Event:

CAGNY 2021 Ingredion Q&A Session (Feb 16, 2021)

Speakers:

James P. Zallie, President and CEO

Jim Gray, Executive Vice President & Chief Financial Officer

Moderator:

Tiffany Willis, Vice President of Investor Relations and Corporate Communications Officer

Q&A Session:

Tiffany Willis: Good afternoon, and welcome to Ingredion's break out session. I am Tiffany Willis, Vice President of Investor Relations and Corporate Communication Officer. I will serve as your moderator, for today's session with me, are Jim Zallie our President and CEO and Jim Gray our Executive Vice President and Chief Financial Officer. Now, we will go right into questions.

Our first question, how will your joint venture in Argentina impact your business in South America?

Jim Zallie: Well thanks, for that question let me take it first. So, we are very proud of the joint venture that we just announced on Friday with Grupo Arco in Argentina. Grupo Arco is a very respected company in Argentina, with brands that they sell around the world in more than 100 countries and they have a high-quality food ingredients business. The joint venture that we formed covers Argentina, Uruguay, and Chile and it combines three of their manufacturing facilities, with two of our manufacturing facilities.

The total revenue of the joint venture is going to be approximately $300 million dollars and will really provide an opportunity, for the two companies to leverage their manufacturing footprint across Argentina and for the Southern Cone. And then also, work together to bring a variety of both core and specialty food ingredients to the Southern Cone market, and bring innovation to customers from a stand point of how the joint venture is accounted for, from an accounting stand point, I'm going to turn that over to Jim Gray to handle. Jim.

Jim Gray: Thanks. As we disclosed in our 8-K, we will be having an impairment relative to our books mostly due to our accumulative translation adjustment, approximately $310 million dollars. We will also be impairing some of the existing assets, our property, plant and equipment, as well as contributing working capital to the joint venture. The joint venture itself will be on a stand-alone basis. We will account for it on an equity basis. And, I think to note, which is important is that our hyperinflation treatment for accounting in Argentina; which had traditionally shown up in our financing cost, that will now be against the equity income that comes from the JV. With that, I'll will turn it back to Tiffany.

Jim Zallie: Our core will hold a 51% state in the joint venture and Ingredion will hold 49% state in the joint venture.

Tiffany Willis: Perfect, our next question. How is Ingredion positioning itself with large markets, such as India and China? Can you provide some more color on this?

Jim Zallie: Yes, so from a standpoint of China. China is the largest specialty food starch market in the world. And, Ingredion has been operating in China for more than 30 years and we have been manufacturing in China for approximately 20 years and recently, we are investing more than $85 million dollars to expand our modified starch capacity to meet market growth demands. We weathered 2020 extremely well, when you consider the impact of the pandemic in quarter one and we delivered a very strong performance in China last year. So, we are very excited about the prospects of these investments that we are making to meet the market growth demands going forward and those investments will be commissioning in the first half of 2022. So, Jim any other comments you would like to make about China?

Jim Gray: Not about China. I think overall, ASEANI has also been a focus for us. We include India within our ASEANI region and generally see our ability to bring our starches and some of our other ingredients into India, as it's definitely a growth opportunity for us.

Jim Zallie: Yes, in India we have a small presence today, but a very good import model into India and continue to assess opportunities to enter that market more fully over time.

Tiffany: Perfect, our next question is going to come from Rob Moskow on specialties. It is a multi-layered question. What organic growth rate do you expect from specialty sales over the next five years to hit your 2025 target? Do you need acquisitions to achieve this 50% plus goal? Also, do you expect sale declines in corn-based, starch-based commodities?

Jim Zallie: Yes, I don't think we expect to see declines in necessarily the specialties corn-based products that we have. You're referring, Rob, to the big goal, that I have put out for the organization, which is to get our specialties to greater than 50% and that will come we believe through a combination of both organic and inorganic moves that we will make between now and 2024-2025. The growth rates by growth platform we did layout in the presentation and we expect to see mid-single digits for starch-based texturizers, clean and simple in the high-single digits, step changed growth with plant-based proteins and double digits, mid-double digits type of increases of 15% or so for food systems as well as sugar reduction. And then we intend to complete bolt-on acquisitions that add to the value proposition of each and every one of those specialty investments over time.

Jim Gray: Maybe, I'll just add that Rob I realized you asked a question from the prospective of 2025. What we lay out in our four-year goal is still an expectation for our specialty net sales to grow mid-to-high single digits.

Jim Zallie: Yes, and what I would say is what we are very consciously targeting to do is to diversify our portfolio beyond corn with specialty rice, specialty tapioca, and specialty potato to give ourselves, again, more formulated capabilities to problem solve and deliver more complete ingredient solutions to customers for texturing and that would be furthered complemented by the portfolio of plant-based protein that we offer. We think that approach is going to serve us very well when you think about a gluten-free application beyond corn for example, other snacks like cereals and a variety of other products.

Tiffany Willis: Continuing with the topic is specialties. The next question comes from Ken Zaslow. What percentage of the specialty business is protected by intellectual property? It looks like you are expecting specialty margins to be 18-20% by 2024. What gives you confidence to be able to expand these margins?

Jim Zallie: From an intellectual property standpoint, we have intellectual property that protects, I would say Jim, 20% or less of the specialty portfolio would you say or 25% of the specialty portfolio?

Jim Gray: Specifically, patented? Yes.

Jim Zallie: Yes, probably in that range and we believe because of the vertical integration, because of the investments that we have made, controlling the supply chain specifically around stevia or plant-based proteins and certainly, when it comes to starch-based texturizers. It affords us the best opportunity to maximize the margin and then also the food systems aspect of things. Where customers both big and small were seeing are interested in more complete food systems and solutions. So our approach again, is to have a complimentary suite of specialty ingredients that we can formulate with, and deliver those both as ingredients, where requested, or as food systems to allows us to maximize the margin capture for the offerings we will be making. So, we are confident that we can achieve the kind of margins that we have indicated tied to the specialty growth we are projecting, tied over the next five years.

Tiffany Willis: Perfect, continuing with intellectual property. The next question comes from Adam Samuelson. Can you also discuss your IP and patent portfolio across your specialty portfolio, which you just spoke about, Jim? But, where do you see the durable source of margin and competitive advantage across the key product categories?

Jim Zallie: I see the competitive advantage coming from the intimacy that we will have with customers aligned with being both broad and deep, along every one of those growth platforms. Again, I think our reputation is unparallel when it comes to starch-based texturizers. The franchise that we built in clean and simple and the player that we expect to be in a few short years, in plant-based proteins. Certainly, acquiring PureCircle has propelled us to a leadership position with the leader in stevia, which has a very formidable IP estate that we have acquired and has given us very good technology as well. So, I think by the breadth and depth of the offerings that we can provide for each one of those growth platforms, and again combining the four to produce the fifth, which is the food systems provides us an opportunity for incremental intellectual property, but at the same time we want to be quick and nibble and agile and delivering and co-creating with our customers to deliver consumer preferred innovation. So, it's going to be about speed, its going to be about co-creation and at the same time developing the technologies that under pin each one of those growth platforms.

Tiffany Willis: Our next question is on M&A activity. Could you give an update on synergies from the recent M&A activity and has COVID accelerated or impacted negatively your initial plans?

Jim Zallie: So, let me take it first from a standpoint of PureCircle and then let Jim make some comments. PureCircle, we acquired I think it was in July of last year, we formally closed on the acquisition. We really were undeterred in relationship to the pandemic, on our ability to get after the cost synergies, the SG&A savings and we delivered and I think we stated in the earnings call approximately $14 million dollars of cost savings synergies there. We are working supply chain synergies right now, very hard and I don't think we are deterred there. The Verdient acquisition is being integrated as well.

One of the benefits, that Ingredion has when we make an acquisition like that in Saskatchewan, even though the border between the U.S. and Canada is closed. So, for someone like myself I can't travel to Canada necessarily without quarantining, but we have a whole team of engineers and manufacturing folks in Canada. In Canada, in our plants, both in Cardinal, Ontario as well as the London, Ontario plant and those engineers have been in Vanscoy and have been helping and assisting and leading that integration so we do not think that project will be delayed. We are projecting for that project to be completed in the first half of this year. Anything I am missing Jim, on M&A and integration?

Jim Gray: No, I would just add that we defiantly leveraged the fact that both virtual meetings with Teams, so you can get your experts where ever they may be in the world to be addressing the problem that you are facing within the integration. But, as Jim alluded to in our Canada example, but also in either Malaysia or China with regard to PureCircle we have local teams that have been able to get into the key facilities and help with whatever challenges we have been presented and keep everything on track and on time with regard to our integration plans.

Tiffany Willis: And the next question will talk about M&A further, but it's also going to talk about capital allocation. It is coming from Adam Samuelson. How do share repurchases fit into your short and medium-term capital allocation plans? Also, can you discuss the willingness to do a larger acquisition to more materially shift the portfolio away from legacy corn starches and sweeteners?

Jim Zallie: So, let me just make a headline comment on capital allocation, and then I am going to turn it over to Jim, and Jim can turn it back to me from a standpoint of bigger transformation acquisition. So, Adam thank you for the question. Over the last four years, Ingredion has deployed approximately $3 billion dollars in cash, spilt between buy backs as well as acquisitions, growth capital, and dividends. Jim, I am going to turn it over to you to give a break down on that, because I think it is informative, and then you can turn it back to me for the M&A question.

Jim Gray: Sure, Adam we talk about cash from operations; which is obviously is driven by both your income, your rate of your debt as well as your change in your working capital. But, when we look at our cash from operations, we really have two first priorities in our capital allocations. So one is our capital investments both in maintaining our assets but also in growth capital. So under Jim's leadership, over the last three years, we have stepped up our capital investment into growth. That is because those organic opportunities, really appear to us to provide very attractive returns. They're very closed in investments to our current strategy, and our teams really know how to execute and put that capital to work. So, we can generate future revenue and future cash flow.

We have also deployed capital towards our dividend, about $660 million dollars over the last four years. It's about 22% of our total cash from operations and then what is left is what we called strategic cash for deployment and so that can either go towards acquisitions and/or share repurchases. We have deployed about $1.1 billion dollars over the last four years towards share repurchases and/or acquisitions and we'll continue to look at and have flexibility with both our existing cash on hand at the end of year. As well, as the anticipated cash from operations, as we move through 2021. In considering both, so we will look at what we think in terms of M&A and I will hand it back to Jim. But, also very much consider potential share repurchases or change in the dividend.

Jim Zallie: Yes, from a standpoint of M&A, Adam, we as you know have a strong balance sheet and we were very pleased this past year with specialty's growth in all four regions. That is, in spite of absorbing the full impact of the pandemic. So, what that did and what we said on the last earnings call was that helped validate -- that execution helped validate our conviction in the strategy and that is of those four or of those five growth platforms. And, so again any M&A that we can do, which would probably be more targeting of more bolt-on M&A to support the value propositions and strengthen those we would do.

At the same time, you know we always as a company conferring with our Board about what else we might be able to do to change the trajectory of the company and look at opportunities that not necessarily would be considered a bolt-on, but could be considered transformational, but it will always be enhancing the five growth platforms and be it will be something that is completely aligned to what we consider to be the trends, that are shaping the food industry. Whether it be clean label; whether it be in plant-based proteins; whether it be in sugar reductions, that's the area we would be looking to enhance with any M&A moves we would make.

Tiffany Willis: Perfect, we are going to shift gears back to specialty and margin. The question comes from Ken Zaslow. He would like to revisit specialty margins and ask in a different way. Are you currently generating those level margins in specialty excluding start-up costs? And if not, how are you deriving the incremental profit margin in specialty?

Jim Zallie: Jim, do you want to take that?

Jim Gray: Yes, I think I understand Ken where your question is coming from. So, today when we breakout our share with the adjusted operating income profit growth looks like both in 2020 as well as our goal for 2024. You can work backwards, into the applied operating margins from our specialty business and they are in that range. We do see that currently it is absorbing some of the operating costs for the start-up of the plant-based protein facilities that we have progressing in 2021. As, we get into 2022 and through 2024, we do see those margins just because of both the absolute price of the products that we sell, as well as the underlining gross margins. We see an opportunity for that margin contribution from our specialty to expand our margins as a total company over our four-year goal.

Tiffany Willis: Now sticking with specialties we have another question from Adam Samuelson. Specialties have grown to be about 32% of revenue in 2020 from 26% in 2016. Over that same time period, gross margins have not increased at the same rate. Why wouldn't specialty growth be more visible in long-term margin trends?

Jim Zallie: I think what has happen over the last few years for the total company is related to the decline in our core sweetener products, primarily, in North America and that is just related to some of the capacity in balances that we have seen and the accelerated trends pressuring full caloric beverages for example. So, I think over time and where the actions we have taken, so if we just take a couple of actions we will continue to progress to address the challenges in the core and if I move to the Southern Cone for a moment we just made a very significant move to strengthen and reduce earnings volatility long term in Argentina, for example and that’s a country where the last few years has obviously hampered overall Ingredion margins, so that is a very decisive move.

We are now completely out of ethanol, so we have removed ethanol from our portfolio completely with a move that we announced with the closure of our ethanol assets in Cedar Rapids and so we are less dependent by moves that we have made. The closure of the Stockton Plant for example in 2019, so HFCS as well as industrial starch out of our portfolio. So, we, as an industry supplier, are less exposed relatively speaking to that core business as our specialty’s business continues to grow and I believe that our margins for specialties, which are well in excess of some of those core products, will be evident going forward in comparison to what has transpired in the past, combined with the actions that we have taken to strengthen and reduce the earnings volatility from the core products over time. At the same time, that core business will generate cash that we intend to deploy for future M&A for specialties.

Tiffany Willis: Shifting to plant-based proteins. Where do you see the growth of plant-based in your portfolio? Can you talk to me about keeping up with the demand?

Jim Zallie: So, right now we are very focused on both of our manufacturing facilities. The South Sioux City facility and the Vanscoy, Saskatchewan facility to get those fully functional and in a position to supply customers needs in the second half of this year. So, we are very proud of the fact that we have food grade certification for both pea protein isolate and pea starch in January of this year. We are well on our way in Vanscoy, Saskatchewan for the pulse flour and the concentrates. So, we have a very active and full customer pipeline that we are looking to progress and again, getting the certifications, qualifications – there's a tremendous amount of customer interest from a standpoint of applications. It's certainly a meat alternative. We have a very strong focus on dairy alternatives because for Ingredion, our starch-based texturizers are found widely in a variety of dairy applications. So, that would be another targeted application. Pet nutrition is another one, with some of our plant-based protein products, as well as snacks and as I mentioned before cereals.

Tiffany Willis: Great, we highlight rice in our presentation, so can you provide some more explanation about opportunities that Ingredion has for rice?

Jim Zallie: Well, thank you for asking that question. We made a strategic acquisition of a company called Sunflower in Thailand a few years ago. We then subsequently invested to upgrade that facility, and also more than triple I believe, the capacity for specialty rice, starches and flours from that facility and the reason we did that is because we have a very complicated supply chain where we were importing rice starches from that region but modifying them elsewhere and to basically bring about a step change in our cost structure, we decided to leverage our assets in Asia and vertically integrate the operations all within Thailand and we have seen very strong growth for rice-based starches, that are very high value and they are premium priced are they are sold because of the fact that they are gluten-free. They are hypoallergenic or associated with hypoallergenic. They are rapidly digestible, so for infant and baby foods, they are attractive. They also give a very clean melt away in the mouth from a texturizing and mouth feel standpoint. So, they have very interesting properties, which plays to our heritage of being a leader in understanding texture, but also opens-up some new categories for us around the world really and one of the biggest growth opportunities for us is in North America, for example, while we have enhanced the supply chain significantly now consolidating in Thailand.

Tiffany Willis: Going back to South America. What are the biggest risk factors to a recovery in margin in South America, if we think over the next 12- 18 months?

Jim Zallie: So, first of all in South America I just did not want to underscore the fact that last year was a good year for us in South America, despite that region weathering some really tough, tough challenges from the stand point of what the pandemic brought upon them. Everyone's read about Brazil, Ecuador, Colombia and Peru and the severity of the lock downs, but our team down there had been working over many years to strengthen our core business as well as drive specialties growth. They did both of those extremely well and we also did a very good job on cost management over the last few years, and again last year and executed upon an organizational transformation that delivered about $7 million dollars in savings last year, so the team has really been focused on operational excellence and focused on the customer and in quarter four last year we failed to mention this, but in the earnings call that was the best quarter in South America since 2012.

The team enters this year with momentum having already enhanced margins in the core business and I believe while specialties are only 19% today. There is an opportunity to increase that percentage and we have again a very strong reputation with the leading customers, certainly in brewing, as well as all of the major food companies throughout South America and I'm confident in our South America team that they will continue to build on the success of last year.

Jim Gray: I would add too. Given the previous long recession in Brazil and some of the slower growth that was occurring in the region, just in the last two years, we started to see a trend toward small growth but nonetheless growth. I think that was paused by the pandemic. We expect to see a-lot of the stimulus that is down there continue to spur economic growth. That allows our plants that have some head room for capacity to operate at that next ton at that next incremental contribution margin and so that will still allow us as we expand to our full capacity as demand takes up, we should be able to see expanding margins in South America.

Tiffany Willis: We have spoken a little about intellectual property and patents and someone would like to revisit that. In speaking about that, can you help me understand the relationship between an increase in patents to the increase in the business in Ingredion?

Jim Zallie: Well, I think that intellectual property is very important when you are dealing with products that are derived from new technologies and so for us, we have a focus on innovation. It is part of our heritage. One of our values is to innovate boldly and supporting all of our growth platforms, we have also technology platforms that we have identified and those are proprietary so I do not intend to divulge exactly what our technology platforms are, but those guide our innovations team to again be generating innovative ideas, in which they can protect by intellectual property and in some cases we will do that through trade secrets, if it made sense. It is important for us as we continue to innovate to support the growth in those platforms. We have done that over the years to protect our interest, while we commercialize those products and drive sales and profits.

Jim Gray: I would add that our patent portfolio is not just on some of the applications or particular molecule that Jim has highlighted. There is also patents around our process and to the extent that we can improve our process or improve our manufacturing cycle that actually both might help us with capacity coming out of the existing assets, but it also may reduce our capital in the future, as we are looking at our standing business capital or as we look at growth capital to the extent that we have a conversion process that actually requires less capital overall it's going to drive a lower cost position in the ingredients that we make for our customers.

Tiffany Willis: Before we wrap up with about 2 minutes. I would like to offer both Zallie and Gray do you have any closing remarks that you would like to offer to the audience?

Jim Zallie: Jim, do you want to go first?

Jim Gray: I would just emphasis that…Thank you again CAGNY for inviting us. As we have the chance to talk about the growth of our company in terms of our specialty portfolios and our specialty emphasis. I think from us you will hear more of a focus on our cash from operations, our capital allocations, and how we really have a business that does generate cash, which we feel that we can really put to use in creating stockholder value.

Jim Zallie: And, I would just compliment what Jim is saying more from the standpoint of the cash and the operation the mechanics of being a very financially healthy company that we are very proud of. To say, that hopefully what came through in today's presentation is the fact that Ingredion is genuinely a purpose driven organization, with great values that guide us and is helping to guide all of our employees to do the right thing at all times and to live our purpose to make life better for all stakeholders.

Tiffany Willis: Thank you Zallie and thank you Gray and thank you everyone for joining us virtually. With that, I will conclude this session.