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INGR.N - Q4 2022 Ingredion Inc Earnings Call

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**OVERVIEW:**

INGR reported full-year 2022 net sales of almost $8b and reported diluted EPS of $7.34. Co. also reported 4Q22 net sales of approx. $2b and reported diluted EPS of $1.71. Expects 2023 reported and adjusted EPS of $7.70-8.40.

## CORPORATE PARTICIPANTS

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**Noah Weiss** *Ingredion Incorporated - Vice President of Investor Relations & Corporate Communications*

## CONFERENCE CALL PARTICIPANTS

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## PRESENTATION

**Operator**

Good day, and thank you for standing by. Welcome to the Ingredion Incorporated Fourth Quarter and Full Year 2022 Earnings Conference Call. (Operator Instructions) Please be advised that today's conference is being recorded.

I would now like to hand the conference over to your speaker today, Noah Weiss, Vice President of Investor Relations. Please go ahead.

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**Noah Weiss** - *Ingredion Incorporated - Vice President of Investor Relations & Corporate Communications*

Good morning, and welcome to Ingredion's Fourth Quarter and Full Year 2022 Earnings Call. I'm Noah Weiss, Vice President of Investor Relations. On today's call are Jim Zallie, our President and CEO and Jim Gray, our Executive Vice President and CFO.

The press release issued today and the presentation we will reference for the fourth quarter and full year results can be found on our website, ingredion.com, in the Investors section. As a reminder, our comments within this presentation may contain forward-looking statements. These statements are subject to various risks and uncertainties and include expectations and assumptions regarding the company's future operations and financial performance. Actual results could differ materially from these estimated in the forward-looking statements, and Ingredion assumes 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 could be found in the company's most recently filed annual report on Form 10-K and subsequent reports on Form 10-Q and 8-K.

During this call, we also refer to certain non-GAAP financial measures, including adjusted earnings per share, adjusted operating income and adjusted effective tax rate, 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*

Thank you, Noah, and good morning, everyone. I am pleased to report that for 2022, Ingredion delivered outstanding performance with top line and adjusted profit growth growing 15%. We finished the year with a strong fourth quarter with net sales up 13% and adjusted profit growth up 49%. Our teams demonstrated resilience and agility throughout 2022 as they overcame macroeconomic headwinds while executing against our driving growth roadmap while also expanding and transforming our solutions and opportunity set with customers.

2022 was yet another year of unexpected challenges that demonstrated the strength of our business model and the ability of our teams to anticipate and respond effectively. Our largest raw material input, corn was significantly impacted by both the Ukraine conflict and a drought in Europe. Yet despite those supply shocks, our team was able to secure raw material, keep our customers supplied as well as overcome unexpected raw material inflation. Also related to corn and energy, we expanded our hedging practices to mitigate profit volatility and an approach that we will continue to follow going forward. The strong demand we experienced last year, coupled with supply chain constraints, provided the opportunity to drive value creation from customer and product mix management, which was enabled by improving the terms of customer contracts.

Furthermore, despite a significant strengthening of the U.S. dollar, and 2/3 of our sales being outside of the U.S., we successfully offset more than $200 million of foreign exchange headwinds. Lastly, I'm especially proud of the work our team did ramping up production and sales from our new Shandong facility despite countrywide COVID challenges. With expanded capacity for specialty modified starches, our business in China is well positioned for accelerated growth as the economy reopens.

As we look to 2023, we are focused once again on addressing head on many of these same challenges, even as some begin to diminish. We will continue to utilize the levers available to us, whether it's the capacity expansions we've invested in for growth, pricing to offset inflation, operational efficiencies for cost reduction, or expanded risk management practices, all to deliver against our growth objectives.

Turning to our performance. We finished the year strong, delivering record top line performance for the fourth quarter, with sales growing 13% and adjusted operating income increasing 49% or up 57% on a constant currency basis. For the full year, top line and adjusted operating income performance was also outstanding, both achieving 15% growth compared to the same period last year. These results were driven by robust performance across both core and specialty ingredients.

Additionally, we continue to successfully offset higher raw material and logistics costs as well as significant foreign exchange impacts. Looking at the net sales performance in a little more detail. From a segment perspective, all 4 regions generated strong net sales for the full year and fourth quarter led by North and South America. Notably, on a constant currency basis, Asia Pacific and EMEA demonstrated considerable -- considerably stronger results.

Turning now to our strategic pillars. During the fourth quarter and full year, our teams did an exceptional job of executing with agility across our 4 strategic pillars. Beginning with specialties growth. Last quarter, we updated you on the progress we are making to expand our starch-based texturizer network capacity to further enhance the resiliency of our global supply chain. Of the $160 million investment, I'm pleased to report that we have completed 1/3 of the capital installations. This strategic set of investments will provide headroom for growth. Reduce local delivery costs and improve service by shortening supply chains.

Turning to commercial excellence. Our pricing centers of excellence, supported our sales teams to deliver $1.3 billion of net sales growth through pricing pass-through of input cost inflation and customer and product mix management. If we look at specialty ingredients more broadly, this business grew double digits, both for the quarter and full year. This sustained momentum continues to validate the significant ongoing investments we are making to transform our portfolio toward on-trend and more competitively differentiated and unique ingredient solutions.

Against our all life sustainability goals. In the fourth quarter, we reached 47% sustainable sourcing of our 5 priority agricultural inputs, up from 33% last year. We are tracking well against our goal to achieve 100% sustainable sourcing for our 5 priority crops by 2025. We are equally excited about the potential to drive value creation from our third strategic pillar, cost competitiveness through operational excellence. We are holistically assessing how we buy, make and move our raw materials and finish products effectively to customers and at the lowest cost. In this regard, we are making investments to enhance supply chain connectivity and visibility and drive digital transformation of the factory floor. In addition, we are extending our global operating model to bring together our global procurement organization. This represents an opportunity to better leverage our global scale and build more value-creating supplier relationships.

It is also noteworthy to highlight that once again, this past year, we deployed expanded raw material risk instruments to reduce cost volatility. This was also a contributor to our overall strong performance. Lastly, we continue to advance our purpose-driven and people-centric growth culture. We are pleased to have been recognized as a top employer in 5 Asia Pacific countries. And in early December, our 2030 emissions reduction targets were validated by SBTi.

Let's now turn to the progress we are making within a couple of our specialty growth platforms and discuss how we are continuing to invest to lead in these growing markets. First, beginning with sugar reduction and specialty sweeteners. We delivered over $400 million in net sales with strong double-digit growth again in the quarter. PureCircle's talented go-to-market team delivered 14% net sales growth and positive operating income by volume and breakthrough product innovations. We are excited by the tremendous opportunities we see for our sugar reduction franchise worldwide. I'm also pleased to mention that we increased our ownership of the PureCircle business to 87% up from our original 75% stake.

Turning now to our plant-based proteins business. Net sales for 2022 were $36 million, up 118% from the prior year period. Although sales doubled and our profitability slightly improved, we did not grow the top line nor reduced the operating losses as much as we had expected. Our South Sioux City facility is laser-focused on improved product quality attributes that we believe will appeal to broader market segments. We see exciting growth opportunities in fortified bakery, alternative dairy, sports nutrition and beverages. We continue to see the current $10 billion market for plant-based proteins, which is growing steadily at more than 6% per annum as an exciting growth opportunity. We remain committed to our strategy to execute upon a formulation approach towards structuring and fortifying plant-based foods with a leading portfolio of protein flowers, concentrates and isolates.

A new highlight in specialties we wanted to mention is our expansion into pharmaceutical applications and investments in India. During the second half of the year, we made 2 acquisitions in India in the high-value pharma ingredient space with our Q3 purchase of Amishi and our quarter 4 acquisition of Mannitab. These additions are part of our strategy to selectively expand our pharma ingredient portfolio and diversify into high-value nonfood adjacencies. Both acquisitions complement our existing global pharma footprint and add capabilities on the ground in India, which is one of the fastest-growing specialty pharma markets. We anticipate double-digit net sales growth and above average gross margins as we grow these 2 businesses.

Now let me hand it over to Jim for the financial review, after which I'll make a few concluding remarks before we open it up for Q&A. Jim?

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**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Thank you, Jim, and good morning to everyone. Moving to our income statement. Net sales of approximately $2 billion were up 13% for the quarter versus prior year. Gross profit dollars and margins were higher year-over-year up 120 basis points from Q4 last year. Reported and adjusted operating income were $157 million and $168 million, respectively. Reported operating income was lower than adjusted primarily related to costs pertaining to the U.S.-based work stoppage at our Cedar Rapids facility.

I'm happy to share that on January 22, we ratified our agreement with the union. We anticipate some costs related to the work stoppage in the first quarter of 2023, but not to the extent of prior quarters. Our fourth quarter reported and adjusted earnings per share were $1.71 and $1.65, respectively, for the period, up significantly from the prior year.

Turning to our Q4 net sales bridge. We achieved strong price/mix of $336 million including the pass-through of higher corn and input costs. This was partially offset by foreign exchange impacts of $65 million and decreased sales volume of $39 million.

Turning to the next slide. We highlight net sales drivers for the fourth quarter. Of note, foreign exchange was a minus 4% headwind in the quarter, with the most significant impacts in Asia Pacific and EMEA. It is worth noting that lower volumes were primarily driven by unique events within some countries. For example, within Asia Pacific, in Korea, the rapid increase in corn costs led to pricing events in the second half of the year, which impacted our core ingredients volume.

Furthermore, Pakistan's macroeconomic challenges have led to overall softer demand. As we mentioned previously, the Ukraine-Russia war created a shortage in corn export supply. And consequently, prices rose globally soon after. Historically, in rising corn cost market cycles, our pricing has lagged the change in the cost of corn, and subsequently, our gross margin percentage has been compressed. Of note, even though corn costs increased 18% in the quarter based upon the index shown here, we were able to expand gross margins. This result is more evidence of the resiliency that we are building into our business processes and practices to flatten the impact of changing corn and co-product values throughout the year.

Turning to our earnings bridge. On the left side of this slide, you can see the reconciliation from reported to adjusted earnings per share. On the right side, operationally, we saw an increase of $0.62 per share for the quarter. The increase was driven primarily by an operating margin increase of $0.82, partially offset by unfavorable foreign exchange of minus $0.10, and unfavorable volume of minus $0.09 per share.

Moving to our nonoperational items. We had a decrease of $0.06 per share in the quarter. The decrease was primarily driven by higher financing costs of minus $0.15.

Now let's move to a brief review of full year results. Net sales of almost $8 billion were up 15% versus prior year. Gross profit margin was 18.8%, down 50 basis points. Full year reported and adjusted operating incomes were $762 million and $787 million, respectively. Reported operating income was lower than adjusted operating income primarily due to restructuring and other costs. Our full year reported earnings per share was $7.34 and adjusted earnings per share was $7.45.

Turning to our full year net sales bridge, 15% net sales growth has been driven by $1.3 billion of not only price pass-through but also improvements to our customer and product mix.

Turning to the next slide. We highlight net sales drivers for the full year. Strong price mix of 19% was partially offset by minus 3% of FX and minus 1% of sales volume on a reported basis. When we adjust for the Argentina JV, net sales for South America would have a positive 2% contribution from sales volume. For the company, the volume contribution to net sales would improve to a positive 2%.

Let me turn to a recap of full year regional performance and update you on specialty ingredients mix. North America net sales were up 19% when compared to the same period in 2021. The increase was driven by strong price mix where dynamic pricing and a richer contribution from specialty products helped to drive top line performance. North America operating income was $565 million, up 16% versus the prior year, driven by favorable price mix and expanded raw material risk management. In South America, comparable net sales were up 23% versus prior year. It is worth noting that specialty ingredients have grown significantly and now represent 22% of the region's net sales. South America operating income was $169 million, up 22%, which increases predominantly driven by favorable price mix, partially offset by higher corn and input costs.

Moving to Asia Pacific. Net sales were up 11% for the full year and up 19% on a constant currency basis. Asia Pacific operating income was $93 million, up 7% versus prior year, with favorable price mix that was partially offset by foreign exchange impacts and higher input costs, notably in Korea. Excluding foreign exchange impacts, adjusted operating income was up 17% for the full year. In EMEA, net sales increased 11% for the full year and absent foreign exchange impacts, net sales were up 25%. EMEA operating income was $110 million for the full year, up 4% compared to the prior year due to favorability in Europe, which was partially offset by macroeconomic challenges in Pakistan and foreign exchange impacts across the region. Excluding foreign exchange impacts, adjusted operating income was up 19% for the full year. Of note, in a year witnessing significant price increases across both core and specialty products. The proportion of Specialty Ingredients net sales grew or held constant in all 4 regions.

Turning to our earnings bridge. On the left side of the page, you can see the reconciliation from reported to adjusted. On the right side, operationally, we saw an increase of $1.12 per share for the full year. The increase was driven by margin improvement of $1.70, offset by foreign exchange of minus $0.33 and lower volumes of minus $0.23.

Moving to our nonoperational items. We saw a decrease of $0.34 per share driven primarily by higher financing costs of minus $0.23 and a higher effective tax rate of minus $0.17 per share.

Moving to cash flow. Full year cash from operations was $152 million. Our cash from operations has benefited from an increase in net income, which was more than offset by an increase in working capital investments. As even higher corn costs flowed through our financials beginning in Q1 2022, our working capital balances started to increase further as higher invoice prices pass through our accounts receivable and inflating corn costs were reflected in our inventory values. As we look to 2023, we expect higher invoice prices as we catch up in our contracted pricing with 2022's inflation.

Net capital expenditures were $293 million and in line with our 2022 expectations for capital commitments. With respect to acquisitions. In the quarter, we acquired additional shares of PureCircle for minority shareholders for $6 million, taking our ownership to 87%. For the full year, we returned $288 million to Ingredion shareholders, paying $176 million in dividends and repurchasing $112 million of outstanding common shares.

Now I'd like to introduce our 2023 outlook. We expect net sales to be up mid-double digits driven by strong price mix and volume growth. We expect reported and adjusted operating income to be up high single digits to low double digits compared to last year. 2023 financing costs are expected to be in the range of $106 million to $122 million, reflecting higher incremental borrowing costs. Our adjusted effective annual tax rate is anticipated to be between 26.5% and 28.5%. Cash flow from operations is expected to be in the range of $550 million to $650 million, which reflects an anticipated investment in working capital of approximately $200 million. Capital expenditures for the full year are expected to be approximately $300 million. We expect our full year 2023 reported and adjusted EPS to be in the range of $7.70 to $8.40. This excludes the impact of acquisition-related integration and restructuring costs as well as any potential impairment charges. We expect total diluted weighted average shares outstanding to be in the range of 66.5 million to 67.5 million for the year.

In terms of our regional outlook. North America net sales are expected to be up 15% to 20%, driven by favorable price and customer mix. Operating income is expected to be up low double digits driven by favorable price mix, partially offset by higher input costs. For South America, we expect net sales to be up 5% to 10%, reflecting favorable price mix. South America operating income is expected to be up low single digits with favorable price mix mostly offsetting higher input costs. In Asia Pacific, we anticipate net sales to be up 10% to 15% versus the prior year. We expect operating income to be up mid-double digits driven by favorable price mix and PureCircle growth, partially offset by higher input costs. For EMEA, we expect net sales to be up 25% to 30%, and we expect operating income to be up mid-single digits, as we navigate foreign exchange impacts in Pakistan's economic uncertainty. Corporate costs are expected to be up low single digits.

That concludes my comments, and I'll hand it back to Jim.

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

Thanks, Jim. I hope that our call today has been helpful in conveying the depth and breadth of Ingredion's achievements in 2022. As you heard, despite many challenges, we delivered very strong results. As I reflect on the past year and look forward to 2023, I'm confident that we are well positioned to continue to execute against our strategic pillars for growth. Our priorities will be to grow our specialty ingredients portfolio, drive plant-based protein sales, continued grind optimization and maximize value from finishing channels for core ingredients while also further mitigating profit volatility.

And lastly, invest in R&D to drive innovation and digital capabilities to transform the supply chain and enhance the customer experience.

In closing, we are confident that Ingredion is well positioned to continue to deliver sustainable growth and create value for our shareholders. Now let's open the call to questions. Operator?

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## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions) Our first question comes from the line of Ben Bienvenu with Stephens.

**Benjamin Shelton Bienvenu** - *Stephens Inc., Research Division - MD & Analyst*

Hey, thanks. Good Morning guys.

**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Hey,Ben.

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

Good Morning Ben.

**Benjamin Shelton Bienvenu** - *Stephens Inc., Research Division - MD & Analyst*

So I want to start with the guidance, the range of $7.70 to $8.40. Jim, could you talk a little bit about the elements that will create the variability in that range? How do we get to the top versus the bottom? And then also as a follow-up on guidance, what are you guys assuming with respect to FX?

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

Yes. So what I would say is, as we look at the balance in relationship to some of the watch outs as well as the opportunities. On the watch out side, clearly, macroeconomic factors that could impact customer demand. That all being said, the products that we supply are very diversified and versatile and they typically perform very well during periods of recession and periods of economic growth. But that's something that obviously we would watch out for. If there was some sort of a very poor crop for corn once again in perhaps North America or in Europe, and then clearly, foreign exchange, continued perhaps devaluations, that would be some of the watch out.

So on the opportunity side, if customer demand comes in stronger than planned, and we have either no recession or a mild economic downturn, then that would be an upside and accelerate cost optimization initiatives. We have some really, very active programs as we globalize our operating model, and I referenced global procurement. That is being aggressively stood up right now in our organization. We see a lot of opportunities there. If we can deliver on those sooner. That will be upside. And then better-than-planned plant-based protein sales commercialization there's a big lever there to be gained to drive accelerated sales development there. So Jim, do you want to add anything?

**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Yes. I would just say that we still see year-over-year corn cost inflation. While we kind of try and help you with an index of what maybe CBOT looks like, the cost of corn that we incurred in the year in 2022 is still going up in a number of our countries. And then also, we still see some of -- typically, you would call it fixed cost, but those fixed costs have things like wage increases, we're still reconciling some of our energy increases as we turn over our hedges. And so those are built into an expectation around our COGS increases. And of course, if we get kind of more volume than we expect, we'd probably get favorable cost absorption.

But right now, I think our guidance is kind of more conservative in how we look at volume and just anticipating that we're getting some COGS changes due to either the change in corn and/or some of the underlying rate increases we're seeing in some of our more manufacturing fixed costs.

**Benjamin Shelton Bienvenu** - *Stephens Inc., Research Division - MD & Analyst*

Okay. Great. My second question is related to the top line growth that you guys are discussing and in particular, what looks to be really strong pricing into 2023. My question is, it sounds like tighter industry capacities are driving stronger pricing, what do you think is the duration of that tight supply/demand backdrop for capacities across the industry? Is this something that is multiyear in nature? And I ask because it seems as though given all of the headwinds that you guys referenced for your business over the last several years, it very much feels like we might be on the path to kind of sustain earnings growth in this business as we come out of what has been a challenging last few years. And I'm curious to the level of visibility or confidence you guys feel to be relative to that characterization of the business.

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

Yes. What I would say is that one of the big determinants of industry tightness is obviously grind utilization. And what we've indicated is that the fundamentals and market conditions, primarily in the United States are very favorable. And that is because grind utilization remains at very elevated levels, perhaps at almost historical high levels. And remember, we operate in this industry with heavy fixed assets that prevent -- provide barriers to entry and long lead times if anyone was to expand capacity, which we don't see. And what we're also seeing is increased demand for renewable feedstocks. And so that's creating, again, more demand for grind and thus affording opportunities for companies like ourselves to look at existing capacity to trade up through the finishing channels and downstream processes for more value-added offerings across both core and specialty.

And I think you're seeing ingenuity at work and innovation at work across the industry as it relates to that with a finite amount of grind. And we're certainly doing that. We're certainly focused on driving the value creation from both core and specialties, and we're seeing opportunities to do so that we haven't seen these kind of conditions that allow us to get that kind of leverage from both aspects of our business. And I think others are equally adopting that approach. And it's one of the things that we feel very good about that our integration across both of those allow us to leverage the corn network and the procurement network for optimal efficiencies across both businesses.

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**Benjamin Shelton Bienvenu** - *Stephens Inc., Research Division - MD & Analyst*

Ok, great thanks. Best of luck.

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

Thank you.

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**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Thank you Ben.

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**Operator**

Our next question comes from the line of Adam Samuelson with Goldman Sachs.

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

Yes, thank you. Good Morning everyone.

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

Good Morning Adam.

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

I guess if I just think about the 2023 guidance and I think the comments you made on volumes were fairly kind of keeping expectations restrained. If I was to think about the profit growth, especially in North America, just help me if you can dissect our break up the kind of pieces between just price cost or net price cost mix and kind of faster specialties growth and maybe some of the lower losses from plant protein and other investments? Or and any other productivity or other factors we should be thinking about just trying to make sure you can waterfall kind of the drivers of growth and think about where it's all coming from?

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

Let me take a shot at just making a couple of points, and I'm going to turn it over to Jim. Obviously, our North America results, we're very pleased with. It was a highlight for the quarter. And the reason for that is, again, the performance of both our core business as well as specialties with specialties growing again, very strongly. And there is some excellent work being done on customer and product mix management, which allowed us to take the limited capacity and work to make sure that we are optimizing margins across both customers, and we've introduced something called profit velocity in relationship to our product line management initiatives as it relates to how do we make sure that we're optimizing our margins on a quantified -- on a limited asset base over a unit period of time. Given the constrained capacities that we're seeing in the industry.

So I think you're seeing a combination of very good pricing centers of excellence at work. I think you're seeing excellent work on customer and product mix management and also profit velocity and product margin work as well. So it's a real team sport team effort across operations and the go-to-market teams, and I think they're working better than ever. And I think that's why we're very pleased with the results in quarter 4. Jim, do you want to add anything?

**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Yes. Adam, I think in our full year guidance for North America, where operating income is up low double digits. Relative to pricing being up kind of up 15% to 20%. What's in that is very simply is that when we were entering 2022 and we had our contracts with customers, we were pretty expansive in hedge and corn. So our corn costs that we were past experiencing in 2022. We're probably a little bit less because we had hedged relative to where corn moved after the start of the Ukraine-Russia.

Now as we roll over those hedges, we're looking at the elevated cost of the corn strip and where co-products are. There's just corn inflation that's built in, and that's been reflected in our pricing conversations with customers. And so we're going to see some COGS increases in North America, and that's really kind of, I think, beneath what we're sensing in terms of op income up low double digits versus the price and the customer mix.

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

That's helpful. And I guess, it probably ties into that last point on the cash flow in the quarter, which came in I think, below where you had counted on a few months ago, and it seems like working capital was the big piece. Is it purely just higher corn and flowing through inventory, the hedging and then receivables because of the higher sales dollars and just the confidence that, that working capital headwind is not as significant and you got a better handle on it going into '23.

**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Yes. I mean really, I think is -- obviously, we'll see a step-up in our invoice pricing here on Jan 1. So there will be a little bit more investment as we get into Q1, Q2 into accounts receivable. But I think we're finishing on driving that and replenishing some of our safety stock inventory all throughout 2022. And as we go into 2023, better able to -- we're in a really nice position, I think, relative to some of the past supply chain disruptions that we've had, we're just in a good spot going forward. So I don't see as much investment change in the cost of the value of our inventory. So I feel like we're in a little bit more controllable spot with regard to working capital.

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

Super helpful. I'll pass it on. Thanks.

**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Thanks Adam.

**Operator**

Our next question comes from the line of Cody Ross with UBS.

**Cody T. Ross** - *UBS Investment Bank, Research Division - Analyst*

Good Morning, thank you for taking our questions.

**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Hi Cody, welcome.

**Cody T. Ross** - *UBS Investment Bank, Research Division - Analyst*

Thank you. You already discussed a little bit about your COGS inflation for the year, but I'm hoping to put a finer point out of it or on it. Can you discuss broadly your expectation for price gains coming out of the contract season and compare that to your cost outlook for the year? And then I have a follow-up.

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

Yes. As it relates to contracting and pricing. As we've guided for the year, we believe our net sales will be up mid-double digits again this year in comparison to last year with the majority of that increase coming from price mix, and that reflects the continued pass-through of inflation, again, as well as what I referenced earlier, the effective customer and product mix management. Jim, did you want to build on that?

**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Yes. Cody, I mean I think we've referenced in terms of the year-over-year change in COGS is somewhat driven by inflation, probably more maybe 2/3 or 3/4. It's just going to be lapping some of our corn costs or our tapioca costs as we go from 1 year to the next, where we effectively hedged in 2022 and now we have to kind of replace both our desire to purchase corn or other raw materials, and then we're placing hedges against that. You also have the rollover energy costs, right? Those are all kind of expected. I think that what I would also just highlight is that with strong price mix, our volume, while positive, is -- I think we're taking a balanced approach towards volume. And so we're probably not getting as much of absorption of fixed costs that we would kind of anticipate if we were in a less inflationary environment globally. And so that's also part of our COGS change.

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

The other thing that I would include would be and I probably should have mentioned this as perhaps an opportunity for 2023 is in quarter 4, we did have year-over-year improvements in gross margins. And one of the contributors to that was improving supply chain conditions, which we referenced. And so if that were to continue, and we are seeing some of those trends developing that's something that could be favorable for us as well. It certainly helped us to a degree in quarter 4, which allowed us to expand our year-over-year gross margins in the quarter.

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**Cody T. Ross** - *UBS Investment Bank, Research Division - Analyst*

That's helpful. Thank you. And then I just want to discuss South America a little bit because it came -- the top and bottom line came in weaker than we expected and below your full year guidance, what drove the shortfall? And then given other peers in the region noted slowing consumption trends, do you expect the segment to be softer going forward? Thank you.

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

Jim, do you want to?

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**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Well, Cody, I don't -- that question to look exactly. But what we were seeing, I think, in terms of finishing in South America, overall, just the second half of the year finished nicely in terms of sales volume and then also just continue to really price through all of the FX impacts on our raw materials. So very -- I think very overall pleased with how we're looking at the businesses in Brazil, Colombia and as well as Peru. We're very -- we have a very kind of a maturing pricing center of excellence there, obviously, given the inflation that is evident in both Brazil as well as some of the other South American countries. So you need to be very agile in terms of how you're looking at the next 2 to 3 months at corn and/or cost of energy and pricing that through. So I mean I think I look back in South America had a tremendous year in terms of operating income growth.

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

Another tremendous year on top of the 2 previous years of significant top and bottom line growth. And that's across the 3 regions, really Brazil continue to perform. The Indian region, Colombia had an exceptional year and also a very strong quarter. And even our Peru business had a very, very strong year. So we're very pleased actually with the performance in South America.

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**Cody T. Ross** - *UBS Investment Bank, Research Division - Analyst*

Great, thank you. I will pass it on.

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

Thank you.

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**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Thanks Cody.

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**Operator**

Our next question comes from the line of Robert Moskow with Crédit Suisse Securities.

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**Robert Bain Moskow** - *Crédit Suisse AG, Research Division - Research Analyst*

Hi, Jim. Hi Jim.

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

Hi Rob.

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**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Hey Rob.

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**Robert Bain Moskow** - *Crédit Suisse AG, Research Division - Research Analyst*

Hi. I was hoping to get a little more color on the phasing for your 2023 quarterly. Are there any comparisons that are easier than the others? Or anything where the pricing lags? And then secondly, can you give us some examples of like what customer product mix management means like what you're actually able to do with your customers to, I guess, to trade them to higher margin products within your portfolio? Or what else could it involve. Thank you.

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

Sure. I'll take the second question. Jim will take the first one on phasing. Jim?

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**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Yes. Given the OI growth that we experienced both in Q1 and Q2 of last year, I'm expecting kind of low to mid-single-digit OI growth in the first half of the year and then stronger growth in the second half. I think we really expect high single to low double-digit OI growth just for the full year, barring kind of any significant changes in the layout of our raw material costs, primarily outside of the U.S.

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

And as it relates to customer and product mix management, specifically the conditions, as I referenced in the market over these last 2 years has allowed us to work with those customers that we believe are going to be the best strategic partners for us longer term. And we were forced and had to be more discerning in relationship to the products that we would be supplying to different customers that represented longer-term strategic growth opportunities. So through some really good work with customer profitability analysis, customer growth forecasts for the categories in which we are in and doing some really very good analysis and decision-making and intelligent decision-making. I think we have improved the profitability of our customer mix and done it in a way that we think aligns for better long-term strategic growth. The same in relationship to product mix management with product line managers that we invested in, in the business about 3 years ago, timed with our pricing centers of excellence.

We complemented those teams with product line managers that are looking at profitability and again, introducing the concept of profit volatility, which is how much profit you can make on an asset in a given period of time you said volatile velocity...

**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

You said velocity...

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

Sorry, profit velocity. Thank you, Jim, for correcting. But looking at that, so we can maximize the amount of profit on a particular unit operation in a given period of time. Hopefully, Rob, that gives you a little bit of color on how that's helped further improve our performance.

**Robert Bain Moskow** - *Crédit Suisse AG, Research Division - Research Analyst*

Yes. And maybe a follow-up. Are you also walking away from certain customers as a result that were not profitable? And then maybe also, are your fill rates where you want them to be right now in terms of being able to supply demand?

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

Yes. As it relates to having to be very critical in relationship to where we sold our products, for sure, we had to make some tough decisions over the last, say, 18 months. From a standpoint of how our operations are running and our fill rates, we're very pleased with that. And we do see upside there as our teams continue to -- we've identified constrained assets. We have programs in place to release capacity on each and every one of them. We've quantified the value at stake, and the teams have all of that as a go-get for this year. So again really good collaboration between our operations and our go-to-market teams in that regard across both core and specialty ingredients. So we're happy with the fill rates, but we see opportunities going forward.

**Robert Bain Moskow** - *Crédit Suisse AG, Research Division - Research Analyst*

Got it. Thank you

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

Thank you Rob.

**Operator**

(Operator Instructions) Our next question comes from Ben Theurer with Barclays.

**Benjamin M. Theurer** - *Barclays Bank PLC, Research Division - Head of the Mexico Equity Research & Director*

Good Morning Jim and Jim.

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

Hi Ben.

**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Good Morning Ben.

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**Benjamin M. Theurer** - *Barclays Bank PLC, Research Division - Head of the Mexico Equity Research & Director*

Just 2 quick ones. So one, and you've talked about it a little bit on the plant-based protein side, and there was a little softer than what you hoped for, for this year. But if we look into 2023, how should we think about the ultimate headwind also like framing it in between the relatively wide range for the segment of 50 million to 70 million, which both would be good growth rates, but what would you need to get this to, call it, operating profit breakeven versus it was still a loss in 2022?

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

Yes. I'll make some comments just on the overall segment of plant-based proteins. And then I'll turn it over to Jim to take the last aspect of your question on getting to breakeven. So the way we're looking right now at the plant-based business, as with any fast growing and rapidly evolving category, consumer taste and preferences change. And as a result, we're seeing customer product quality requirements becoming more particular for different applications. Now that represents an opportunity for companies that can deliver against those quality attributes.

And we're also seeing, and it's not a surprise that customers are being more prudent regarding new product launches in this current environment. We continue, though, to have a robust customer project pipeline and have sharpened our focus to target particular segments for growth. And we believe this focus is going to allow us to increase our sales growth, which will be the lever that we need to drive the fixed cost absorption and the incremental profitability.

The plants are running well, and we have partnership, customer relationships to, again, deliver against their specifications as they introduce new products to consumers that are very particular in regards to what they're looking for in these different categories, whether it be alternative meat, alternative dairy, beverages, sports nutrition, et cetera. Jim, as far as the specific question on the threshold or leverage on the sales side. Do you want to take that?

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**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Yes. So Ben, I think within 2022, while we had a pretty significant operating loss, we improved upon that versus 2021. I think our expectation as we go into 2023 is to, again, just a modest improvement in that operating loss. And what we're really -- and that's sort of included in our guidance. What we're really looking for is as we go from that mid-30 million-ish sales and get into that more doubling range, we really start to then pivot in terms of our volume throughput on our 2 facilities.

And that really then starts to -- the sales beyond that really start to really help us close down. We get enough contribution margin to cover our fixed costs. And so I think right now, we would be looking at taking all of '23, let's get the momentum behind the top line sales and all the success, I think we're seeing in the sampling and the product quality improvement and build that momentum into 2024 sales and then maybe more towards the end of '24, we'll be getting to somewhere where at least kind of cash breakeven.

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**Benjamin M. Theurer** - *Barclays Bank PLC, Research Division - Head of the Mexico Equity Research & Director*

Okay. Perfect. And then capital allocation. I mean, obviously, you done a minor increase of your stake in PureCircle, and that obviously has been one of the very success story on growth. Would you consider buying the rest of it on because it seems like there's not much left over? Or how should we think about just like the focus between the balanced capital allocation, maybe adding something you already own now 87%, just to understand a little bit the M&A opportunities you might see out there?

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**James Derek Gray** - *Ingredion Incorporated - Executive VP & CFO*

Yes. So within our agreement with the remaining shareholders, we have the rights to purchase the remaining 13% of PureCircle over the next 3 years. So we'll complete that and have 100% ownership of PureCircle by more towards 2025. It may happen sooner, but that's within our agreements.

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**Benjamin M. Theurer** - *Barclays Bank PLC, Research Division - Head of the Mexico Equity Research & Director*

Perfect.

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

And as well -- and just in relationship to overall M&A, we continue to have a very active M&A pipeline, nurturing long-term relationships and that's part of our capital allocation strategy for sure.

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**Benjamin M. Theurer** - *Barclays Bank PLC, Research Division - Head of the Mexico Equity Research & Director*

Perfect. Thank you very much.

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**Operator**

And I'm currently showing no further questions at this time. I'd like to hand the call back over to Jim Zallie for closing remarks.

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

All right. Thank you. And I'd like to thank everyone for joining us this morning. We look forward to seeing many of you at our upcoming investor events, and I want to thank everyone for your continued interest in Ingredion.

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**Operator**

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

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