? Like is the minimum actually 20% below, for example, the normal level?

And secondly, as we think about this year's volume, you do mention in the call that you secured flat volumes year-on-year, but there will be continued destocking. So I don't really understand what that leaves us on a net basis for the Fibers volume year-on-year. Should we just assume flat? Or does this mean there is a risk to the downside?

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

On a full year basis, you should assume that the tow volumes are stable last year. So that -- just to get that question on the table. And then we have some volume growth we're pursuing in textiles on top of that sort of stable volume situation. The way you think about the contracts last year relative to the contracts we have this year. So we started the year last year with volumes that were obviously better in Q1 and then they were became less each quarter.

Q1 started largely with customers buying in their contract ranges, but not all at the bottom of the ranges. And that's where the volume sort of was sort of normal in that sense, outside of a couple of things that we started the year with under destocking, but a lot of customers were normal. And then as the year went on, more and more people started taking actions and going to their contract minimums to try and destock.

And we had also had some growth commitments from a couple of customers last year that was -- that they had plans on assets in the ground. They were buying the volume for their growth, that they thought they were going to have and winning some share from some competitors and that growth didn't materialize for them.

So suddenly, they're sitting on more material they needed and started but really reducing their demand, too. And that's sort of how the volume evolved to where we were, where most people are focused on destocking at the end of the year.

So in that context, we then sort of pursued and achieved a bunch of contracts that have volume ranges to them. And when we look at those contracts that we have in place now and the actions that we've taken, we believe, on an annual basis, the volumes when they're at their minimum will be stable to the volumes we realized last year.

But those contracts, while they're volume commits on an annual basis, they're not -- they have flexibility quarter-by-quarter and how much they buy in the annual commitment. And so they're modestly lower in Q1 on their commitments. So they have to buy a bit more to stay in their contact zone as we go through the year which also coincides with, I think, less destocking that they need to accomplish this year relative to last year.

Salvator Tiano - Bofa Merrill Lynch Asset Holdings Inc - Analyst

Okay. Perfect. That's very helpful. The other thing is a little bit on the variable compensation. I mean you are walking a tightrope trying to make sure that earnings will grow this year, as we said in the guidance -- in the outlook.

So -- and you're cutting costs by, I believe, over \$300 million in terms of the gross cost reductions, right? So in this context, why would the variable compensation will be such a big headwind? Then I guess if you do not deliver on earnings growth because of whatever happens in the macro environment, how should we think the headwind -- like will the the variable comp be a headwind? Or could it actually end up being neutral year-on-year?

William McLain - *Eastman Chemical Co - Chief Financial Officer, Executive Vice President*

So what I would highlight is, obviously, as we set out with our business plans in 2025, the expectations at the start of the year were much higher than what was realized. Obviously, we reset commitments, but the plan was in place and we're accountable to shareholders for that plan. As a result, you're going to see lower -- there's lower variable comp expense in our P&L in 2025 and there will be lower cash payments here in '26 for those plans.

As we're resetting the business scenarios that Mark's outlined today, we expect to deliver on those. And if we deliver that stable cash and also deliver on all the actions, net of some of the headwinds, we would expect that the variable comp would reset and would be a headwind year-over-year of about \$50 million to \$75 million, depending on where we see those scenarios play out.

Operator

Jeff Zekauskas, JPMorgan.

Lydia Huang - *JPMorgan - Analyst*

This is Lydia Huang on for Jeff. How much have you spent on the second methanolysis project? And what would help you make a go or no-go decision? And are you looking for another baseload contract given Pepsi has been pulled forward?

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

So as far as the second project is concerned and expense, obviously, we've already done some engineering expense around building the facility in Texas, and then we lost the DOE grant, and we put all that work on hold. So we're not spending any money on engineering at this stage until we've lined out and developed a compelling project to be a lot more capital efficient in how we're approaching it to restart the project and go forward.

So right now, we don't have any engineering expense or headwind from a capital expense point of view. Obviously, there's a team working on the circular economy across all platforms around the globe. And we're taking that cost down to some degree, too, as we adjust the rate at which we're progressing.

But -- so that's where we're at. But I would say though, around the second project, one, we're really excited that Kingsport can be debottlenecked by 130%, which allows us to grow more from the first plant, have better ROIC from the first plant before we get to the second plant, and that's what's enabling us to be confident that we can grow the especially economic recovery and serve the rPET market with some of our customers who are coming back and wanting to buy from us a lot sooner, as I described earlier, due to the degradation of mechanical material that they can buy. So that's all really good.

And it gives us time to work on this idea of more capital-efficient second plant, which we very much want to build. And so we've got three different options going on there where we're looking at different locations and assets we could leverage that already exist that we feel very good that at least one of them will be quite viable to move forward.

But because of the debottlenecking, that means we can avoid ramping up significant CapEx around this platform this year and next. So it's a great solution to moderate our capital in a very difficult economic environment and make sure we have good strong free cash flow right now.

But keep on track with the circular platform, which we believe, is still going to be incredibly successful over time. I mean, without a doubt, people are buying a little bit slower in the specialties right now because not because of recycling just because there's a lack of demand for their products, right?

The consumer durable guys are under a lot of stress. So this all lined up and works out quite well to have a great platform, manage cash in the short term, be responsible to our shareholders on return on investment.

Lydia Huang - JPMorgan - Analyst

And is the Pepsi contract, the main contributor? And this is for the Kingsport project, is that the main contributor to the \$30 million incremental earnings in '26? Or is that later in the year?

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

So the revenue growth for the Kingsport project in '26 running '25. Certainly, there is a significant amount of revenue coming in from rPET. Pepsi is one of the contracts that we have in place. We also have several other strategic leading brands, ramping up volumes with us on rPET as well. So that is a big part of the 4% to 5% revenue increase.

To what degree the specialties play a role in the final outcome for the year? It goes back to the macroeconomic question we talked about. If the world stays stable, we expect some growth in the specialties especially in consumer durables, where Renew content we involve. We still have 100 customers committed and buying specialty Tritan Renew and some cosmetic Renew products, et cetera. They're just not ramping volumes up as much as we'd like because the economy is so challenged.

Once they start -- once you have a stable economy, that starts -- they start launching new products to try and accelerate their growth and our volumes will grow with them. So as the year plays out, we expect some of that specialty business, hopefully, will start coming in and being a bigger part of the mix, but a very good portion is rPET, but it's not just Pepsi, it's several other customers.

Operator

Mike Sison, Wells Fargo.

Michael Sison - Wells Fargo Securities LLC - Analyst

Mark, when you think about sort of restoring earnings -- Eastman's earnings power back to where it used to be, is there anything structural, do you think, in either the end markets or competition or China or something that could prevent that?

Or -- and then just a quick one on your outlook for AM and AFP for sort of underpinning the significant earnings growth. What is kind of the range of volumes that you need? I know you have a lot of that volume with new products and within your control. What's sort of the variable on the volume growth that you need to get that sort of significant EBIT growth?

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

Thanks, Mike. And yes, we spent a lot of time on this question, and we talked a bit about it at the deep dive and how we thought about getting back to what we said was normalized earnings and you can go back and look at some of that material because I think most of it is still true in what we said then to where we are now.

Without a doubt, when you think about the driver of where our earnings are today, it is primarily due to lower volume from economic demand that's impacting AM and AFP to some degree as well as CI. So it's -- that demand, whether it's high-value specialty growth in AM, very attractive growth in AFP or even just North American high value relative to exports in CI, has all been impacted by the economy.

And it's been weak, as we all know, for over four years, which is pretty unprecedented in that kind of a time frame, like 2009, 2020 were short blips, really steeped down and snap back. This is a long duration.

So as we look at all that, and I said this earlier, there's a huge amount of potential pent-up demand to recover. Cars are 15 years old. Appliances are getting to their end of life when they bought them back in 2020. The housing market being 20% down. And for us, total housing is what matters, not new builds to be clear.

The total housing, which is now down 20%, starts to recover, that's a lot of paint. That's a lot of appliances that go with people moving into a new or an existing home. And so there's a lot of upside in demand that can recover a lot of our earnings. So that's sort of the key, is that innovation, you've got the circular platform driving a lot of growth on top of a core market recovery.

And what's been impressive over the last three years, we've done a phenomenally good job of maintaining our price and our variable margins while defending our share because of our innovation, giving us differentiation.

So if volume comes back, the incremental margins, the volume recovery and the utilization benefits that go with it, I think, are quite significant to bring earnings in AM and to some degree, AFP back in a meaningful way and even help CI recover in their earnings. So I think that's all really good.

Now obviously, the structural -- so I don't think we have a structural problem in AM and AFP. We have a cyclical market demand problem. That has been our challenge. And to some degree, that's also true in CI. Now there are structural challenges in the olefins world, in the acetyls world from excess capacity in China impacting some of the chemical intermediate margins.

And there's a debate, obviously, going on in the industry around to what degree did that structural pressure change. I mean right now, we are for sure at the bottom of the market when the prices are at the variable cash cost of the Chinese. So I don't think that's sustainable. But to what degree it fully recovers, is unclear on CI.

Now with CI, when you think about it, the actions we're taking on E2P provide a big lift the margin recovery and demand recovery in North America will provide a lift. So there's a way to get the earnings back from where they are today to probably \$150 million, \$200 million in a normalized place. Now that's probably below where we were in the past, trying to reflect some of the structural challenges that we expect, but a significant improvement from where we are today.

Fibers, as we've already covered, I think, we're trying to stabilize in this year. What's interesting is if you look at the EBITDA in 2020 -- 2019 for CI and fibers together, it's around \$520 million. If you look at last year and put EBITDA together, it's about \$100 million less.

So from a structural question, which is more of a fiber CI question, just E2P can get you back to where we were in 2019 and then we have the specialties building on that. And we're taking a lot of cost out to -- \$225 million to \$250 million of cost is also coming out to offset structural challenges to enable us to get back to normalized earnings. So we still think it's possible to get back to that \$2 billion kind of number.

Gregory Riddle - Eastman Chemical Co - Vice President, Investor Relations

Let's make the next question the last one, please.

Operator

Laurence Alexander, Jefferies.

Gregory Riddle - *Eastman Chemical Co - Vice President, Investor Relations*

Laurence, are you still there? Becky, may we go on to the next one.

Operator

(multiple speakers) Laurence' line.

Gregory Riddle - *Eastman Chemical Co - Vice President, Investor Relations*

Okay. So I think that's -- go ahead. Go ahead, Becky.

Operator

No, that's okay. Sorry, I was just going to say that was our last question.

Gregory Riddle - *Eastman Chemical Co - Vice President, Investor Relations*

Perfect. So thank you, everyone, for joining us today. We appreciate your time, and hope you have a great rest of your day.

Operator

This concludes today's call. Thank you for your participation. You may now disconnect.

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