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## INGR - Q2 2019 Ingredion Inc Earnings Call

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**OVERVIEW:**

Co. reported 2Q19 net sales of $1.4b, reported operating income of $168m and reported EPS of $1.56. Expects 2019 net sales to be flat to slightly down and adjusted EPS to be $6.60-6.90.

## CORPORATE PARTICIPANTS

**James D. Gray** *Ingredion Incorporated - Executive VP & CFO*

**James P. Zallie** *Ingredion Incorporated - President, CEO & Director*

**Ryan Koller**

## CONFERENCE CALL PARTICIPANTS

**Adam L. Samuelson** *Goldman Sachs Group Inc., Research Division - Equity Analyst*

**Brett Michael Hundley** *Seaport Global Securities LLC, Research Division - Research Analyst*

**Heather Lynn Jones** *Heather Jones Research LLC - Founder*

**Kenneth Bryan Zaslow** *BMO Capital Markets Equity Research - MD of Food & Agribusiness Research and Food & Beverage Analyst*

## PRESENTATION

**Operator**

Ladies and gentlemen, thank you for standing by, and welcome to the Ingredion Second Quarter 2019 Earnings Conference Call. (Operator Instructions) As a reminder, today's conference is being recorded.

I would now like to turn the conference over to your host, Ryan Koller. Please go ahead, sir.

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**Ryan Koller**

Thanks everyone joining us today for Ingredion's Second Quarter 2019 Earnings Call. On today's call, you will hear from Jim Zallie, our President and CEO; and Jim Gray, our Executive Vice President and Chief Financial Officer. Our results were issued this morning in a press release that can be found on our website ingredion.com. The slides accompanying this presentation can also be found on our website and were posted a few hours ago for your convenience. As a reminder, our comments within this presentation may contain forward-looking statements. These statements are subject to various risks and uncertainties. Actual results could differ materially from those predicted in the forward-looking statements, and Ingredion is under no obligation to update them in the future, as, or if circumstances change. Additional information concerning factors that could cause actual results to differ materially from those discussed during today's conference call, or in this morning's press release, can be found in the company's most recently filed annual report on Form 10-K and subsequent reports on Forms 10-Q and 8-K.

During this call, we will also refer to certain non-GAAP financial measures, including adjusted earnings per share, adjusted operating income, adjusted effective tax rate and adjusted cash flow from operations, which are reconciled to U.S. GAAP measures in Note 2 non-GAAP information included in our press release and in today's presentation's appendix.

Now I'm pleased to turn the call over to Jim Zallie.

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**James P. Zallie** - *Ingredion Incorporated - President, CEO & Director*

Thanks, Ryan, and welcome to everyone joining us today. I would like to begin today's call with a perspective on our business performance during the second quarter. For the quarter, our global net sales were down 4% due to the impact of foreign exchange weakness. Absent the foreign exchange impacts, net sales were up 1% versus the prior year.

Our sales teams continue to take aggressive pricing actions and delivered $39 million of favorable price increases in the quarter versus the year ago period. Operating income from the quarter was down 11% year-over-year, 7 percentage points of which were due to negative foreign exchange translation impacts. As we discussed last quarter, our North America business has faced a challenging raw material market and is lapping higher co-product values. Additionally, the unresolved U.S.-China trade dispute continued to create crop inventory imbalances, which reduced co-product values. These factors have resulted in a higher net cost of corn. As we navigate these challenges, we remain focused on strategic initiatives to forge growth and drive value creation.

We're pleased that specialty ingredients delivered net sales growth in the quarter, led primarily by sugar reduction and specialty sweeteners. In the second half, we will begin allulose production at our manufacturing facility in San Juan del Río, Mexico, which will complement our existing portfolio of specialty sweeteners. Enabling us to capitalize on the growing consumer demand for plant-based foods, our previously announced joint venture with Verdient Foods is progressing well. We are actively filling our customer pipeline for animal nutrition and consumer food products and anticipate incremental sales in the second half of this year. Building on this momentum, we are pleased to announce that we've expanded our relationship with Verdient to broaden our protein portfolio. This will further increase our capacity to produce food-grade, specialty pulse-based concentrates and flours from peas, lentils and fava beans. This enables us to even be better positioned to meet the growing demand from our customers for consumer-preferred plant-based foods. We provided details of this exciting development in the news release that was issued earlier today.

We also expect to be operational at our South Sioux City Nebraska plant, producing pea protein isolates for customer qualification by the end of this year.

In our starch-based texturizers growth platform we are making good progress, expanding our production of specialty potato food starches as we integrate Western Polymer's manufacturing capabilities into our network.

By broadening our portfolio of consumer-preferred specialty ingredients, we are increasing our capabilities to co-create with customers to drive growth. With cost also as a strategic priority for Ingredion, we have accelerated our Cost Smart savings program. I am really pleased about the excellent progress we're making on multiple fronts, and we're exceeding our 2019 savings target. Our teams are identifying ways to remove complexity, eliminate barriers to execution, improve effectiveness and efficiency and operate with increased agility. We now expect to deliver $30 million to $40 million of 2019 year-end cumulative run rate savings. This is an increase from our previously communicated savings target of $24 million to $34 million.

Now moving to North America, net sales were down for the quarter. Although, we continue to deliver specialty volume growth, this was more than offset by the planned Stockton volume shed of high-fructose corn syrup and industrial starch. North America operating income was $139 million, down 7% from last year. The decrease was driven by higher corn costs and lower co-product values and the timing of scheduled plant maintenance at Argo, our largest facility.

In South America, net sales were down due to foreign currency weakness, primarily in Argentina and Colombia. However, we delivered volume and net sales growth in Brazil and took aggressive pricing actions across the region. Operating income was $16 million, down 20% from the year ago period, driven by significant foreign exchange impacts primarily in Argentina and in Columbia. This was partially offset by low double-digit organic operating income growth in the region, including specialty sales growth.

In Asia Pacific, net sales were down for the quarter due to unfavorable foreign exchange impacts across the region. We continue to deliver top line growth and margin recovery in ASEANI, driven by increased tapioca pricing. Operating income was $23 million, down 15% versus the prior year. The region experienced slower economic growth due to the impact of trade disputes and weaker foreign exchange rates, which drove [higher] (added by company after the call) input costs across the region.

Moving to EMEA, net sales were down, given currency devaluation in Pakistan and foreign exchange weakness in Europe. Operating income was $23 million, down 21% from a year ago. Unfavorable foreign exchange impact across the region, driven primarily by the Pakistan rupee devaluation and higher raw material costs were partially offset by strong pricing actions.

Now let me turn it over to Jim Gray, who will review the financial results in more detail. Jim?

**James D. Gray** - *Ingredion Incorporated - Executive VP & CFO*

Thank you, Jim. Net sales of $1.4 billion were down 4% for the quarter. Gross profit margin was lower by 110 basis points, driven by foreign exchange impacts and higher material costs across the regions.

Reported and adjusted operating incomes were $168 million and $178 million, respectively. Second quarter reported operating income was lower than adjusted operating income by $10 million due to restructuring costs related to our Cost Smart savings program and Western Polymer integration.

Our reported and adjusted earnings per share were $1.56 and $1.66, respectively.

Q2 net sales of $1.4 billion were down $62 million from the same quarter last year. Unfavorable FX of $77 million was [primarily] (added by company after the call) attributable to weaker currency valuations. Lower volumes accounted for $24 million of sales decrease, while favorable price and product mix were a $39 million increase, or 3% of net sales.

In North America, volume was down year-over-year, driven by volume shed as we ceased wet milling at our Stockton facility in November 2018. This was the first full quarter of volume shed impact year-over-year as we continue to serve customers into Q1 through the end of their contracts.

Price/mix in North America was flat.

In South America, foreign exchange devaluation in Argentina was the largest driver of year-over-year net sales decline. Volume was up modestly at 1%. Price and product mix were up 12% as our teams took price increases to pass through higher material costs and recapture some of the foreign exchange impacts that we've been experiencing in Argentina and Brazil. APAC had a 3% net sales decline due to foreign exchange impacts and lower core volumes. This was partially offset by favorable price/mix from specialties growth.

EMEA experienced lower net sales due to foreign exchange impacts across the region that were only partially offset by favorable price/mix. For the quarter, reported and adjusted operating income decreased $25 million and $23 million, respectively.

North America operating income decreased $11 million due to higher net corn costs resulting from lower co-product values and timing of scheduled plant maintenance at Argo.

South America operating income was down $4 million, driven by the impacts of currency devaluation in Argentina, and a weaker Columbia peso.

Asia Pacific operating income was down $4 million from the year ago period. Higher regional [corn] (added by company after the call) costs, primarily in Korea, and foreign exchange impacts were partially offset by specialty volume growth and improved price/mix.

EMEA operating income was down $6 million from a year ago. Unfavorable foreign exchange impacts, including Pakistani currency devaluations and higher corn costs were partially offset by improved price and product mix.

Corporate costs were lower by $2 million for the quarter, driven by Cost Smart savings offsetting inflation.

Let me turn to the second quarter earnings per share. On the left side of the page, you see the reconciliation from reported to adjusted. On the right side, operationally, we saw a decrease of $0.22 per share, foreign exchange impacts were unfavorable $0.13 per share, while margin was a decline of $0.09 per share, attributable to higher net corn costs experienced within our regions.

Moving to our nonoperational items. We saw an increase of $0.22 per share for the quarter, largely driven by lower financing costs, favorable tax and lower average shares outstanding. Financing costs were net $0.08 per share favorable, which included lapping of foreign currency valuation charges related to Argentina in the prior year. Lower adjusted taxes contributed a $0.02 per share increase, shares outstanding contributed a benefit of $0.12 per share.

Let me turn to our year-to-date financials, which I will cover quickly. Net sales were down 4% year-to-date; reported and adjusted operating incomes were $329 million and $344 million, respectively; reported operating income was lower than adjusted operating income by $15 million. This difference is due to severance and other costs related to Cost Smart of $13 million and Western Polymer integration cost of $2 million. Our reported and adjusted earnings per share were $3.04 and $3.20, respectively.

Moving to the net sales bridge. Our year-to-date net sales were down 4% versus last year. Unfavorable foreign exchange has negatively impacted net sales by $171 million. Volume declines of $57 million primarily in North America and South America were offset by $117 million of favorable price and product mix. By region, we see unfavorable foreign exchange impacts across South America, EMEA and Asia Pacific.

Volumes for the first half were down 2%, driven by North America, partially attributable to volume shed from our Stockton closure and South America's volume weakness in the first quarter. Price and product mix is up 4%, with South America and EMEA continuing to lead aggressive pricing actions. Year-to-date, reported and adjusted operating income decreased $61 million and $57 million, respectively. North America's operating income decreased by $29 million due to higher net corn costs as a result of lower co-product values, higher inventory and production costs and a modest impact from the extreme weather in the U.S. and Canada.

Remaining regions are down primarily due to foreign exchange impacts and higher input costs. Corporate costs were lower by $4 million given the same reasons mentioned previously.

Moving to earnings per share. Operationally, we saw a decrease of $0.58 per share, primarily driven by foreign exchange impact of $0.28 per share and margin decline of $0.26 per share.

Moving to our nonoperational items. We saw an increase of $0.18 per share for the first half, primarily driven by lower shares outstanding. Higher adjusted taxes contributed a $0.09 per share decrease. The increase in the effective income tax was driven primarily by a favorable lap of 2018 excess tax benefit related to share-based payment awards.

Moving to cash flow. Cash provided by operations for the first half of the year was $253 million. Capital expenditures of $156 million, down slightly from the prior year ago period. Acquisitions and investments were $52 million, reflecting investments in Western Polymer and other ventures.

Turning to our income statement outlook. We expect modest growth in the second half of the year. However, due to the recent run-up in corn cost from heavy rains and delayed planting season in the U.S., we anticipate higher prices for corn in the second half in North America. Our adjusted EPS guidance for 2019 is now in the range of $6.60 to $6.90. We expect net sales to be flat to slightly down, and adjusted operating income to be down versus last year.

FX impact is expected to be negative $0.42 to $0.50 a share with continued currency weakness in EMEA due to Brexit and softer Asia Pacific economic growth.

We expect corporate expenses to be moderately higher year-over-year as we invest in global business process optimization and innovation, partially offset by Cost Smart savings.

2019 financing costs are expected to be in the range of $80 million to $85 million. Our adjusted effective annual tax rate is expected to be between 26.5% and 28%.

We expect total diluted weighted average shares outstanding to be in the range of 68 million to 69 million for the year, considering the impact of the accelerated share repurchase agreement. As Jim mentioned earlier, Cost Smart is now expected to deliver $30 million to $40 million in 2019 year-end cumulative run rate savings.

In North America, 2019 net sales and operating income are expected to be down, assuming current market conditions for corn and co-products, which have been negatively impacted by excessive rain and late crop plantings in the U.S. as well as continued crop inventory imbalances arising from the U.S.-China trade dispute.

Moving to South America. Net sales and operating income are expected to be flat. Volumes are expected to be up modestly.

2019 Asia Pacific net sales are expected to be modestly up, however, operating income is expected to be down due to foreign currency weakness across the region and the impact of trade disputes on lower volume demand and corn costs in Korea.

Moving to EMEA. We expect net sales to be modestly up. We anticipate specialties growth in Europe and core growth in Pakistan. We expect operating income to be down due to currency impacts throughout the region, higher corn costs in Pakistan and a prolonged impact from Brexit towards the end of the year.

In 2019, we expect cash from operations to be in the range of $610 million to $660 million. We expect to invest between $330 million and $360 million in capital expenditures, of which, a significant portion supports our specialty growth platforms.

That brings my comments to a close. Now back to Jim Zallie.

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**James P. Zallie** - *Ingredion Incorporated - President, CEO & Director*

Thanks, Jim. As you heard from me and Jim today, we continue to navigate a very challenging global business environment, while remaining intentionally focused on advancing our roadmap for driving growth. This roadmap is defining our strategic direction, the value propositions we offer customers and the value-creation opportunities for our shareholders.

We are strengthening our specialty growth platforms in the areas of sugar reduction and specialty sweeteners, plant-based proteins and starch-based texturizers. By broadening our consumer-preferred specialty ingredients portfolio, we are also increasing our solutions capabilities to co-create with customers to drive growth. This work continues to be anchored by our purpose and performance-driven culture. In our most recent annual report, we shared our refreshed values and unveiled an inspiring core purpose statement that guides our actions. By aligning our talented and engaged workforce around our values and purpose, we are strengthening our business culture, while driving transformation and growth.

Now let's open the call for questions.

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## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions) And our first question today comes from the line of Brett Hundley with Seaport Global Securities.

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**Brett Michael Hundley** - *Seaport Global Securities LLC, Research Division - Research Analyst*

Jim Gray, can you just remind me how corn basis affects the company? And whether or not you guys are taking a look at changing how you -- if and how you can cover corn basis?

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**James D. Gray** - *Ingredion Incorporated - Executive VP & CFO*

Sure. Brett, just for everyone on the call because all might not be familiar with corn basis. So we buy corn, and on top of that, there is usually a transportation or a small brokerage fee to deliver the corn to our various facilities. And I think what Brett is alluding to is that we've seen the Eastern corn belt have a near-end shortage of corn and so basis costs have risen. Generally, about half -- to remind everybody, half of our contracts are really passed through the cost of corn to our customers. Included in that is a reference to basis depending upon which plant our customer is purchasing corn from. And the other part of our customer base, which is more of a fixed price type of contract, we usually include some thoughts around basis, our expectation for basis with the gross cost of our corn when we follow our hedging policy. So if you see a run-up in the spot price of corn, if you see a run-up in the cost of basis, generally, it's going to be -- lead to just basically a higher net cost of corn, and over time, what we're trying to do is really figure out how we pass that through to customers.

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**Brett Michael Hundley** - *Seaport Global Securities LLC, Research Division - Research Analyst*

And then just on the sweetener side. I had a question that aimed to tie together bulk sweeteners with specialty, particularly as we head into 2020. So many beverage companies out there have obviously been working on low or no-calorie drink innovation in recent years and some of these products, I think, are really starting to help lead beverage company results higher. A lot of the ingredient players out there, including yourself, are developing solutions around differing specialty sweeteners, and you guys mentioned allulose in your prepared remarks. From the wet miller's perspective, what does the negotiation with beverages companies look like? And does it tie back at all to bulk sweetener for those of you that supply such products? Like, I guess, how separate are those 2 business segment interactions when you're dealing with the larger beverage companies out there?

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**James P. Zallie** - *Ingredion Incorporated - President, CEO & Director*

I don't think they really are that separate. I think the contracts that we've had -- the deep contracts that we've had for so many years with the large beverage companies supplying sweeteners, caloric sweeteners, ties in very well to the innovations that they are trying to drive for lower-calorie, mid-calorie and no-calorie type beverage innovation. So our sweetener capabilities which are enhanced by our position with Stevia, BESTEVIA, the Reb M product that we have as well as allulose, which will be coming, and those 2 ingredients complement each other very well, along with our portfolio which we have developed, which was one of the reasons why we've done so well this past quarter is related to non-GMO sweeteners for food products as well. I think, all puts us in a very good position to, again, co-create with customers for sugar reduction.

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**Brett Michael Hundley** - *Seaport Global Securities LLC, Research Division - Research Analyst*

And then just a final question for me, and then I'll hop off is, I did wanted to go back to the plant protein update. And I had 2 questions for you guys there. So number one, a number of newer plant-based protein companies or using soy isolate in their products. Do you guys understand their desire to move to be pea protein, if, in fact, that has become more readily available? So just trying to understand what those discussions look like as you ramp your capabilities. So that's the first question relates to soy isolate potentially going over the pea protein. And then secondly, do you guys have any interest in producing corn protein from the kernel? And would that displace co-products in anyway?

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**James P. Zallie** - *Ingredion Incorporated - President, CEO & Director*

Let me just take the question in relationship to soy versus pea. I think that there -- to your point of -- there is a variety of plant-based proteins that are being used and formulated to meet the emerging accelerating demand for meat alternatives and alternatives dairy products, et cetera. Soy is very well established and is more plentiful today than pea. So -- and pea though has very good functional properties and advances have been made from a standpoint of flavor and taste. So soy also has some concerns from some consumers in relationship to allergenicity, the way it's processed and extracted as well as GMO status. So pea, on the other hand, overcomes those and is more desirable, but there is a supply/demand imbalance where demand is outstripping supply right now. So that's why we felt investing in pulse-based products, non-soy, is even more on trend within the plant-based foods growth category. And so we think the investments that we have made good will put us in a very good position given than supply/demand imbalance and the complementary portfolio of pulse-based products, lentil, flava, and pea isolates. So that's how I kind of would explain that. In relationship to the corn protein, corn protein is an insoluble protein and it has more limitations in relationship to functionality. But we'll be looking at protein sources as part of our very comprehensive approach. Over the next 5 years, we're going to be continuing to invest and broaden our research and development capabilities as a well as our sourcing capabilities for a variety of plant-based proteins. I think the CEO of Beyond Meat just yesterday talked about the breadth of plant-based proteins that they're going to pull from to formulate with, and you're seeing that today, and so that will be consistent with our strategy as well.

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**Operator**

And we do have a question from the line of Rob -- I'm sorry. Ken Zaslow, with Bank of Montréal.

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**Kenneth Bryan Zaslow** - *BMO Capital Markets Equity Research - MD of Food & Agribusiness Research and Food & Beverage Analyst*

Just couple of questions. One is, seems like the earnings adjustment is related to the FX as well as higher corn prices. So just two points on this. One is, in history, you've been able to price through the FX over time. So is it fair to say that, in 2020, you'd actually regain anything that you'd lost on the FX, assuming FX stabilizes? And then the second part is, when did you change the policy -- or how much do you change in policy on locking in North American corn versus high fructose corn syrup? I was always in the impression that you largely kept, in the September to January period, that you locked in high fructose corn syrup and locked in corn, this year seems to have been a little bit of a divergence from that. Can you talk to those 2 points?

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**James P. Zallie** - *Ingredion Incorporated - President, CEO & Director*

Yes. Let me take the first one, Ken, and then I'm going to turn the second one over to Jim Gray. So just kind of relationship to ForEx, it is absolutely our policy that we work diligently and have, over many years, to pass through the effects of foreign exchange. What I would say is that within the last 18 months, the magnitude and the pace of foreign exchange devaluations in non-U. S. dollar-denominated currencies has been absolutely extraordinary and unrelenting. So just in the quarter, we had $77 million of ForEx impact, and $48 million of which was in South America alone, $13 million was in Pakistan, for example. The Columbia peso, which has been strong forever, or pretty stable forever, devalued significantly. So what I would say is that we're in catch-up mode, and we're passing through. If you look through some of the numbers that we've provided in the last few earnings call, in a quarter, we're catching up 60% to 70% of the ForEx devaluations through -- putting through price increases. So we're rowing very hard, and I think, in successive quarters, we will catch up. But it's extraordinary, the devaluations that we're experiencing. I think we've all seen that the British pound is devalued now to a 34-year low and it's just extraordinary the amount of devaluation in foreign currency. But we have been demonstrating that we've been putting through significant pricing and also, at that same time, upgrading our mix and driving specialties growth where we can to offset some of these unprecedented ForEx headwinds. And I'm going to let Jim comment on the corn piece.

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**James D. Gray** - *Ingredion Incorporated - Executive VP & CFO*

Ken, maybe to your question with regard to how we look at the layout of corn, and how we hedge against that. One, there hasn't been any policy change. Generally, when we're contracting with customers, and they have a firm price that we're providing to them as well as the volume commitment from the customer, we're usually thinking about covering the corn that we need to produce the product for them in the first, second, third quarter. As we move through the year, we get into Q2. Now we're thinking about what hedges we would need to be laying on for the Q3 and the Q4 production. So we don't hedge 100% because we also will have -- if you have changes in the gross cost of corn, you usually have a parallel change in the co-products that we sell. And so they act as a bit of a natural hedge. I think what we're seeing is that you have late plantings in spring, a run-up in what the future cost of corn is expected, primarily in Q4, and yet, we haven't really seen co-product values move yet. Feed moved a little bit up, but really, corn gluten meal and corn oil have really stayed flat. So we have a bit of a widening exposure. All it does is just it increases the cost of our corn, it's more towards the end of the year for North America. We're being prudent in saying, currently, right now, that's what we're looking at. And as we move into next year, clearly, that's an exposure that's in our P&L and we'll be talking to customers about how the underlying corn market has changed.

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**Operator**

And we do have a question from the line of Heather Jones with Heather Jones Research.

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**Heather Lynn Jones** - *Heather Jones Research LLC - Founder*

So just a quick detail-ish question. Your forward guidance, does that assume where current futures are and basis trends? You mentioned the Eastern corn belt. So assume where those are currently or are you assuming some appreciation in corn?

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**James D. Gray** - *Ingredion Incorporated - Executive VP & CFO*

Yes. When we're looking at pulling together a forecast that supports our outlook, we're always just taking, at that particular point in time, what the layout of the futures of the corn market look like. And so what we were previously looking at, early May of last year, was probably futures layout between $3.60, $3.70 a bushel. And we've seen stuff move up to north of $4 a bushel, $4.20, $4.30 a bushel. And so really what we're considering is, is like some of that in your December future is really more what we're kind of thinking now in our consideration.

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**Heather Lynn Jones** - *Heather Jones Research LLC - Founder*

And then going to the by-products. Like you said, those have been incredibly depressed. So I understand that about half of your more commodity like business in the U.S. is cost-plus. On the other half, what do you think the likelihood is of you being able to renegotiate those going into 2020? You're basically take pricing higher to offset the high -- the lower co-products. And could you help us understand how your specialty contracts are set up with regards to the by-products because these values have been depressed for a while, and given there are ongoing trade issues, it wouldn't seem like a recovery is around the corner. So just -- how are you guys thinking about positioning us for that going into late '19 and into 2020?

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**James P. Zallie** - *Ingredion Incorporated - President, CEO & Director*

Yes. I mean, historically, our business model, over time, passes through the change cost of corn and we expect to do the same going forward and that would be into next year as well. Clearly, the entire industry is being impacted right now by the run-up in gross corn costs. The impact to net corn costs by the continued, I'm going to call it, say, structural -- you can say structural decline in the soy corn complex related to this China trade dispute, which appears to be very protractive, longer than, I think, most of the industry thought. Then on top of it, you have the run-up in basis due to historically late corn plantings and the impact that that's had on the entire corn belt, and Jim referenced the Eastern corn belt and what that's done to basis. So the entire industry is experiencing an unprecedented run-up based on a variety of factors, some of which we've seen that have been weather-related in the past, but some that we haven't seen from a standpoint of a dislocation and how the corn versus soy complex kind of trades. So I think with that as the backdrop to me, that's the overriding factor that we, as a company, will be focused on as we go into contracting next year. Historically, our business model allows us to pass through that changing cost of corn in the marketplace, and we expect to do that as we go forward.

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**James D. Gray** - *Ingredion Incorporated - Executive VP & CFO*

I mean, Heather, and just remind everybody, when you look at syrups and when you look at industrial starches, the cost of the raw material is a higher portion of the overall cost structure. So if you have underlying costs increasing, then that's a discussion that you need to have with customers. To maybe address your latter question, which was really around specialty and the input of specialty corn, while we use some different types of corn to create our specialties, and also we have a large tapioca franchise, on a comparative basis, the cost of the raw material in a specialty is less. And we have more value added from how we finish the final product that we're providing to customers. So it tends to be slightly more insulated versus the volatility of what we might see on the impact of cost of sales on a syrup.

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**Heather Lynn Jones** - *Heather Jones Research LLC - Founder*

Okay. My final question is just, going back to your plant-based investments and you're ramping those up and then allulose, could you give us a sense of where -- I mean because demand trends are clearly strong and are accelerating. So where is your expectation as far as those businesses could be at a revenue run rate basis by late 2020, early 2021?

**James P. Zallie** - *Ingredion Incorporated - President, CEO & Director*

Well, what I would say is that, just -- we're really very excited about the specialty growth platforms and the recent investments we're making to build the capacity to allow us to meet the increasing customer demand. And just to start with plant-based proteins, since we made the commitment to enter the plant-based protein isolate market with significant investments in South Sioux City, Nebraska, to your point, the market has continued to grow significantly. There were some statistics that just came out very recently that the plant-based food market is estimated to grow from $3.4 billion to $4.5 billion from '17 to '19, and the global alternatives market is expected to hit $13 billion by 2024. What we said at CAGNY is that the investments in our plant-based protein growth platform, between now and 2022, will reach $100 million in sales. And we've announced an additional investment with Verdient to expand our plant-based protein just today. So it will be something that would be on top of that. And what I would say is that we see tremendous customer interest. We'll be offering a complete portfolio and variety of pulse flours concentrates and isolates. And one of the things that we also have which complements plant-based proteins is the deepest and broadest portfolio of specialty starches and that deep knowledge of the role texture plays in food systems. So combined with the leadership position in specialty starches, we think we're very well positioned to co-create innovative new plant-based foods with our customers. And what we said at CAGNY, we would stand by, especially given the fact we're making -- we've even made a further commitment and an investment to expand even quicker with Verdient.

**Operator**

(Operator Instructions) Our next question comes from the line of Adam Samuelson with Goldman Sachs.

**Adam L. Samuelson** - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

So I was hoping to dig a little bit more just on the guidance in the back half of the year, and just make sure that I'm clear on kind of the implied improvement both second half versus first half and on an operating basis year-on-year, and just the drivers in light of how corn costs have played out. And just help me think about what's improving within the portfolio or how the cadence of earnings kind of plays out to drive some -- both half-on-half improvement as well as, I think, year-on-year improvement if I'm doing this math right.

**James D. Gray** - *Ingredion Incorporated - Executive VP & CFO*

Sure. Is there -- I think what we suggested in the guidance if I looked at how both Q1 and Q2 have played out relative to lapse versus prior year. I think, across EMEA as well as South America, you've -- we've probably seen some of the kind of the impact from FX has really played out in the first half. Now we're going into the second half other than maybe the Pakistani devaluation that occurred in here in Q2, we're looking really looking at I think an easier second half, and therefore, we're alluding to what we see is, basically, kind of flat guidance for South America. EMEA, we're still waiting on kind of now what the Brexit impact might be in Q3, Q4. With regard to Asia Pac, we do see that we do have some additional headwinds and it really is around how we're seeing a bit of growth slow in China. It's also impacting Korea as well as some of the other northern kind of Asia Pacific countries as well as we've seen really some weakening in the currencies there. And so product that comes over from the U.S. and/or cost of corn if it's purchased overseas, has a higher land and transactional cost. And so that's going to -- that's really probably the change in our thoughts as we look at Asia Pac. North America, we do see moderately up for the second half, primarily given the fact that we had some onetime headwinds in Q3 of last year. Those lingered and had some costs into Q4, and so we were at the -- I think, previously, when we thought about North America, we had taken to account both the cost of corn as well as the lower co-product values. Now we're just seeing, primarily in Q4, against North America's forecast, an expectation for a slightly higher cost of corn due to just kind of the things -- the way things are laying out right now. And we can -- hope that helps.

**Adam L. Samuelson** - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

It does. Just to be -- I was just trying to digest, relative to kind of where you were last quarter, just the entirety of the -- just -- is it fair to describe the decrement to guidance is entirely on higher corn costs, and we could use that as a baseline to think about the sensitivity that you have to corn prices. I'm just want to make sure we're framing this right because as corn markets remains volatile and it could be interesting to see how the USDA plays out in acreage and yields are small and in terms of the volatility in the corn market. Just trying to make sure I've got a better handle on the sensitivity to incremental perspective changes in the corn price?

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**James P. Zallie** - *Ingredion Incorporated - President, CEO & Director*

Yes. I would say that, in relationship to the second of impact and the impact that's had on our guidance, the run-up in corn cost, and what we project from what we sit today for the second half, is contributing about 2/3 to the impact that is baked into the guidance. The additional impact would come from the steepness of some of the ForEx devaluations that we talked about. Pakistan certainly, and Korea, that we've called out as well, some of that weakness that we've called our, which, again, hit us in the quarter and will carry through with us to the second half.

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**Adam L. Samuelson** - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

Okay. And then just lastly for me. As I think about -- assuming we're in a world now where corn is going to be 4-plus for next year, given the state of the U.S. crop this fall. How do you approach the pricing negotiations for next year? Just -- it would seem like the bar on required kind of pricing on HFCS and the other core products has gone up considerably, and what's already been a pretty tough demand environment and just how do you see the supply chain response to the kind of price increases that might require to cover or the demand you'll also see the higher HFCS prices needed to cover corn costs?

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**James P. Zallie** - *Ingredion Incorporated - President, CEO & Director*

Well, what I would say is that, we are experiencing, right now, a significant increase in overall corn costs, again, driven by those 3 factors that we talked about, just the overall gross corn cost just based on uncertainty about yields and the size of the crop and co-products, which remains at a structural lower level than it had historically. And then on top of that, you've got basis. So these are 3 real dramatic impacts to everyone in the entire industry. And so should those all continue as we head into contracting because it is a little early. Typically, that process begins in September through the end of the year, and we would provide market updates based on those changing corn and ag markets. So again, I think that will dominate the thinking in relationship to how we approach that and it's just a little early right now. And as you know, we don't typically comment on contracting at this point in time in the year.

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**Operator**

(Operator Instructions) It does appear at this time there are no further questions from the phone lines. Please continue.

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**James P. Zallie** - *Ingredion Incorporated - President, CEO & Director*

Okay. All Right. Well, I just wanted to thank everyone for their time today. And Jim and I both hope to see many of you in our travels in the near future. So thanks very much for your time and attendance today. Thanks.

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**James D. Gray** - *Ingredion Incorporated - Executive VP & CFO*

Okay.

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**Operator**

And ladies and gentlemen, today's conference will be available for replay after 9:30 a.m. today through August 8. You may access the AT&T teleconference replay system at any time by dialing 1 (800) 475-6701, entering the access code 469695. International participants may dial (320)

365-3844. That does conclude your conference for today. Thank you for your participation and for using the AT&T executive teleconference service. You may now disconnect.