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PRESENTATION

Operator

Good day, everyone, and welcome to the Eastman Chemical First Quarter 2020 Conference Call. Today's conference is being recorded. This call is being broadcast live on the Eastman's website, www.eastman.com. We will now turn the call over to Mr. Greg Riddle of Eastman Company Chemical, Investor Relations. Please go ahead, sir.

Gregory A. Riddle - *Eastman Chemical Company - VP of IR & Communications*

Okay. Thanks, Molly, and good morning, everyone, and thanks for joining us. On the call with me today are Mark Costa, Board Chair and CEO; Willie McClain, Senior Vice President and CFO; and Jake LaRoe, Manager, Investor Relations. In case you missed it, yesterday after market close, in addition to our first quarter 2020 financial results news release and SEC 8-K filing, we posted slides and related prepared comments in the Investors section of our website, www.eastman.com. This is new for us, and I hope it's helpful to you.

Now before we begin, I'll cover 2 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 the company's first quarter 2020 financial results news release during this call, in the preceding slides and prepared remarks, and in our filings with the Securities and Exchange Commission, including the Form 10-K filed for full year 2019 and the Form 10-Q to be filed for first quarter 2020. Second, earnings referenced in this presentation exclude certain noncore and unusual items and used an adjusted effective tax rate using the forecasted tax rate for the full year. 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 first quarter financial results news release, which can be found on our website. With that, I'll turn the call over to Mark.

Mark J. Costa *- Eastman Chemical Company - Chairman & CEO*

Thanks, Greg. Before we turn it over to your questions, I want to take a few minutes to make some comments. We all recognize that our world is facing unprecedented challenges right now. COVID-19 isn't like anything we've ever seen before. For those affected by the pandemic, I want to recognize how difficult this must be for what you're experiencing. So many are helping too in this difficult time, in the health care community, our first responders and government and local communities. And to them, I want to express my gratitude for helping keep us safe. As importantly, I want to thank the men and women of Eastman. It's been said that characters are revealed through adversity and Eastman team has demonstrated its character and risen to every challenge we've faced. We've come together in tremendous ways to keep everyone safe, all while keeping our operations going. I particularly want to thank our operators, our mechanics, our electricians and their families who've kept our plants running and get our products out to our customers every day. And to the many Eastman employees who are working from home or on site. Thank you for continuing to support our customers and keeping business going. So to you, my colleagues, at Eastman, thank you for your courage, your ingenuity, and your dedication. You're truly making an incredible difference in a material way.

Turning to Q1. We had a strong first quarter in earnings and even more impressive free cash flow generation. This quarter demonstrates what Eastman can do when we have a day of sunlight between the trade war starting to moderate and COVID starting to escalate. Given all the uncertainty related to COVID-19, it's extremely difficult to predict financial results for 2020. So we are withdrawing our guidance. We did see some impact in the first quarter as we attribute a $20 million to $30 million EBIT decline to the impact of the pandemic.

Our diverse end markets mitigated some of this. While we saw a substantial impact in transportation and textiles, we also saw stability in a number of our other markets. As we look forward, we expect to see increasing challenges in transportation, textiles and energy markets. We also see a number of markets providing stability, such as consumables, medical, personal care and ag. And there are markets where we expect a mixed impact, such as building construction, consumer durables and industrial chemicals. None of us can know what will actually happen with how we attempt to restart these economies across the globe. We can take some insight and hope from the recovery we're seeing in China. We are far from having insight in how North America and Europe will restart. We were able to continue to lead from a position of strength because our innovation-driven growth model and our operational discipline. The benefits, especially in this uncertain time, have never been clearer. We have a long track record of transforming our portfolio towards specialties. And within this portfolio, we have built an outstanding innovation capability as well as a decisive operational execution capability.

Eastman has industry-leading cash flow, which we have taken aggressive actions to sustain in this current environment with a strong balance sheet and significant sources of liquidity. In addition, we have a proven track record in our specialty businesses of driving growth above end markets with our innovation-driven growth model. That said, in this incredibly uncertain time, we are focused on the actions we can control and are exceptionally well positioned to weather this environment. We are realizing stability from our diverse end markets and leveraging our strong customer engagement. We're taking significant cost actions, adjusting our operations to the current demand environment, significantly reducing discretionary spend and deferring some turnaround of assets. We're expecting strong free cash flow this year with working capital expected to be a source of greater than $250 million beyond previous expectations. We reduced our expectations of capital expenditures by approximately $100 million to a range of $325 million to $375 million. Finally, we will maintain our disciplined approach to capital allocation, with a focus on our strong dividend and a significant debt repayment program, which we now expect to be substantially greater than $400 million for the year. All in, we've made great progress strengthening the company, and you can see the evidence in the first quarter earnings and cash flow. With that, Willie and I are happy to take your questions. Operator, we're now ready for the first question.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Our first question will come from Vincent Andrews of Morgan Stanley.

Vincent Stephen Andrews - *Morgan Stanley, Research Division - MD*

I didn't see your prepared remarks, but I'm happy. I'm happy you're doing them, and I look forward to reading them in the future. I did just skim them. But with that said, Mark, I'm wondering if you can just talk a little bit. I saw in the slides, you talked about April being down 15% versus March, and it sounds like March was worse than the other 2 months of the first quarter. But maybe you could just contextualize April? How much it's down versus the overall first quarter?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

Sure. So as we said in the slide, we really try to provide some perspective across the markets and sort of grouped them into 3 categories, Vincent. And it's good to hear you and you sound healthy as well. About 40% of our markets are quite stable and doing quite well, being relatively flat sequentially. And in those markets, you've got things like personal care, consumables, which is a range of things from packaging adhesives to packaging polyesters, et cetera. The medical pharma parts good, ag, nutrition. And all those markets are going to hold up relatively well in this. Then you've got somewhat challenged markets that are like building construction, consumer durables, electronics, industrial chemicals, where they're actually still also sequentially declining, as you can see in April, but we expect those to continue to sort of do relatively okay to the more impacted ones in transportation, textiles and energy. So there really are 3 things. That diversity of end markets, especially that 40% that gives us a stability in the world is incredibly helpful in this time. And we would expect that to sort of continue through the quarter. The -- what we call mixed impact are a little bit harder to call. I think there's some of that, that's holding up well, like consumer durables, a lot of our innovation and Tritan and things like that are allowing us to create our own growth. So we're seeing stability from not just markets, but innovation in some of those applications. Architectural coatings is holding up really well as well as our architectural interlayers. But it's reasonable to expect some of that's going to moderate as existing projects might be completed, et cetera. But through Q2, I think it's going to be okay. The question is what happens longer-term to some new starts in housing. And then the real challenge, of course, is in transportation, which I think is extremely well documented, where you've got auto plants, tire plants shut down all over the world, fortunately, China coming back. But we track every tire plant, every auto OEM, every window plant down to the model and are mapping all that out. As you know, they're all shut down now. So the question is when are they going to start back up? And we see that recovery and that sequential improvement in China already, but obviously, U.S. and Europe is still a question mark. So we've been conservative. We've assumed that the auto OEM market's going to be down, from an OEM production point of view, be down 50% for the quarter, which is on the sort of more pessimistic end of the range of the consultants out there. and that's really to inform our production and inventory strategy as opposed to trying to say we can predict earnings at this point given the uncertainty. But -- so we've been very aggressive in how we manage our plans for that. And we'll see how it recovers. So overall, I'd say April's a good indicator of the quarter. I think that we could expect it to be a bit more challenging in May as supply chain line catches up to us with a lot of these plants being shut down. And then we presume that, along with the consultants, that things will start back up to some degree. And so you'll see some of that benefit in June. Does that answer your question?

Vincent Stephen Andrews - *Morgan Stanley, Research Division - MD*

Yes. So just to recap, it sounds like you're saying being down 15% in April, sequentially, it's probably about right. It'll be a little worse in May, and may be a little bit better in June. But if we think sequentially between 2Q and 1Q, we could think about your volumes being down. I'm just going to say 15% to 20%. Is that fair?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

I mean, I think that's a range to start with. I just really want to emphasize for everyone, no one knows what's going to happen here, right? I mean, there's just a phenomenal amount of uncertainty when we don't even know how the U.S. and Europe are going to restart yet. And there's a lot of questions that we have to answer that go with that. So we can get people back to work in a lot of companies, but it's really a question of what consumers are going to do, are they going to go back to restaurants? Back to their more -- normal life activities? Travel? Shop in retail stores? Buy cars? We don't know how the consumer's going to behave coming out of this, which will then dictate when auto plant start up, when tire plants start up. Housing is going to play out when it comes to -- they've got great DIY and projects that they're finishing in construction, but how many new starts are going to happen? So there's a lot of crystal ball gazing. I think April is informative, and it's 1/3 of the quarter. But what we're going to do is be conservative, really focus on cash generation, manage what we can control. And we will give you updates through the quarter as we get more insight.

Operator

Our next question comes from Jeff Zekauskas, JPMorgan.

Jeffrey John Zekauskas - *JP Morgan Chase & Co, Research Division - Senior Analyst*

How did you make so much money in Chemical Intermediates on a sequential basis? I think you were up over $8 million, maybe it was $20 and $20-ish million in the fourth quarter. And can you talk about the dynamics? What are you doing right there?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

Well, we have a great commercial team there that does things right every day and how it optimizes every market to place products at the best price possible and optimize our big engines that support our specialty businesses. You've got to remember, Chemical Intermediates role is clearing the excess capacity that isn't going into the specialties. And my hats off to that team in doing that. It's a dynamic time. We did have a very strong sequential improvement from Q4 to Q1. And it was really driven by 4 factors. The first was strong volume growth. So we saw strong improvement in ag, alkylamines, that market had been pretty depressed. There's a lot of destocking going on in the fourth quarter last year. The ag market came back to life. Those are high margin products for this segment. And so that was quite helpful. But we also saw strong demand in a lot of other markets, acetyls, plasticizers and a few others. So volume was the biggest driver of all of the levers that improved it. the second was a lack of shutdowns. So we had a huge shutdown going on in the third and fourth quarter last year. A lot of that expense was in the fourth quarter. So we didn't have that. So that was a $20 million benefit in itself from Q4 to Q1. The third was an improvement in spreads. So we got our spreads back to being about where they were in Q1 '19. So that was a bit of an improvement from Q4. Some of it was cracking spreads, got better in January and February. Unfortunately, they started to compress a bit in March, but we got the benefit of that. And the last part was the licensing. So we told you we had a sort of robust multiyear licensing program that we were driving in our fourth quarter call in January, and we got the first installment on one of those licenses in the first quarter. I'd say that was a smaller part of the story, but progress. There's more of that to come this year when we complete that license. And then we -- as we've said, have a portfolio of licenses we're looking at doing as we go into the next couple of years. So it was just great success, Jeff, on sort of every line of the income statement and the assets ran well, utilization was good.

Jeffrey John Zekauskas - *JP Morgan Chase & Co, Research Division - Senior Analyst*

How representative are those operating earnings for the remainder of the year? Or what are the headwinds or tailwinds that you foresee? And when you talked about April being down sequentially by 15% for the company as a whole, how much was April down year-over-year?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

Well, April, on a year-over-year basis, just to take that quick question first, was similar to sequential. And regards to the CI store, unfortunately, it's not going to hold up like it did in Q1. We do see some headwinds as we go into Q2. And the key components there, one is volume, different story, ag is continuing to hold up and be really strong. But with the COVID-19 impact, you certainly see markets slowing down. Our chemical needs do go into end markets that face these headwinds that we're talking about. So they're going to see that demand pressure on multiple markets. And in the current environment with the oil situation, a lot of what we would, sort of excess capacity, we would export to Asia after serving sort of North American, European markets, is to sort of run the assets totally full. Those markets -- those export markets aren't as available. Asia still hasn't come really back to the life. Margins aren't great. So you got a bit of that -- it's low margin volume, but some of that export volume that's sort of restricted in this current environment. So volume will be the -- unfortunately, reverses outside of ag amines as being a bit of a headwind. And the second part is, you can run the models, and I know you have them, Jeff. Cracking spreads are a bit more challenged as we go into this quarter. And so we'll feel a bit of headwind from that. And then we'll -- as we slow down the big engines due to decline in specialty business, we're going to have asset utilization headwind that occurs across the 2 big complexes in Longview and Kingsport and that higher sort of cost per unit with these lower rates will impact CI as well as specialty. So it will feel a bit of that. So you're going to see a meaningful decline with all those factors as we go into sort of Q2 with this business. I would note that oil is, on a corporate basis, neutral to positive, but it will have an impact on CI.

Operator

Our next question comes from Frank Mitsch from Fermium Research.

Frank Joseph Mitsch - *Fermium Research, LLC - Senior MD*

Greg, yes, the prepared remarks were helpful. And as I was reading the prepared remarks. On the cost reduction front, you had outlined that you were going to save $20 million to $40 million this year and $100 million over a 3-year period. That's been accelerated to $150 million this year. Can you talk about the buckets that, that falls into? How are you going to get at -- how are you going to build up to that $150 million cost savings in 2020?

William Thomas McLain - *Eastman Chemical Company - CFO & Senior VP*

Yes. Thanks, Frank. This is Willie, and I'll lead on that question. So as you think about -- Mark's already highlighted how we're changing our operational footprint and becoming focused on cash here in late Q1 and planning to run that way for the rest of the year. Also, that enables us, I'll call it, to reduce the level of contractors on site. It also results in changing the scope of some of the maintenance, et cetera. Additionally, another key lens to that is discretionary spend. We have stopped travel, reduced consultants and third-party services as you think through that. So those are the key factors. Also, as you think about that, we did get some of that benefit in Q1. It was a small amount. We expect that to increase in Q2 to be about 1/3 of the $150 million. And that 1/3 in Q2 will probably only partially offset the impact of our idling plants and reducing the operation rates, and then the remainder would be in the second half of the year.

Frank Joseph Mitsch - *Fermium Research, LLC - Senior MD*

As I think -- Willie, as I think about what you just said, it sounds like a lot of that is more transitory. At some point, you are going to have contractors back on site. You are going to travel, et cetera. So should we be thinking about this $150 million as kind of a 2020 reduction versus your previous plan? And then that will dissipate in '21 and beyond?

William Thomas McLain - *Eastman Chemical Company - CFO & Senior VP*

So Frank, for the second half of the year, we are going to be focused on improving the long-term structural cost of the company. And we highlighted that on our year-end conference call with a $20 million to $40 million. We're looking to accelerate that and transform the operational as well as our functional footprint for the long term. But you're correct. In the near term, we had pivoted the actions on the temporary front and made what has normally been fixed cost variable. And some of that will come back. But you have to remember, we have strong variable margins in our specialty product lines across Advanced Materials and AFP, and they will more than obviously offset that with those spreads.

Frank Joseph Mitsch - *Fermium Research, LLC - Senior MD*

All right. Understood.

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

Frank, just to add, we recognize that a good portion will come back. It's important to keep in mind if demand really doesn't come back much, we can extend these savings. For longer than what we've currently assumed to ride through even a more difficult time. On the flip side, I think we're learning a lot about how we can operate and be efficient in this work-from-home environment and there's different operating modes, so we're embedding that into our thinking about how to improve our long-term cost structure. And we're certainly escalating and accelerating what we intended to do on that $100 million-plus program to get more of that as we go into the back half of this year as well as next year. So there's a lot of actions we're taking to sustain through this second phase of activity, our cost. Key thing I want to emphasize, though, is none of what we're doing is cutting our innovation programs. So we are optimizing for this environment. We're very focused on cash, but we are also focused on making sure that we have a long-term strategy in place as we come out of this to have strengths, to create our own growth when the markets actually come back to life. Through innovation, continue to have that kind of engagement with customers. We're still actually getting a lot of engagement with customers today. On innovation, even in this sort of virtual environment, we've had a number of wins. We've even have a recycled Tritan content product that we launched. We've already got 3 wins on that. Nalgene, Camelbak and a couple of other big brands have adopted. We're getting wins on our recycled cellulosics as we speak, 2 of the largest ophthalmic manufacturers have seen the power of a half bio content, half recycled content product for their offerings, continue to get wins in Tetrashield for can packaging and food where we've got just great chemical resistance and toughness and non-intent BPA. So good news is innovation is still live. We're still focusing on keeping those programs going, but we are very aggressively going after every other bit of cost.

Operator

Our next question comes from Alex Yefremov of Keybank.

Aleksey V. Yefremov - *KeyBanc Capital Markets Inc., Research Division - Research Analyst*

I would join everyone supporting the prepared remarks. Question on free cash flow. You have about $400 million in dividends. You said substantially more than $400 million in debt repayments, maybe another $50 million in buybacks. So can we say that kind of the floor for your free cash flow is about $850 million and it's really substantially more than $850 million this year?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

So yes, let me answer that question. We expected it. And I want to start a little bit just back on the market comment. So obviously, demand is unpredictable. That's why we pulled earnings guidance. And we are in the position to sort of understand what happened in April, but not know what's coming for the rest of the year. But we have to make some assumptions, and we are modeling scenarios like everyone else is doing different kinds of recovery out of the second quarter. We do believe the second quarter will be the toughest quarter with the complete shutdown of these global economies and the indication as we see it now, that people will start trying to come back to life through this quarter. I want to emphasize this diversity in markets is a huge help for us to maintain stability. The 40% that's very stable and even 35% that's sort of mixed is providing a lot of stability to offset the challenges that we have in that transportation, textile side. And there's a lot of uncertainty there. We do see price stability. So we saw great price stability in the first quarter. We expect price stability to continue into the second quarter in the specialties. So we are getting some benefits there from raw materials and would expect that to continue through the year. And as I said, low oil is sort of a neutral to positive event for the overall portfolio. So that's all what we know about the markets. In that great uncertainty, what we have to do is focus on what we can control. And so what we can control more so is a lot of our cash generation outside of cash earnings. And so we're doing everything we can to stay close to our customers, make sure we don't lose share, keep our innovation going so when the markets recover, we will cover with it. We've acted really quickly to idle all of our plants or campaign them or reduce utilization. We moved very quickly in March when we saw this was going to get worse outside of China with the COVID spread. So we really sort of ramped back raw material purchase and everything else in the plant so that we could take advantage of what demand does exist to pull inventory down, and we're doing a great job of that. So working capital $250 million, we think will been released. And with all the cost actions really described, $150 million on the cost side and about 40% of that will flow into the second quarter number on that $150 million and reducing CapEx $100 million. So lots of levers that we're pulling. And so when we look at that and run our scenarios, obviously, the dividend is our priority. We're going to pay that. It's a great strong dividend. It's been increasing for over a decade.

And on the delevering, which is our focus, we do think we can do substantially more. And what that means to us, even in a very slow economic recovery, we believe we can do greater than $1 billion of free cash flow. And obviously, if the recovery is better than that, there's upside. So when we say substantial, it's substantial that we're going to make a lot of progress in our delevering. But people should not be using that to try and reverse engineer earnings. It's what we're trying to do on cash flow so things -- and the levers that we can pull, we can pull even harder in inventory if we need to, we can pull harder on costs if we need to. But it's a cash-centric strategy that we're operating right now.

Aleksey V. Yefremov - *KeyBanc Capital Markets Inc., Research Division - Research Analyst*

Understood. Mark, very helpful. And just to follow-up on your margins, it's understandable that your volumes will affect your margins. But in terms of spread between price and raw materials, by the end of the year, should we expect that spread to be at a healthier level than, let's say, back half of 2019 or even first quarter? And related to that, if you could update us on your view on the methanol contract headwind this year?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

Sure. So I'll take the first part of that question, and I'll let Willie answer the contract question. So spreads in the specialties, we do expect to improve our spreads in Advanced Materials of the raw material tailwinds that we have there. With the 2/3 of AFP as we sort of separate that out for you, we expect spreads to improve with good price stability relative to the raw material declines. And so in all those areas, I think we see that Fibers, very steady spreads for the year. All that is, I think, a place where we can get some additional cash and earnings benefit. The 1/3 of AFP, I'd say, the tires adhesives, it's going to be more stable spreads, but at the challenged levels we had in the back half of last year. We don't see it getting a lot worse this year relative to the second half of '19, but we don't expect it to get a lot better given the sort of competitive dynamics in that spot. And in Chemical Intermediates, as I said, we've got some challenges there on spreads. Something important to note about this oil topic is our crackers and the spreads there are a little bit different than other companies'. So it's not nearly as challenged at this point as it was in the past. So '10 to '16, we had a huge tailwind when oil went up and we had stranded gas in the U.S. that let ethane and propylene also be stranded and really cheap. You got to remember, our crackers are propylene centric because that's what we make specialties from. That's why they exist. So we're much more propane-based in our crackers. And we -- on top of that, we made the RGP investment to even further reduce the amount of ethylene we produce, replacing some of the NGL feeds with RGP. So that changed the dynamic. So we're now 70% to 75% propane, 20% to 25% ethane, the remainder 5% to 10% is RGP. And propane isn't stranded anymore, right? So it stranded up through about '16, but they added so much export capacity to export propane. That's now reconnected to the oil market. So propane propylene spreads are a lot more connected than ethylene to ethane. And RGP is very tightly correlated to PGP. So the volatility still is going to be a challenger, but it's not nearly the challenge that we would have faced back in '15 and '16, as an example with its low oil now. So we have some spread. It's more about competitive intensity than it is about cracking spread that's going to sort of pressure some of these margins in this competitive environment. But spread will be a challenge in CI. But net, when you put it all together, we're in really good shape on spread to sort of be a bit better this year than last year.

William Thomas McLain - *Eastman Chemical Company - CFO & Senior VP*

Okay. Mark, on the methanol front, just to follow-up quickly, is we made the transition, as we highlighted in January. We had marked that contract to market. So I would actually say it's actually a slight tailwind on earnings and a modest headwind on cash overall. But we're exposed to coal-based methanol as well as natural gas and market. So well positioned on the methanol front.

Operator

We will take our next question from David Begleiter of Deutsche Bank.

David L. Begleiter - *Deutsche Bank AG, Research Division - MD and Senior Research Analyst*

Mark, just looking at Q2, thinking about -- how should we think about decremental margins in the specialty businesses given the asset utilization headwinds you've called out here?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

I'm going to let Willie take that one.

William Thomas McLain - *Eastman Chemical Company - CFO & Senior VP*

Yes. Thanks, David. On the decremental margin front, we've highlighted the fact that we've idled plants, we're lowering capacity utilization. And that -- a lot of that is focused on our transportation, textiles and energy end markets, and that is predominantly in Advanced Materials and Additives & Functional Products. And as you think about AM, we've previously talked about how the margins have shown through as the specialty and premium products have grown. And that's because of the fixed cost leverage as they've been able to grow. So you can expect a little bit of the reverse here in Q2 as we focus on maximizing cash generation and reducing cost in this environment. However, you should expect on the recovery that as the demand recovers for these businesses that -- then it would bounce back. A little bit of contrast between AM and AFP is the fact that Advanced Materials has idled more plants, whereas Additives & Functional Products has slowed those down. Additionally, given the specialty nature and the linkage across the streams, there are more fixed cost and capital involved in those specialty product lines that result in the decremental margins and fixed costs being worse. When those variable margins come back, the reverse is true, and we would expect to see that in the second half of the year.

David L. Begleiter - *Deutsche Bank AG, Research Division - MD and Senior Research Analyst*

Got it. And Mark, just on this -- I'm sorry.

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

Go ahead.

David L. Begleiter - *Deutsche Bank AG, Research Division - MD and Senior Research Analyst*

Yes, just on the strategic alternatives process, that 1/3 of AFP that you highlighted back in October, any update or progress you made on that initiative?

William Thomas McLain - *Eastman Chemical Company - CFO & Senior VP*

Yes, David, let me go first, and Mark can follow-on. We had several interested parties pre the COVID environment, but it's difficult to get a transaction done now. And obviously, we need to focus on the earnings impact of this event. We are also focused on restructuring these businesses right now and continuing to evaluate our manufacturing footprint in these businesses, and we'll have decisions soon on those. Additionally, we're taking cost out such that on the other side of the COVID environment, we can focus on other strategic actions that we can take with these businesses.

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

So I think that's not exactly a surprise that we'd be sort of challenged from a process point of view. The thing I want to add beyond just the restructuring activities, and we intend to be aggressive there and hopefully make some decisions here soon about our asset footprint, the innovation is actually very attractive to potential interested parties and actually going quite well. So our new Crystex that is far superior to the competitors' in the marketplace, is getting a lot of adoption more than we thought. That's one plant that's actually running well right now in this tire environment. In fact, we've had to increase rates there because of the demand for it. So that's helpful and encouraging. Obviously, the overall market is extremely difficult in tires. But it's good to see that the innovation still is attracting attention and adoption, and it's at a better price. Same is true in tire resins. We've been launching and trying to validate a new set of differentiated tire resins. And we've virtually, once again, had progress innovation-wise in verifying and validating that with a couple of big MNCs seeing the value and wanting to move forward to those programs. And even over in adhesives, our new UltraPure, sort odor-free, VOC-free resin is getting a lot of adoption right now even in the context. So the innovation's important. It's all part of restructuring the business and improving it while we have it as well as making it more valuable to other people. So we're just going to have to get through this short-term environment.

Operator

Our next question will come from PJ Juvekar of Citi.

Eric B Petrie - *Citigroup Inc, Research Division - VP & Senior Associate*

Mark, it's Eric Petrie on for PJ. How much did your premium products and Advanced Materials grow in first quarter? Or were there destocking actions by auto OEMs for interlayers as well as head up displays?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

Yes. So it's a bit of a split story between auto and the rest of the business. So the 2/3 of the revenue, remember auto is only 1/3 of the revenue of Advanced Materials, did really well. So we had strong engagement, volume growth in a lot of different applications, especially in that more stable category we gave you in the slide. So packaging that's inside of consumables did really well. We had decent, very strong, stable medical. It's important to think about in advanced materials that well, the 1/3 automotive is a big part of our earnings. The second largest market is consumer durables that actually held up well because of Tritan continued to create its own growth. So that's actually been reasonably good. The third largest market for this business is medical, very stable, very profitable and doing well. The fourth market is these consumables, I mentioned, stable. Fifth is architectural, even there, holding up relatively well. So all of that's gone fairly well and why you saw earnings be up and stable. Automotive, which is a very high margin part of our portfolio in the entire company, whether it's AFP or AM, obviously, we saw good demand. Actually, we saw good demand in January and February. And then, obviously, demand came off with the escalation of COVID in March. That is that $15 million to $20 million of EBIT headwind we called out was really sort of transportation related, and it was really March related. So we felt that impact on the demand there. So overall, it's holding up pretty well, except for transportation. And prices held up well. Raws came in to be quite a benefit for the quarter. And the asset utilization was, in general, pretty good in the first quarter. We haven't really seen the impact of asset utilization in this business until we get to the second quarter.

Eric B Petrie - *Citigroup Inc, Research Division - VP & Senior Associate*

Helpful. And then secondly, some paints and coatings companies are guiding volumes down for second quarter by 1/3. Are you expecting similar declines?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

So in automotive coatings, we would expect to see a pretty dramatic decline, as you saw. We're assuming OEM production is going to be down 50% sequentially. So automotive coatings is going to track that and be quite a large headwind. On the other side, architectural coatings seem to be holding up a lot better based on what we're seeing and what I heard the coating customers that we have, say, earlier this week. So I think that number you're quoting is a bit of a blended number. We have 2 markets that have very different sort of tracks between architecture and OEM -- auto OEM.

Operator

Our next question comes from Duffy Fisher from Barclays.

Patrick Duffy Fischer - *Barclays Bank PLC, Research Division - Director & Senior Chemical Analyst*

Within your AFP segment and AM segments, can you walk through the products where your competitors would base their chemicals off of oil? And so even if they have kind of lesser quality products, maybe with this lower oil environment they will push harder on price?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

Sure. So Advanced Materials, oil is sort of -- ultimately drives a lot of the raw material costs for pretty much the entire segment outside of the cellulosic products, Duffy. And so in that area, you have that potential. So far, we've seen great price stability through all last year, right? Paraxylene was a tailwind all last year. Prices have been holding up relatively well. Starting to give some back. To be clear, as we've said in many calls in the past, you don't hold on to all of it, right? You've got to treat your customers with respect and share some of the raw material value, and we're going to do that. But still, net, I think it's going to hold up quite well from what we can see. And things like Tritan, where we're the only competitor in the world, we've got a lot of control over pricing. On the auto-related markets. Interlayers is annual contracts. So those prices got established last year. So they don't have a lot of movement to them when it comes to raw materials within the year. And then in performance films, it's also very price stable. They -- it's a consumer product, and our prices are pretty stable there. The value that we present in performance films is not remotely connected to raw materials. So overall, I'd say that segment, it's going to have some prices come down a bit this year with raws, but hold up really well. In AFP, if you go to the 2/3 of AFP that we called out. So coatings, specialty fluids, Care Chemicals, crop, et cetera, that's actually going to have pretty good price stability, has had good price ability through last year and expect it to continue to have really good price stability this year. There are some cost pass-through contracts in Care Chemicals and coatings that we'll pass on some of those raws, but the spreads will be stable, which is in the end, all we want from a long-term point of view. But you'll see some of that impact. That's about 2% of the 6% for the overall segment as those cost pass-through contracts for the first quarter, as an example. We will see some increased price competitive behavior in adhesives and tires in the 1/3, but that's also sort of stabilized. They got very competitive by the back end of last year. And I don't think spreads are going to compress a lot more from that to this year. So overall, I'd say we're in pretty good shape Duffy, to either neutral or improving, even in this environment. And that portfolio, Fibers, is totally different, as you know, where those prices at 1% down will be that for the year. And in CI, I think I've already addressed.

Patrick Duffy Fischer - *Barclays Bank PLC, Research Division - Director & Senior Chemical Analyst*

Sure. Okay. Great. And then I think it was in your prepared remarks, you made a comment where you thought transportation demand -- I don't know if you said it was going to be stronger or less bad than tire in aerospace. So is that a call on kind of those markets? Or is there some inventory in those different segments that may skew that how it hits your business? But can you just talk through why you think transportation will be stronger than tires and aerospace?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

So when we say transportation, Duffy, it's all 3. Right. So when we talk about transportation, and in any reference, it's always autos, tires and aviation. So all 3 are in that comment about being a very challenged market. What I'd say is, tires and aviation is more challenged than auto OEM. So you can go get the external data, but obviously, no one is flying right now. And I think the rate of people flying is going to come back slower than the rate of people buying cars. And because initially (inaudible) cars, by the way, that could be an upside here is who wants to get in mass transit right now. We could see more cars sold on the back end of this thing as people shift their behavior towards being in their own car versus mass transit. We're not baking that into our forecasting, but it might be an upside. But tires is -- demand's very much off. It's not just the OEM side, but the refinish side -- the replacement tire side is obviously off because no one's driving. And so net, that overall segment is what you see 40% down is all of that rolled together.

Operator

Our next question comes from Matthew DeYoe of Bank of America.

Matthew Porter DeYoe - *BofA Merrill Lynch, Research Division - VP*

Glad to hear you're doing well. It's a little hard to believe it was only a couple -- maybe 2 months ago or so we were at Fort Lauderdale, but I wanted to touch a little bit on Frank's prior question. You had mentioned the second half of the year, you're looking for more of the structural savings. And so if we think about the cadence of those stickier savings as we move through 2021, 2022, can you talk a little bit about that? Is it still perhaps $100 million in structural costs? Is that larger now? Would an eventual announcement on asset footprint optimization be included in those numbers? Is that upside?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

Sure. So the $150 million, obviously, a lot of it is connected to demand. And by the way, you'll be very happy if that temporary cost relief comes back because it's going to come back with revenue that has very high variable margin to pay for it. So we'll be celebrating those temporary costs coming off. The -- but the structural side, I think, is what we said. So we have a lot of work going on, an extensive, comprehensive program on an operational transformation project to look at every element of how we operate from supply chain, manufacturing, inventory management, et cetera, to take out significant costs, that analysis. And work going on is discovering more opportunity than we expected, and we'll give you more insight on that as we refine it. So we're excited about that, and that will allow us to escalate and increase that $100 million as our long-term goal as well to get some more of it into the back half of this year that would annualize into a real helpful benefit for next year. It does include asset rationalizations. And we told you we're going to address our Singapore plant, where that has material benefit. Obviously, with the tire situation, we're looking at optimizing our tire footprint, asset footprint, and we'll make some decisions around that. So it is a combination of better maintenance, better network optimization, better supply chain management, more efficient operations as well as asset rationalizations, pulling every lever we got. And we're going to look at SGA too and figure out how we take our business operating model that's really working phenomenally well and how we've built and developed that over the last couple of years in improving how we operate, make commercial and operating decisions today. And see if we can -- that will enable some efficiencies. Something else I'd note just on the back half of this year. It's important to keep in mind that as we're running our plants and something that Willie said about idling a bunch of facilities or severely reducing their run rates. That changes cost from going from into inventory and flowing out to being a period expense. So in the second quarter, you're going to see a pretty significant hit on period expense of conversion costs that will be sort of charged in the quarter as opposed to flow normally. So that will hit Q2, but it becomes a mere image benefit in the second half of this year because our total conversion cost for the year is going to be down with all the actions we're taking. But the timing of when it shows up by quarter is going to be very different than any other year because so much -- it's going to sort of aggregated into the second quarter. So even on a second half basis, we've got that 60% of the $150 million coming in. We're also going to have this period charge sort of, if you will, reversing because it's no longer in inventory. So as long as demand comes back at some level in the back half of the year versus Q2, you're going to see that benefit. So there's a number of things that help the back end that's just cost accounting on top of all the actual actions we're taking to reduce cost that you got to keep in mind.

Matthew Porter DeYoe - *BofA Merrill Lynch, Research Division - VP*

That's helpful. And I guess, if I can find one more in. You mentioned you're the only producer of Tritan, which is frankly the case, but the product does compete against polycarbonate and SAN. And the other 2, I would imagine, we're seeing some pretty significant price deflation. So does the value proposition of Tritan change at all here? Does that possibly limit growth on the back end as we move out of this and Tritan and maybe has the higher product price versus peers than before?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

Yes. So Tritan wins in the marketplace for -- historically for 2 reasons, and now it has a third. So historically, we launched it into specific applications where we actually had better product performance in the sort of normal functional way. So better chemical resistance, better performance in these houseware applications and medical applications then polycarbonate as a starting point. Then, of course, BPA became an issue. So we picked up a lot of share and a lot of stability in our pricing because we have BPA free and polycarbonate's not. So that helped a lot and has allowed us not really -- we don't really compete against polycarbonate anymore in the applications we're in. San is out there, but it's brittle breaks if you drop it,

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it doesn't have the toughness at all compared to what we do. so it's a real downgrade. If you want to go that product. And now people are starting to -- especially in Europe, as a leading indicator, really starting to worry about styrene. So we're getting a lot of conversations from brands that they want styrene-free solutions. So that's also helping us. And then the third thing we've added that I think is going to be very significant for the entire portfolio in specialty plastics is recycled content, whether it's Tritan or sort of -- or other really core copolyesters or even a cellulosic, we now have the ability to add recycled content through chemical recycling, which means I can put recycled content all these products and no compromise in performance whatsoever. It's identical product, just has recycled content. So we're already getting wins, as I mentioned earlier. So that's adding a whole another level of differentiation and value to sort of taking plastic out of the environment, and truly offering circular solutions where we can actually take back products from cosmetics or hydration vessels or any other source and loop it straight back into that same product even on textiles over in fiber. So lot on going to help us continue our differentiation.

Matthew Porter DeYoe - *BofA Merrill Lynch, Research Division - VP*

Is there a market price premium? Are you catching that price premium on recycled content? Are you finding that people are willing to pay up for it?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

We're not going to discuss that right now. That's a customer-by-customer basis. But there is a value to this that -- and a cost to this. And we're confident that our spreads will be equal to or better than our current spreads.

Operator

Thank you our next question comes from Kevin McCarthy of Vertical Research Partners.

Kevin William McCarthy - *Vertical Research Partners, LLC - Partner*

A couple of questions on chemical intermediates. Mark, I was wondering if you could expand a bit on your licensing activities. Last quarter, you had discussed some ethylene glycol market opportunities in-licensing. Was that the source of the revenue in the first quarter how much of a benefit did you have? And what does it look like for the balance of the year relative to the magnitude of the first quarter contribution?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

So I'll let Willie take this one.

William Thomas McLain - *Eastman Chemical Company - CFO & Senior VP*

Yes. Thanks, Kevin. So as you think about what we said in January, we said we would get licensing revenue of roughly $25 million to $50 million over a 3- year period. I would say this first installment is a modest amount that we see on this. And we would expect potentially more in the second half of the year as we hit additional milestones. But you can think about it as being, I'll call it, a little bit less than the $25 million on the low end.

Kevin William McCarthy - *Vertical Research Partners, LLC - Partner*

Okay. And then with regard to volume in chemical intermediates, Mark, I think you called out 4 different factors there. One of them was strong volumes in ag. I was curious about your volumes in oxo alcohol. Did you see any sort of a boost from isopropanol into sanitizers or sort of COVID related demand there? Or is that too small to matter in your mix?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

I would call it too small a matter. I mean, there are certainly some boosts in the propanol area. We see demand holding up relatively well in some of these stable markets. And so CI, where their products are going into those stable markets are benefiting from it. but I wouldn't call it significant offset. The real benefits we're seeing on the positive side the COVID-19 crisis is more in parts of specialty plastics, where we're going into face shields and the barriers, the grocery store, if you see those plastic barriers up between the checkout person and the consumer, that's our heavy gauge sheet that goes into those applications. So you're seeing a lot of strong growth in some of that. Medical is obviously doing relatively well. Pharma, et cetera. so there are places where we certainly see some benefits in that stable section of what we called out on that market map. But more and smaller amount in AFP.

Operator

Our next question comes from Matthew Blair of Tudor Hold.

Matthew Robert Lovseth Blair - *Tudor, Pickering, Holt & Co. Securities, Inc., Research Division - MD of Refining and Chemicals Research*

I'm glad to hear everyone is safe. We think of Eastman as having a lot of connections to propylene, both on the commodity side as well as specialty side of your business. Given that refineries are a key source of propylene, could you talk about what impact, I guess, if any, you would expect lower global refinery run rates would have on Eastman here?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

Yes. So we expect the reduced rates on the refineries to help maintain a better PGP price. But it's like the price of oil, the demand is off to such a degree. It's a little hard to figure that out yet here in the second quarter. But we do see PGP holding up relatively well compared to ethylene by a significant amount. And that spread, therefore, to propane is holding up reasonably well. So that's helping. But I wouldn't -- I don't think it's going to cause a spike up in propylene at this point given where overall macroeconomic demand is.

Matthew Robert Lovseth Blair - *Tudor, Pickering, Holt & Co. Securities, Inc., Research Division - MD of Refining and Chemicals Research*

And then I was hoping you could talk a little bit more about the dynamics in tires. Previously, you've highlighted your exposure to areas like commercial in replacement rather than OEM. And based on the March data, it looks like replacement is holding in better than OEM. So I just want to clarify, is that is that reversing as you head into Q2 where these replacement tire markets are softening more than OEM?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

well, I think there I think the expectation of our tire customers is that they're both softening, everything is soft, right? So what you've seen higher plants do, we serve the vast majority of them across the globe, given our market position in Crystex, and PPDs. So we have a pretty good visibility. And when we track by line, by plant, you got about 90% of them shut down in April in the U.S. and Europe. Obviously, they're starting to come back to life in China, but it's like OEMS, I mean, they're shut down. It's a combination of destocking their channel, like we're all doing to focus on cash generation as well as uncertainty demand if people are driving if there's limited commercial activity. There's going to be just less replacement tires needed here in the short term, people are going to run with what they've got, especially in this period of shelter in place. So I think they're adjusting to that. There's a few plants that are starting to turn back on now. Seeing that in a few places, but we're far from seeing them all come back to life. But I do think the replacement business, for sure, is going to be more stable than OEM in a normal time or even in a sort of normal recessionary time. But what we're in right now is just nothing like anything we've seen before. It's not like a recession, right? Everything light just went off, right, on all service activity or commercial activity. The retail stores, et cetera. So there's just a huge change in mobility that we have to work our way through, even applies to auto refinish, where normally, that's very stable, but obviously, that's declined a lot right now, too.

Operator

Our next question comes from Mike Sison of Wells Fargo.

Michael Joseph Sison - *Wells Fargo Securities, LLC, Research Division - Senior Analyst*

You guys all sound well and healthy. Mark, it's been a while since volume has been a tailwind, but hopefully, over time, things get better. Where do you think profitability or margins can get to if volumes return, maybe on a more normalized environment whenever we can get back to that? Well,

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

I certainly think that if we look all the way back to 2018, when you get to -- before the trade war started and that then got followed on by COVID-19, I mean, you can't really make this up. Those margins that we had back then were, I think, quite attractive and representative of where we were as a company and where we should be going forward. So I don't see any reason that we won't have attractive margins in the 2/3 part of AFP and obviously, we're stabilizing fibers. There's obviously uncertainty in CI and that1/3 part of AFP. So I think that as we look at it, there's no reason not to get back to 2018 and the performance that we had back then.

Michael Joseph Sison - *Wells Fargo Securities, LLC, Research Division - Senior Analyst*

Got It. And as a quick follow-up, I think you mentioned you felt oil prices where they're at would be neutral. But I was kind of thinking about chemical MB, it's a much smaller part of your portfolio, your specialty business is much larger. So why wouldn't oil be more of a beneficiary given the lower prices and raw materials for your other businesses?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

Well, I think it is, and you're right. I mean, CI was 14% of our earnings in 2019. So it's not a significant part of our story. You've got 2 combined effects on CI at the moment because the oil price is so low, right? You've got the sort of competitive dynamics, spread compression part of this as well as reduced volume, which is not normal for that segment. Normally, they can clear all their volume. But because the price of oil are where they're at, it's more difficult to access the export markets. So the combined effect is a little bit more extreme than what is sort of normal, if you will, Mike. But it is, I think, net, a positive when you look across the whole portfolio and the benefits we'll get in the specialties relative to the impact it has. It's also important to remember that, yes, it's not all cracking, right? So the Alkyl amines business is actually quite stable. Almost all our business is cost pass-through contracts. Demand is going really well there in the ag in markets. Peak acid is a really small business for us. It's just a co-product of making cellulosic. So we don't spend that much time on it. But it's relatively stable, too, because we're predominantly primate only North America because that's the only asset we have. And so those margins are -- prices are a little bit more stable here than they are in Asia. So it's going to be a headwind, but you're right. Net overall, it's a tailwind.

Operator

Our last question today will come from John Roberts of UBS.

John Ezekiel E. Roberts - *UBS Investment Bank, Research Division - Executive Director and Equity Research Analyst, Chemicals*

I'm glad to hear you all well. And that was an interesting observation, Mark, on cars, given no one's expecting any upside there. But my question is you've been transitioning some of the Fibers capacity to apparel, which is obviously going to be weak here for quite a while. Do you have the flexibility to shift back towards a cig tow if smoking activity actually stays pretty strong here over the next few quarters?

Mark J. Costa - *Eastman Chemical Company - Chairman & CEO*

Well, we don't have to shift back, John. The capacity that we have in place to serve the tow market is sufficient to serve the tow market. It's still not growing, right? So it's a very stable business, and we'll be stable. We expect tow volume to be stable this year. It was stable back in 2009. And but the market is still declining in that 2% to 3% range. And we don't see the growth rate yet changing in any meaningful way associated with the pandemic. So the capacity is completely sufficient to serve that market. And it's important that we have enough capacity to serve our customers there because security supply is extremely important to our cigarette customers. So the capacity is repurposed towards textiles we're going to be materially reducing the rates of those facilities to align with the textile demand. So we'll have some asset utilization headwinds in the second quarter associated with that. But we still see a lot of ways to grow and create our own growth. Obviously, we need to get past the sort of shelter in place mode. But when people come out of that, I expect some will still buy cars again, and some are going to buy clothing again. And our value proposition has really been strengthened by adding recycled content to our Bio content, right? So now we're offering a Naia fiber that's half bio from a certified sustainable force, and the other half is not going to be recycled content, taking plastic out of the ocean and the environment. And that's a very compelling value proposition for this right market now. They very much want it. And the third benefit we have is even when it breaks into a microfiber, potentially in the machine washing and get in the ocean, it's certified biodegradable. So we've got that trifecta of an offer in this space that allows us to create growth as long as there's some amount of demand. .

Gregory A. Riddle - *Eastman Chemical Company - VP of IR & Communications*

Okay. Thanks, everyone, for joining us this morning. An audio replay of this call will be available on our website a little bit later this morning. I hope everybody has a great day.

Operator

This will conclude today's conference call. Thank you all for your participation. You may now disconnect.