Transcription
Solvay Conference Call, 06.05.2020
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Overview

Operator
Welcome to Solvay First Quarter 2020 Results Conference Call for Analysts and Investors. Solvay team, the floor is yours.

Jodi Allen
Good afternoon, and welcome to our First Quarter 2020 Earnings Call. This is Jodi Allen, Head of Investor Relations, and I'm joined virtually by our CEO, Ilham Kadri; and our CFO, Karim Hajjar.

Today's call is being recorded and will be made available for replay on the Investor Relations section of our website. I would like to remind all participants that the presentation includes forward-looking statements, which are subject to risks and uncertainties. You may refer to the slides related to today's broadcast which are available on our website.

With that, I'll turn the call over to Ilham.

Ilham Kadri
Thank you, Jodi and hello everyone. I hope that you and your families are all in a good health and managing well through this challenging time. It has now been three months since COVID-19 started taken its toll on China. In the meantime, the virus outbreak has spread into a pandemic and is now provoking an unprecedented global economic crisis.

Today, we have eight colleagues who are infected with COVID-19 and 184 employees in quarantine down from our peak of 369. This low level from results from our good practices and lessons learned from our colleagues in China and Korea, especially the early adoption of preventive measures including, mandatorily teleworking for over six weeks now (about 10,000 employees). I wish our affected colleagues a speedy and complete recovery, and I take the opportunity to acknowledge and appreciate all of our employees for their dedication - those keeping our operations running smoothly and safely, and also those working remotely at home.

I'm inspired by the way I'm seeing Solvay's teams connect and collaborate virtually to meet the changing demands for our customers. While I had always taken pride in the hard work and dedication that exists at every level of the Solvay organisation, the last few months have been nothing short of a tremendous team effort. This crisis is bringing our PURPOSE to life faster than I could have ever imagined - to bond with our customers, to bond together as a team and to be at our best for one another.

To that end, we at Solvay are doing our part where possible to support the fight against COVID-19. There are countless examples of how we're bonding with and supporting our communities in this difficult times, and several are shown here on slide five. Our peroxide business has donated 700,000 litres of disinfectant to hospitals and more than 1 million bottles of sanitising gel. We also partnered with Boeing, a key customer of Solvay, by supplying our Radel medical-grade polymers for use in the production of face shield for healthcare workers.

We have also taken a number of actions to help navigate through this complex global health and economic crisis, and best position Solvay to return to grow when the market starts to normalise. First, we recognise that Solvay plays an important role in supplying our customers with products and services they rely on. Our technologies and chemistries were considered essential, which means we were able to maintain our global operations at full capacity throughout the first quarter, and there were no shutdowns issued by authorities. The only exception as you know was the temporary mandatory shutdown in China when the virus began.

We established a global crisis response team at the executive level that quickly mobilised and developed a strategy to monitor, evaluate and successfully navigate through the crisis situation. We had been holding daily meetings to manage the safety of our employees, prioritise our resources and take decisive actions in a timely and a disciplined manner.

Turning now to the business and macroeconomic environment. The IMF now forecasts global economic output to fall by 3% in 2020. We are entering the worst crisis since the Great Depression of 1930. The automotive industry has been among the hardest hit by the collapse in demand with global production declining 26% in the first quarter, following a decline of 6% in 2019. Many European and US OEMs in the auto industry stopped production in the first quarter. And the aerospace industry is now starting to follow suit. IATA4S latest assessments projects air passenger volumes in 2020 to contract 48%, and in the past weeks Airbus has already announced cutting their production by 30% and Boeing has made similar production cuts. As you know, these two markets represents about 25% of Solvay's sales, so this represents our biggest headwind. Our other key markets including healthcare, consumer goods, agro and food which collectively represents about 30% of sales are relatively resistant, and we are seeing more stable demand. Solvay's diversified portfolio and balanced end market exposure were strengths in 2019, and we'll continue to weather the 2020 storm - and we will build on this trend throughout any market cycle.

As you know, at Solvay, we are a long-term company, focused on the short-term. The impact facing many of our customers is unprecedented, and therefore, we must adapt many of our short-term priorities accordingly, but still keep an eye on our long-term objectives. In this vein, what hasn't change and where we have doubled down our effort, is on our cost, cash and of course, on our customers.

Nevertheless, the impact facing many of our customers is unprecedented. And we have had to adapt many of our near-term priorities accordingly.

I will now touch briefly on each of these objectives starting with costs.
In addition to our ongoing austerity measures, we took steps to advance our cost reduction programme, which delivered €50 million in total saving in Q1 (One-third labour and two-third indirect spend). We did this by accelerating against our existing restructuring plan announced last year; we implemented a group wide salaries freeze as from 1st January; and we reduced the indirect spend, particularly related to technical goods and services across our Global Business Units as well as general expenses.

So turning to cash. As discussed, cash generation has improved significantly over the past year, especially in terms of phasing in inventories. This continued in Q1, where we delivered record level cash generation at €202 million. This marks the fourth consecutive quarter of positive cash flow, and demonstrated that our clear focus and the related incentives are working. Looking ahead, we are even more focused on inventory level credit risk during this period.

And of our customers, in times of uncertainty, especially important to stay close to our customers. To that end, since the onset of COVID-19, the executive committee, myself included, has taken on the responsibility of overseeing progress with our key strategic customers. I'm delighted that we continue increasing the share of wallet. Here are some examples.
We're extremely proud of been involved in developing a product using COVID-19 testing. We cannot reveal many details on these new confidential healthcare applications, but we can say that our teams acted quickly to collaborate with our customer and develop, pilot and produce, and ingredient used for testing. We are also supplying technologies for a potential vaccine for COVID-19.
A second example, and aside from healthcare, we have expanded our business with Murata, who is a leading Japanese manufacturer of electronic components. Almost every piece of electronic equipment in the world has a Murata component in it, and each will have now Solvay inside.
Finally, we signed a long-term exclusive agreement with Honda Aircraft for supplying composite materials for their business jets.

So as you understand, our immediate strategic focus on our cost, cash and customers has supported Solvay's strong financial performance in Q1. We delivered greater than expected EBITDA of €569 million, essentially flat with last year's Q1. Our pricing power combined with our discipline cost management programme enabled us to improve our industry leading margins by 0.8 percentage points to a level of 23%. And our free cash flow delivery of €202 million was nearly €300 million more than the first quarter last year.

While we continue to monitor the pandemic and the impact it has across our relevant markets, we are pleased to see that our resilient businesses and focus on execution has positioned Solvay to deliver strong first quarter performance.

Before turning the call over to Karim to review our financials in more details, I want to note that the market environment we are facing is unprecedented, and will remain dynamic and uncertain. We will we continue to be nimble, and adapt quickly as the situation evolves, but we will also remain disciplined. While some of our needs and priorities may change, our commitment to our GROW strategy remains intact. We are continuing to see progress as we work to implement a strong enterprise-wide operational model, and still a performance-based culture across the entire organisation, and of course live up to our PURPOSE and values every day.

With that, I will turn it over to Karim. Karim?

Financials

Karim Hajjar

Thank you, Ilham. Good afternoon everybody. As you've seen, our reported EBITDA was stable, and our underlying post-tax profit was up over 4.5% on the back of reduced financial charges, and these profits are despite a 6% fall in reported sales.

If I turn to the business segments, I will refer to figures on an organic basis by which I mean constant scope and currency.

I'll start with materials on slide number eight. Net sales of €789 million were down 2.9% organically, driven primarily by reduced volumes in the aerospace market.

I'll first discuss our two largest markets, auto and aero, which together represent 25% of group sales. Composite Materials, as anticipated, was impacted by the production stoppage of the 737 Max programme. Sales to other commercial aero programmes were stable in the quarter whereas sales to the military sector grew by double digits in the quarter. Mitigation plan, which were already underway late last year were deepened and accelerated early in the quarter, and helped to offset the 737 volume decline to maintaining EBITDA levels.

Specialty Polymers sales were essentially flat versus Q1 2019. Our high-performance polymers used in auto were up 2% versus Q1 2019, and that outperformed the market in the context of LMC light vehicle world production estimates being down 26% in Q1 this year. Part of the outperformance relates to further penetration of our technologies into specific areas such as electric motor components and turbo chargers. And we believe also that some of the outperformance could have resulted in higher inventory levels in the industry. Other markets prove resilient, including consumer goods and healthcare, electronics, and together these represent about 17% of group sales, and together they were resilient.

Taking a step back, overall, EBITDA for Materials were down 5% organically to €228 million as a substantial cost measures and price support helped to mitigate much of the aero volume decline. It's also important to note that costs in Specialty Polymers were €25 million higher in Q1 this year related to the accounting effect of reduced inventory level this year compared to last year. Despite this accounting effects, we were able to deliver solid EBITDA and margins of 29% only half a percentage point below that of last year, and up sequentially against Q4 last year. So, overall in these circumstances, a strong quarter for Materials.

Moving to slide nine into the Chemicals segment. Sales declined 3.2% organically to €800 million. In Soda Ash, sales were down 4.2% due to lower demand in building and construction, which represents 8% of group sales. Other markets including container glass, detergent and healthcare partially mitigated the decline, and prices remained stable overall.

Peroxides performed well with sales of €172 million in line with last year's level. The business saw good demand in traditional pulp markets including tissue products and disinfectants. Pricing power combined with cost discipline enabled us to maintain a strong bottom line performance in the quarter.

The remaining businesses in the Chemicals segment, namely are Silica and Coatis businesses were stable with organic sales levels similar to the first quarter last year. Overall, the Chemicals segment continued to demonstrate intrinsic resilience with EBITDA increasing 5.4% organically to €239 million thanks to the combination of solid demand, improved pricing and operational excellence. And together this translated into 2.5 percentage point increase in margins, which are now at 29.8%.

Turning to the Solutions segment on slide 10. Net sales declined 6.5% organically to €883 million.

I will begin with oil and gas, which is one of the most challenging markets, but now represents less than 5% of group sales. We've all witnessed the unique developments over the past few weeks, and that was on the back, I remind you, of an already very difficult period in the industry since the middle of 2019. The dramatic fall in demand has led to an oversupply of oil and gas, and our customers are significantly impacted. Now, we had already initiated a strong turnaround in the third quarter of last year, including restructuring our business, cutting costs, and fundamentally aligning our value proposition to the change market environment. Our team has already reduced the cost base substantially, and they're focused on bringing solutions that address the new needs of their customers. Our exposure to other end markets in Novecare, such as home and personal care, agro and coatings, altogether represent about 30% of the group, and about half of Novecare sales. And demand in these markets was resilient, and this led to slightly higher sales year-over-year despite some impact from the shutdowns in China. This strength helped to partially offset the oil and gas headwinds.

Turning to Technology Solutions, sales were down just over 2%. Mining, the largest market in this business, sustained good demand as most of our key customers were still operational. And this helped to offset weaker conditions in other industrial and auto markets. Special Chem sales were slightly down but strong demand for semi-conductors helped to offset weaker demands in thermal insulation. Aroma sales were up 9%, thanks to higher volume and pricing from natural vanillin ingredients which are used in food and in fragrances.

Taking a step back, overall, the Solutions segment EBITDA was down 4.3% in the quarter with stable demand across a variety of markets combined with strong, very strong, cost control measures helped to partially offset the headwinds of oil and gas. In fact, EBITDA margins were improved 0.2 percentage point and now stand at 17.4%.

Moving to cash management with slide 11. As Ilham mentioned, the strong Q1 free cash flow performance is almost 300 million above Q1 last year and was fundamentally driven by a group-wide focus on cash. But I'm going to focus and highlight three particular factors.
One, is we continue to see the benefits of a sharper focus on working capital intensity and on saving, and we began to see that indeed in second quarter of last year. But way of example, our inventory levels in Q1 this year were €162 million lower compared to Q1 last year.
Two, we had a tax gain of €65 million cash associated with additional voluntary pension contributions following the receipt of proceeds from the Polyamide divestiture.
Three, as you know, we decided to curtail capital expenditure during the quarter and already benefited from lower cash spend of €15 million in this regard.

Now, I turn to slide 12. In April, we increased our committed undrawn credit facilities by €750 million to take the cumulative total to €3.25 billion. On top of that, we have cash and cash equivalent of €0.9 billion at the end of March. We have no financial covenants and very low refinancing risk indeed because our next maturity is a hybrid bond of €500 million with a coupon of 5.12% and a first call date of June 2021. So, whilst we acknowledge that we see that credit rating agencies have been taking rating actions on a large number of chemical companies, we do note Moody's recently affirmed our credit ratings at Baa2 albeit with a negative outlook.

Turning to the topic of pensions I will highlight that we made additional voluntary contributions to several plans.

In Q1, we made a total of 460 million contribution in France and in the US, and I remind you that this is on top of the 140 million contribution in the UK in December 2019.
These total contributions amount to €574 million and they will use for annual pension cash spend by over 60 million a year beginning this year.

So, in short, you have seen that over time, our portfolio has proved to be strong and resilient. We are delivering consistently strong cash generation and, indeed, we are tackling to most structural pension issues that had previously weighed on our cash generation. And as I had explained, we have a strong balance sheet with ample liquidity reserves and low refinancing risk. So, it shouldn't be a surprise that Solvay's board approved management's recommendation to continue with a final dividend proposal of €2.25 per share at the annual general meeting on the 12th May next week.

And with that, I'll hand you back to Ilham to discuss the environment in the second quarter and to provide her closing remarks. Ilham.

Ilham Kadri

Thank you, Karim.

So, despite our strong start for the year, there remains significant uncertainty around the extent of the impact with COVID-19 will have on our business. We are staying close to our customers to understand and quickly meet new demand patterns across our markets as well as manage our inventories and align our operating rates to new levels. To that end and as previously announced, we have withdrawn our full year 2020 guidance originally provided on 26th February. We would provide you with a better view of the full year once market visibility improves.

While we do not believe that we can reliably forecast financial targets at this time, we want to provide you with directional colour on early trends we are starting to see as we enter the second quarter. We saw markets decline in sales in April and our order books for May and June indicate further deceleration and this is what we concern that we expect Q2 to be substantially lower. Indeed, we are seeing pronounced declines in aero, oil and gas and also and softness in pulp and paper and in construction as flat glass produces are shattering capacity.

As these trends continue to unfold, we will continue to make quick informed business decisions with our three immediate priorities in mind. Based on the trends we have decided in early April to immediately implement additional actions to address the changing environment.

First, we are adapting capacity to align with the reduced demand in particular in challenged markets such as oil and gas, also in aero. In doing so, we will maintain higher utilisation rates and reduce unit production costs. As of the end of April, approximately 10% of our global sites were idle and we also had a significant number of sites running well below normal operating rates. We will continue to monitor the situation and further align our productions to demand.

Second, we are reducing staff temporarily. Effective 4th May, we implemented furlough that impacts around 5,000 employees in industrial and administrative sanctions globally.

Third, we applied strict capex management; and as previously announced, we reduced our full year capex plans by €250 million.

But let me be clear, we are prepared to resume these plans when our customers need us.

As you know, Solvay has lived through many market disruptions in its 156-year history. And while we don't have visibility into how markets will evolve, we remain confident in our ability to manage our business to this near-term headwinds and position the company for success across a range of post-crisis scenarios. Our strong diversified portfolio coupled with our financial flexibility and the additional structural actions underway will enable us to emerge a stronger, more resilient company that is well-positioned to unleash our full potential.

Before I close, I want to remind you that we put in place a Solidarity Fund to support our employees and their dependents who may experience hardship due to the impact of COVID-19. The fund will be a charitable entity, administered by the King Baudouin Foundation. We launched this initiative a few weeks ago because we care. It truly exemplifies one of the key pillars of Solvay One Planet and ESG goals which is to improve the quality of life of our employees and society at large.

In addition to senior leaders and the Chairman of the Board, I'm very encouraged by our non-executive directors and the many Solvay employees and private shareholders who have indicated an intention to contribute. More importantly, I take the opportunity to note and appreciate our reference shareholder SOLVAC for their commitment to contribute a minimum of €10 million up to €24 million to the solidarity fund. I also learnt that around 200 investors have also decided to contribute funds and currently is around €2 million. And I'm hopeful that this figure will increase in the next few weeks.

We encourage all shareholders to contribute towards this important goal. Indeed, we consider this to be a concrete example of a truly responsible capitalism. And with that, thank you very much. Karim and I will now address your questions.

Q&A

Jodi Allen
Thank you Ilham and Karim. Before we start the Q&A, can I kindly remind you to limit yourself to one question only to allow time for all participants? And now I'll hand it over to our moderator.

Operator
Thank you. Ladies and gentlemen, if you wish to ask a question by phone, please press 01 on your telephone keypad. We have a first question from Markus Mayer from Baader Heleva. Sir, please go ahead.

Markus Mayer
Good afternoon, Ilham, Karim. I've two questions. One question, first but then I'll ask one more later on. With the full reporting year guided for an expected COVID-19 effect of around 25 million, was actual impact larger or smaller than you've expected, can you quantify its effect?

Ilham Kadri
Markus, good to have you with us. So the question is about our COVID-19 impact in 1Q, right Markus?

Markus Mayer Baader
Exactly, exactly.

Ilham Kadri
Yeah. So you may remember, Markus, and you know, my promise to most of you is to be open and transparent as we possibly can when we have the most accurate current and relevant info in hand. We guided February that the impact of COVID-19 in quarter one will be €25 million and we ended up at €20 million. So not bad, right, you know, taking into account this situation. The impact was mainly in reduced volumes in two segments, mainly in solutions and in chemicals. And main markets were, you know, mostly around the oil and gas, some silica, some Coatis, some Novecare. You may remember that we had a mandatory shutdown in China for two weeks, right, the impacts we cite.

Having said that, COVID-19 in China and Korea had another phase and what we experience today in Europe and the US. I must say, you know, the authorities have been really quick and clean and really transparent about the times of the shutdown, the rights, the return to work. As you know, we had no operations, Solvay had no operations in the Hubei province and that also made us extremely agile to come back to work very quickly. So we made 20 for 25 million estimate.

Jodi Allen
Thank you.

Ilham Kadri
Thank you.

Markus Mayer
Okay. Very helpful, thank you.

Operator
Thank you. Next question comes from Laurence Alexander from Jeffries. Sir, please go ahead.

Dan Rizzo
Hi, this is Dan Rizzo on for Laurence. Thank you for taking my question. How does the down – the current downtrend effect – I'm thinking about the longer-term targets, should we think about the targets as more directional at this point?

Ilham Kadri
Sorry, Laurence, we couldn't hear you very well. Could you repeat please and maybe…

Dan Rizzo
Hold on a second.

Ilham Kadri
Yeah.

Dan Rizzo
Maybe that's better. This is Dan Rizzo for Laurence. I was just wondering how the current downturn is affecting the thinking about the longer-term targets. Should we think about those targets as more directional at this point?

Ilham Kadri
You are talking about the midterm targets?

Dan Rizzo
Yeah, I'm having a bad connection here. Sorry about that. I was just wondering about the long-term targets. Are they still achievable or is it more directional at this point?

Ilham Kadri
Okay. So I guess you talk about 2024 targets, right, and are they at risk, right, Laurence?

Dan Rizzo
Yeah.

Ilham Kadri
Yeah.

Dan Rizzo
I think.

Ilham Kadri
Probably, the connection is not good from both ways probably. This is a good question, Laurence, but as you have noticed, Q2 and full year 2020 is still unclear. It was Dan, basically, right, not Laurence, so hi Dan.

As I said Dan and Laurence, we are a long-term company that is right now focused on the short-term priorities. There is no long term without the short-term. Today, we are not withdrawing our mid-term guidance. When we have more visibility, we will come back to you in due time. It's clear that if the economic crisis resulting from the pandemic lasts longer and deeper than what we can all see right now, this could put these targets at risk.

But whatever recovery shape you wish to assume. And I'm not going to serve you as a soup of alphabet between the V, the U, the prolonged U or the L or the W, right. I mean, the V is probably is ahead (?) for many regions. What I can tell you is you can count on us, on Solvay people and employees and on me personally and the executive committee to make progress executing and delivering our plans which will still grow with the key fundamentals, and I believe that this crisis is actually threatening the fundamentals of it and do whatever we can to serve our customers. Thank you for the question.

Dan Rizzo
[Inaudible].

Operator
Thank you. Your next question comes from Mubasher Chaudry from Citi. Sir, please go ahead.

Mubasher Chaudry
Hi. Thank you for taking my question. I had a quick one on working capital. As I can see, a large portion of the inflow was from other current liabilities. Could you just provide some colour as to what those relate to, please? You mentioned the 5,000 employees are in furlough, are you relying on any government schemes for those employees while they are in furlough? Thank you.

Ilham Kadri
The first question, Mubasher, was around working capital. Again, I think the line is very bad here, my apologies.

Mubasher Chaudry
Sorry. So the working capital inflow for the first quarter, a large portion of it was coming in from the other liabilities.

Ilham Kadri
Yeah.

Mubasher Chaudry
If you could just provide some colour, as to what that relates to please?

Ilham Kadri
Okay. Good.

Karim Hajjar
Let me just look at my detail notes and I'll come back to you in one moment, Mubasher, on the specifics on the working capital because the main drivers are exactly ones that I've described. But I'll come back to you on that, on the working capital.

Ilham Kadri

Well, I mean, quickly on the working capital, because I didn't get it and we are remote. You know Mubasher that since last year, we've been focused on inventories and working capital management, you may remember that. And when I joined the company, and it's actually my first-year anniversary, my fourth quarter, I was not happy with the cash flow phasing, and part of it was due to, you know, less structured and phased inventory and working capital management. We are making progress. It's part of our growth strategy. In quarter one 2020, inventories are down €162 million or 9% year on year. We are now, because of the crisis situation, a lack of visibility, we are working closely with our customers to adapt to the change in needs, and that will help us in managing inventory level. And that's the challenge, you know, as we seek for better managing quarter two forward.

Of course, account receivables or account stables are really important. In times of risk, it's important to manage very well your receivables. With Karim and the finance team and the business unit presidents we implemented the risk management for all our customers. We have five categories. One is low risk, five is high risk, anything above three needs the signature from our, a sign off from our CFO.

So we are really looking at credits. And me personally, I experienced 08-09 and my nightmare and the pain was really on credit management. So the team hears me a lot now saying that the sale is a charity till we collect the money. On the payables, I think we are doing a better job since a year, you know, looking at how we can extend payment term, how we can have strategic suppliers with us. And I commend what the team has been doing, the procurement team across the globe on doing so.

So work in progress. We have now strategic programmes. This was part of our €350 million of cost savings programme, you may remember it, which we launched in November and we updated an increased in February. So definitely working capital, end to end value chain management in collaboration with our customers is in progress. We started with Speciality Polymers, we will move to Novecare because those are where we see low hanging fruit and we see the big impact for Solvay as a corporation.

On the furloughs, I mean, obviously, it's always painful to make furloughs, like any other, you know, action touching people. But at the end of the day here, what we are experiencing is less demand, less external activity, therefore less internal activity and that's what we are adapting. It's about operations, so operating run rate, as I mentioned it, either in capacity wherever we can do that while being very agile and elastic to rebound whenever customers need us. So, this is the trick.

Second, indeed, we are putting people on furlough but we have launched HR guidelines and protection for our people, regardless of the country of residence. And this is what you can expect from Solvay. Some of the countries have an excellent social and health benefit for people who are going to furlough, who are subject to diseases to illness during these tough times. At Solvay we have one unique guideline and we protect all our people equally, including in countries where they are not covered very well. So with those HR principles, we have announced the furlough, and we're going to adapt as the demand, you know, comes back as our customers need us back and obviously this is fluid and dynamic. So yeah, you will see us giving an update in the coming weeks.

Karim Hajjar

Maybe just to come back to your very first point, Mubasher. The working capital is exactly as we said, it's inventories receivables, very strong consistent progress. To your specific point on other working capital, it's a mixed bag of many, many other things like customs duties, VAT. And we've also been optimising and centralising a lot of those activities globally. And that's a contribution towards it. It's not the full figure, but it's a good – it's about half of it, approximately. So effectively, the optimisation covers everything to do with cash. Not just inventories, etc. But thank you.

Operator

Thank you. Next question comes from Mutlu Gundogan from ABN Amro. Sir, please go ahead.

Mutlu Gundogan

Yes. Good afternoon. One question it is. On Q1, your EBITDA ended up flat year on year, which is significantly better than your guidance at the end of February. Can you tell us why March was so much stronger than expected?
And if you allow me not so much a question but more a remark: I really liked the old EBITDA bridge. The new one is also good, I think, but we miss the volume effect, the operating leverage, we can't see the benefit from raw materials deflation, and especially as cost savings is an important part right now, we can't track besides the qualitative remarks. So would you be able to provide that on an ongoing basis?

Ilham Kadri

Yes, thank you Mutlu. I'm smiling because the simplified press release was actually, you know, a result of the comments and my on boarding tour with you guys and many who have complained that we are too complicated to understand. So we tried to simplify. So bear with us, right. Obviously, we want to be, again, as open and transparent and give you the real dynamics and the underlying, you know, performance KPIs of our business. But a point well taken.

Listen, on the Q1 performance, I think there are a few things and I'll add to what Karim and I shared. I think what this company has seen and we have been very busy the last year. For four quarters time goes fast for me. I'm first year in the company and we've been very busy in 2019 or in the past four quarters. I think we have renewed the foundation for the company to start really building up on delivering against growth strategy.

Obviously, we didn't expect COVID-19 to happen. But this, you know, renewed foundation, I'm truly a believer that it's going to help us to weather the storm in 2020, although sometimes you cannot defy gravity. And I'll remind you a few things: we changed management to focus on cash. So cash is king obviously. You heard a lot about it in 2020 and with the crisis. But we say this in quarter two that free cash flow is important. And we managed it since then. We changed the incentives of our precedents, we changed the capital and resources allocation. And frankly we are very blessed that we did it last year, not in January or in February or in March when COVID-19 started expanding from the East to West.

We stopped City Light (a restructuring program), you know. I don't regret it a second. The architectural project. We sold Polyamide on time and we are repairing our balance sheet and paying, you know, down the debt or funding pensions, which is helping us to decrease our expenses on a yearly basis.

So you know, all of this, I think there is not one, two, three. There are many ingredients and I commend the heavy work, the hard work, the intensity of it in the past year which the team did behind the scenes, and that's why you see this strong performance on EBITDA, which is indeed at the same level of 2019. I'm very proud of the free cash-flow generation.

And the financials of our business I think can deliver the liquidity debt, deleveraging goes along with the rest. And I think what we've done with Karim and the executive committee is quickly preparing for the crisis and ensure that we have enough liquidity, 4 billion. We have no covenants. The debt obviously next maturity's June 2021, as we told you. And deleveraging, you know, we did that and we will continue looking at that.

So all in all this is it. It's about, you know, now during crisis situation we embrace the reality. There is no point to deny or to think twice about that. It is happening. We can do nothing about that. And with my team we are redefining what does it mean winning. Even if the strategy is consistent, I think winning will take a different shape during crisis times than during non-crisis time. This is what I learned in 08-09 financial crisis and during the 9/11 crisis.

And then the trick, and I've been saying it, is to execute against the plan flawlessly. Now, you know, bear with me, it's easy to say, it's harder to do. Because we manage volatility and uncertainty but we are developing the muscle. And I'm very happy that I have one year, four quarters, with this fabulous team with us to really go to 2020 and its challenges. Thank you for the question.

Operator

Thank you, the next question comes from Chetan Udeshi from JP Morgan. Sir, please go ahead.

Chetan Udeshi

Hi, thanks for taking my question. I just have maybe a couple. I know it says limit of one but maybe I'll try to squeeze in two. The first question is how are you adjusting structurally to the potential that the aerospace demand may remain depressed for a long time? What can you do? What can you not? In terms of adjusting your capacity cost base, not just for temporary purposes but for say a longer period of demand weakness? That's the first question. Second question was, you know, this 50 million of cost savings that you talked about, firstly how much of that was – you know, how much of that benefit was only in Q1? And does that include the benefit from, you know, 20% of employees being on furlough? Because I think I wasn't very clear whether you are using some of the government schemes as part of the furlough or not. Thank you.

Ilham Kadri

Okay. So, Chetan, I will take the first question and Karim will take the second one. Your first one was about aerospace, right. I mean, I'm sure you have all our numbers. IATA's latest assessment, as I mentioned in my prepared remarks around air passenger volume, they expected it to contract 48% in the past weeks. Let's see. As I said, Airbus has already announced cutting their production by 30%. Boeing is doing the same. So we are reducing our production to reflect this level that customers like or, you know, OEMs like Airbus and Boeing have shared with us, right.

I remind you two things about Composites before I tell you how we're going to address the challenges ahead of us. I'm very proud of Composites and what they've done last year. You may remember when I joined the company, and most of you told me the same, you were not that much happy about the leverage between the top line and the bottom line since the acquisition of Cytec. Last year, and this is the word of our GBU President, not mine, was the best year in the history of Cytec.

So they've done a great job into improving the operational efficiency, right, last year. And the prepared themselves for actually weathering the storm of Q1. 737-Max grounding is not new to us. It started end of last year. I mean, most of last year but end of last year was getting a bigger impact. Q1 as well. And despite that, we had a record EBITDA level last year. And this year we delivered EBITDA in quarter one at the same level as that record quarter, right.

So now it's different. We're entering unprecedented times and we're again accelerating our mitigation efforts. We are taking a strategic look at our manufacturing footprint to look for more ways to improve efficiencies and reduce costs during this time of lower demand. So indeed, we're focused on trying to manage what is our control.

And finally, let me remind you about an important point that the reduction relates to commercial aircraft. We're not adjusting production in the military sector as this continues to remain stable and possibly grow at double-digit level. So military, I remind you, represents 25% of Composites sales. Having said that, Karim, can you address the second question.

Karim Hajjar

Yeah, sure. Well, the 50 million of costs so, I'll make it easy: it doesn't yet include the furlough benefit which are really starting now in major part. But I'll give you some more colour on it. A third of it is to do with people-related cost and two-thirds other. Now, by people, what's in it? It's continuing with the focus and the acceleration of the restructuring programme we'd announced previously. That's the first piece. The hiring freeze, austerity measures, which you'd expect, the salary freeze that we've implemented globally. These are the kind of measures we've taken place. On the two-thirds which are more of an external spend, there's an element of austerity, necessarily you can't travel, etc., at the moment but it's much more than that. There's a structural programme on indirect spend which is part of our GROW strategy. So it's really around battening down the hatches. But that's what this is about.

The furlough point, which are essentially ahead of us for Q2, is really intended as a temporary measure to mitigate and adapt to declining activity levels. And that's yet to come. But clearly you'll see that with the partial mitigation of a sales decline typically. Does that help?

Chetan Udeshi

Yes.

Operator

Next question comes from Matthew Yates from Bank of America. Sir, please go ahead.

Matthew Yates

Hi, everyone, thanks for taking the questions and congratulations on what looks like an outstanding quarter in this environment. I appreciate you're trying to temper our expectations somewhat for Q2.

Ilham, you have said several times that cash has clearly been a priority for you over the last year since joining. So let me ask you a couple of questions related to that. The first is a strategic one. I think Karim highlighted earlier in the call that you've now been put on negative outlook by the agencies. So can you talk about the decision to still go ahead and pay that final dividend versus what's a fairly significant capex cut that you're making and why that won't impact the long-term prospects of the business?

The second question is, apologies, just my own confusion around what is going on with the tax payments in the quarter. It looks like from a cash perspective you've got a refund. I'm just wondering if that's complicated by the Polyamides disposal and capital gains, or what we think an underlying cash tax rate for the year is? Thank you.

Karim Hajjar

Okay, well, let me talk to the second point and I'll come back to the dividend. I'm sure Ilham will add to it.

Ilham Kadri

Yep.

Karim Hajjar

On the tax, essentially by making a contribution in a structured, fiscally-effective way by using the proceeds of the Polyamides sale, we basically get a tax deduction. You can look at it as a one-off. It's cash, it's good quality but it's more of a one-off nature which is why I've highlighted it. So that's all really I can offer on that. The rest is pretty confidential, essentially, it's how we do things here but it's very, very secure.

On the first point, now, beyond what I've described already, talked about Moody's putting us on a negative outlook, etc., fundamentally we've got a very strong balance sheet. We've got strong cash generation and confidence both from the portfolio resilience.

Now, you also made the point around the capex. Maybe one thing to highlight and it may not be apparent, maybe because I have not made it apparent yet, is whilst we've decided to adapt our capex plans, we are really making sure we have our eye on the growth. So 40% of the reduced capex programmes for this year are still eyeing future growth project and R&I. So we're not sacrificing future growth to conserve cash. We're really keeping a healthy tension between adapting to today's priority and preparing for tomorrow's growth.

And maybe just one final point on Moody's rating action. What is helpful is also the fine print. They have given us significant time compared to a few others to come to a stronger performance from a gross debt to EBITDA metric in particular. That is what they focused on more than the cash generation or our liquidity. Ilham, on the dividend?

Ilham Kadri

Yes, thank you, Matthew. Well, listen, you know, we paid the dividend this year for 2019 results, right, and I remind you that we had a record free cash flow generation in 2019. Basically, if I remember what this 300 million euros year on year, right. And Q1 has seen similar trend, as you said, very well, as our focus on free cash flow has happened since day one I joined the company. So, at the end of the day when you close the year, you look actually paying bonuses to your employees, and we wanted to reward our people on the hard work they've done in 2019 and also to acknowledge, reward our shareholders who have put their trust in us and counting on the dividends, right? And that's basically the reason why we decided to recommend the dividends, furthermore taking into account our ability to remain cash-generative in Q1.

Now, you know also the level of our liquidity, so 4 billion as Karim said, no covenants, being in a very, very solid financial robustness. And that's important that indeed we preserve the strength of the company both in liquidity and also we closes Polyamide so we had proceeded to repair the balance sheet as I mentioned.

I think that’s the reason. The future now 2020 is another year, right, with its own share of challenges, right? And we will make the decisions concerning 2020 in due time. So that's how we saw it, right, Matthew, it’s very clinical, very consistent with the way we've done it and with the situation of our financial robustness, cash flow generation, balance sheets and liquidity.

Karim Hajjar

Matthew, one other final comment. I just remember I didn't fully answer your question on the effective underlying tax rates. Just to remind you, this comprises both deferred tax and current tax – is something to do with the cash. And at this point we're still at 26.4%. The strategic guidance remains unchanged. But let's be clear that as the profit pools in the US, etc., change temporarily, I expect all sorts of potential short term changes. But at this point, I'd say no strategic changes to our guidance on things like taxes.

Ilham Kadri

And one more, Matthew, because you have so many questions, I almost forgot it but it should not be unanswered. It's on your capex, right? So obviously the question was why you are reducing your capex by $250 million and are you jeopardizing the future?

Well listen, we remain very agile in this environment, right? I mean we're not here to a hijack or penalise our future. As I said, we're a long-term company managing and tackling the short term. We have an eye on the microscope and an eye on the telescope. Let me tell you that 40% of the remaining capex is 40% investments. It's still going to our research and innovation and development projects, right? So we didn't kill or get to the bone of the growth investments. We're not going to do that.

Now in your reality, we need to be, again, very agile, adaptable, embrace the new realities. We are assisting regularly all investments and making sure the strategic ones continue and that we're not making any delays whenever it makes sense. But if costumers do not need new capacity, if by now we have enough capacities in our own assets, and I remind you that we are also pushing digitalisation inside, our manufacturing and industrial footprint at Solvay, we are actually debottelnecking, and we believe we have enough capacity today to serve our customers today and tomorrow. And frankly, we are looking very carefully at the post-crisis shape of recovery and we are looking how to rebound and be at the start up to the quickest one to obviously win and conquer. But thank you for the question.

Operator

Thank you. The next question comes from Geoff Haire from UBS. Sir, please go ahead.

Geoff Haire

Hello this is Geoff Haire from UBS. Just had a quick question on the Composites business. Just given the recent updates we're seeing from Boeing and Airbus; would it be reasonable to assume that you're going to see negative organic growth on an annual basis both this year and next year in Composite Materials? And could you just break down the different end markets within composite space?

Ilham Kadri

So, as I told you, on composite materials, obviously, as you said, the large big 2s (Airbus, Boeing) are reducing their productions of fleet. And obviously Airbus are now 30%, you know that's Boeing reduced production on wide bodies by similar rates for the big planes. Commercial aircraft for us is around 60-65%. Military is 25%, and the balance is Industrial. That's more or less at high level, you can take those numbers, right.

I mean again, we shall see how things are going to evolve and expected to use this crisis to retire also older aircrafts. This will create probably demand for newer aircraft model. We are hearing it, new airplanes will be probably 25%, 40% more efficient. They have more composites in it. And we are well underway with mitigation efforts. And this is how we were able to deliver frankly a good Q1. And even second half 2019 was very robust because we started really looking at our operational efficiencies, we started looking at our manufacturing footprint. So this is extremely important. Operational efficiencies, manufacturing footprint, automation. It's extremely important to improve the cost structure. So we will continue doing that in the coming weeks and days, so that's the name of the game.
But in a way, we are blessed to have military doing well and we are blessed that we started already this hard work last year. So you would see more from us in the coming weeks and months, Geoff.

Operator

Thank you. And next question comes from Sebastian Bray from Berenberg. Sir, please go ahead.

Sebastian Bray

Good afternoon and thank you for taking my question. It's on composites and profitability. What is the balance of fixed and variable costs in this business? If I look at XL, the market consensus appears to be suggesting that a $1 decline in sales is going to cause a slightly less than $2 decline in EBITDA. Is that a reasonable rule of thumb for the Cytec business? And a quick follow-up. How much more book value is there left in oil and gas that could potentially be impaired? Thank you.

Ilham Kadri

Okay, so I take the Composites and maybe Karim can take the oil and gas.
Well, listen, is that Sebastian? Sebastian, as a reminder, our assets base days in Composites is a bit more flexible and I don’t want to compare with anybody else. I give you that. Meaning we are not 100% vertically integrated into carbon fiber as we procure a large portion of our needs. This means we have less of an issue with fixed costs in a way. In addition, and to complete probably the former question, our portfolio is also well in line with the new single aisle aircrafts, right, such as the A320, 737 and so on. We do not have as large position on the wide bodies such as the A350 or A380. So, you may also think about this when you do some comparisons, right? We tend to believe that this aircraft may be slower to recover. International travel may take longer to return to normal flow in the crisis. But then we have to watch and see. We have a leading position in the defence sector as I mentioned. This sector grew by double digit in Q1 and is expected to remain resilient. Military represents again, 25% of the Composites sales.

That's it. I think it doesn't mean that we can defy gravity, and don’t put me wrong, we will be hit, we are hit. But since last year we've been preparing not for COVID-19, again, but we were preparing really to look again at our return on capital employed, at our efficiencies. I didn't like, like many of you, the leverage between the top line growth and the bottom line growth. I didn't see the right multipliers when I came to the job. And the Composites team did a fabulous job in starting really addressing the operating rates. We took the best competencies we had. We didn't hold on the sole legacy Solvay, and we put them in place with the Composites leadership. And now since four quarters in a row, they are delivering leverage between the top line and the bottom line.
So I truly believe that they have again developed the muscle and we have a mitigation plan underway which we will share with you in due time. Sebastian, on the next question, Sebastian.

Karim Hajjar

Oil and gas, Sebastian. Quite simply, we haven't disclosed that when we took the impairment late last year. It's significantly below obviously as the result of the impairment in Q3 last year. But that's probably as far as I can help you at this point. It is significantly less material. If you look at the total assets of Solvay, it's not going to feature materially.

Jodi Allen

Okay. Well yeah, we reached close to the end. So maybe we have time for one last question before we close.

Ilham Kadri

Yeah, one last.

Operator

Okay. So for the last question, we have Peter Clark from Societe Generale. Sir, please go ahead.

Peter Clark

Yeah, it's just a quick one. In terms of the comments you made on Cytec, are you expecting some sort of mix drag coming on either end on EBIT on the basis that we're likely to see a much slower recovery in automotive and aerospace if it's something you can overcome? Thank you.

Ilham Kadri

It's a good question. I mean, the aero has its own dynamics. If I hear the most pessimistic people, they may see it coming in, recovering for a long time, at least, as I said, not the international travel any short term. You may see domestic travel kicking off quicker than the international ones. The wide bodies and single aisles, and this will favour the single aisles as compared to the wide bodies and the large aircrafts. But it's very difficult to answer, right, very specifically. Also, I mean, you've seen LMC forecasts. All of this is going to depend on the confinement strategies and how fast people are going to come back to work, how fast the economy is going to rebound, what type of stimulus regions or countries, including China, Europeans and the US, are going to put into the auto value chain.

A question as well is about the electrification. You know how fast it's going to go and the emission regulations which have been favouring many of us, specifically in China. But at the end of the day, I'm a believer that we are well-positioned. I remind you that the value proposition for both Composites and Specialty Polymers is about light weighting. I used to say I like metal because we can replace it; and this is for sure going to continue under the hood, batteries in a traditional internal combustion engine car, they use six kilos polymers, our polymers, the high technology polymers. In hybrid, they use 12 kilos. In electric, they use 9 kilos. Batteries need Specialty Polymers products, they need Special Chem solutions, Composite Materials along with Specialty Polymers. And that's why they belong to the same material cluster is not because was funny to put materials together, is because we are innovating the thermoplastic composites and we believe we are the best in class to really develop unique, innovative, highly proprietary technologies and solutions for these markets and beyond. Because thermoplastic composite, as you know, is the recycle, has a fair bit of sustainability profile and can beat many of the metals and metallic alloys type of specification. By the way, this type of programmes is not halted during the crisis. We continue doing testing and innovations, programs are running with our customers.

So yeah, all in all, it's a tough market environment. But again, I asked the team to not focus on what we cannot control. I think our customers are asking on us. And by the way, most of those, I should not forget one of the big value proposition in replacing metal, which is important to keep in mind in in the crisis time, is that we are lowering the total cost of ownership as well. It has a huge impact on the total cost of ownership end to end at the level of 10%, 20%, 30% depending on the segments. So I think everybody now is looking at how they can improve, and this is medium term, obviously the short term is another story. But medium term, the value proposition we have between specialty polymer and composite is a really strong bond and we believe that we are best in class to deliver those solutions.

Jodi Allen
Thank you so much. That concludes today's call. But please I do invite you to reach out to the investor relations team if you have any further questions. Thank you so much for your participation today.

Ilham Kadri
Thank you very much.

Operator
Thank you. Ladies and gentlemen, this concludes the call from cool. Thank you all for your participation. You may now disconnect.