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INGR.N - Q3 2022 Ingredion Inc Earnings Call

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OVERVIEW:

INGR reported YTD net sales of almost $6b, reported operating income of $605m and reported EPS of $5.63. 3Q22 net sales were $2.023b, reported operating income was $182m and reported EPS was $1.59. Expects 2022 net sales to be up mid double digits and adjusted EPS to be $7.00-7.45.

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PRESENTATION

Operator

Good day, and thank you for standing by. Welcome to the Third Quarter 2022 Ingredion Incorporated 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 and Corporate Communications. Please go ahead.

Noah Weiss

Good morning, and welcome to Ingredion's Third Quarter 2022 Earnings Call. I'm Noah Weiss, Vice President of Investor Relations. I'm delighted to have joined Ingredion at such an exciting time for the company, and I'm glad to be part of such a terrific organization. It is great to connect with you all virtually this morning. And for those I haven't met yet, I look forward to meeting you soon.

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 will reference for our third quarter results can be found on our website, ingredion.com, in the Investors section.

As a reminder, our comments within the 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 those 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 can 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 will also reference 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 appendix.

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

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

Thank you, Noah, and good morning, everyone. We had another strong quarter, and I'm pleased to discuss our continued progress and the momentum we are building in the business. For the third quarter, we delivered excellent top line performance, achieving 15% net sales growth, up 19% on a constant currency basis. Our team has continued to do an outstanding job managing inflation by offsetting higher corn and other input costs as well as foreign exchange impacts.

Our third quarter results validated these efforts. We expanded our gross margins and grew adjusted operating income by 17% year-over-year, which was up 23% on a constant currency basis. Looking at our net sales performance in a little more detail. Across all 4 regions, comparable net sales demonstrated considerable strength in the third quarter. Notably, a few of our businesses achieved record all-time sales levels, including Brazil and China, to name 2 of our most important markets.

Our commercial teams addressed head-on persistent global challenges such as input cost inflation, foreign exchange weakness and continued supply chain pressures. Our operations and supply chain teams remained intensely focused on getting our ingredients to our customers when and where they need them.

Now turning to our strategic pillars. Our 4 strategic pillars continue to guide our execution and drive our business momentum, and I am once again proud of what our team accomplished during the quarter.

Starting with Specialties. This business grew mid-double digits in the first 9 months and continue to demonstrate strong top line growth in the quarter. All 5 growth platforms performed well with texturizing ingredients and sugar reduction as standouts. Additionally, plant-based protein sales were up strongly in the quarter and are now more than 145% greater year-to-date. Excitingly, we also commissioned our Shandong, China production facility in July and are ramping up both production and sales. This plant has come online at a perfect time as it enables us to leverage and flex our new network capacity to support our European customers who are concerned about anticipated industry shortages for some starch products due to the severe summer drought.

Moving to commercial excellence. Our teams remain nimble in adapting to a fluid business environment. Our pricing centers of excellence have been instrumental in managing in-year inflationary pressures to deliver almost $950 million in price mix increases year-to-date. Additionally, we expanded our online customer portal to provide better tools and deeper engagement with our customers, enabling them, for example, to readily access real-time order and shipping details.

Regarding our third strategic pillar, cost competitiveness through operational excellence. As I mentioned last quarter, we have implemented expanded hedging strategies to reduce the in-year volatility of corn costs. Since February, and the start of the Ukraine conflict, we have witnessed a global increase in the cost of corn and other agricultural commodities. We believe our hedging strategies have flattened our exposure to raw material cost fluctuations, both in Q3 and for the remainder of the year.

In our global operations, we have deployed a digital capability to model supply chain flows that minimize costs and maximize returns under different considerations such as excess demand and capacity or service constraints. This allows us to optimize our cost to serve while meeting demand and managing supply constraints.

Additionally, we are mitigating regional disruptions of grain supplies due to weather-related events and the Ukraine conflict by leveraging our global procurement and supply chain network to address gaps quickly as they arise. This is a significant achievement on the part of our global ag supply business continuity team, and I'd like to recognize their extraordinary efforts during these times.

Lastly, as it relates to our purpose-driven and people-centric growth culture. Among the highlights during the quarter, our ultra-performance line of plant-based protein concentrates was selected Best Plant-Based Sustainability winner for product innovation at the World Plant-Based expo.

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This is a tremendous testament to our team's ability to innovate and meet consumers' changing needs for nutrition and sustainability in this product category.

Now I'd like to speak to a few examples of how we're creating future growth momentum in specialty texturizers and sugar reduction as well as creating value from our sustainability partnership efforts with customers. First, I want to emphasize the notable achievement of our China team to commission our new specialty modified facility in Shandong, China on time, overcoming numerous challenges such as COVID lockdowns and equipment delays. In July, we commenced production at our new facility which significantly expands our capacity and capabilities for specialty modified starches. We are now the largest producer of modified starches in China which positions us well to meet the growing customer demand for these highly functional texturizing solutions.

And as a reminder, as we noted at our Investor Day, modified starch consumption per capita in China is significantly less than the U.S. or Europe. Thus, with a consumer market of 1.5 billion people, this is an exciting long-term growth opportunity for our company.

Turning now to sugar reduction. We delivered strong double-digit growth in the quarter led by PureCircle. Customer wins, effective pricing strategies and innovative solutions produced 19% net sales growth and positive operating income. And we are continuing to see strong growth for our sugar reduction franchise worldwide. Supporting future momentum, we recently received EU approval for our bioconverted Reb M further positioning us to grow in Europe, which currently accounts for approximately 25% of PureCircle's net sales. This approval adds to our excitement about our growth prospects for high-intensity natural sweeteners in Europe.

Consistent with our strategic intent and our agreement when we acquired PureCircle, we are pleased to share that we have further increased our ownership of PureCircle to 85% from our original 75% ownership stake. And we anticipate additional increases to our ownership over the next 3 years.

Turning now to our sustainability progress. In the third quarter, we achieved 42% sustainably sourced agricultural inputs, up from 33% at the beginning of the year. Our goal, as you may recall, is to achieve 100% sustainable sourcing for our 5 priority crops by 2025. In addition, as part of our sustainability efforts, Ingredion is pleased to be the first major food ingredients company to engage with HowGood, the world's largest data platform for sustainable food, beverage and personal care offerings. Our relationship will deliver increased transparency through scorecards for our ingredients. Ultimately, this will help our customers by giving them the critical data they need to select ingredients that meet sustainability targets for the products they are developing. We anticipate that transparency around our ingredients will better enable our customers to innovate for the growing demand for more sustainable products.

Let me now comment on the macro environment and highlight some of the risks and opportunities we see on the horizon. As you've heard today, our teams have done a great job of offsetting inflationary and foreign exchange headwinds while overcoming supply chain challenges to deliver growth. We expect these pressures to continue, but we believe we are well positioned to manage them.

First, while COVID-related lockdowns and restrictions in China were less of an issue in quarter 3, intermittent supply chain challenges remain. Rail, labor issues, along with sporadic reductions to our preferred shipping modes, have, at times, required us to spend elevated amounts to deliver products to customers on time. Our supply chain and commercial teams continue to navigate this dynamic environment.

Second, regarding inflation. We remain committed to offsetting additional costs through a combination of pricing and productivity improvements from operations. We have demonstrated a track record of effectively managing price risk, and this remains a priority.

Third, foreign exchange continues to be an increasingly important factor for global companies as the dollar strengthens. Our business model has historically allowed us to offset currency impacts quite well over a 3- to 6-month period, and we're confident in our ability to continue to do so.

Lastly, we are watching very closely consumers' buying behavior and price elasticity. It's important to remember that we serve customers across both branded and private label as well as across retail and food service. That diversity mitigates volume risk by enabling us to benefit when one sector strengthens while another contracts.

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With that, let me hand it over to Jim for the financial overview. Jim?

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

Thank you, Jim, and good morning to everyone. Starting first with our Q3 regional performance. North America net sales were up 17% when compared to the same period in 2021. The increase was driven by strong price mix, which was achieved in 2 parts. First, during contracting last fall, which anticipated inflation; and second, due to dynamic in-year price adjustments for freight costs and spot pricing for volumes beyond contract commitments.

North America operating income was $126 million, up $6 million versus the prior year. The increase in operating income was driven by strong price mix that more than offset change in input costs. In South America, reported net sales were up 13% versus prior year, which includes the impact of the Argentina JV presentation change.

On a comparable basis, net sales in the quarter would have been up 21% excluding the contribution of Argentina to the JV in the prior year.

South America operating income was $48 million, up $13 million with favorability being driven by stronger performance in Andean and Brazil as well as positive contribution from the Argentina JV. Excluding foreign exchange impacts, adjusted operating income was up 43% in the quarter.

Moving to Asia Pacific. Net sales were up 13% in the quarter. Absent foreign exchange, sales were up 23%. Asia Pacific operating income was $27 million, up $6 million versus prior year, with favorable price mix that more than offset higher input costs and foreign exchange impacts. Excluding foreign exchange impacts, adjusted operating income was up 43% in the quarter.

In EMEA, net sales increased 9% for the quarter. And absent foreign exchange impacts, net sales were up 27%. EMEA operating income was $30 million for the quarter, up $7 million compared to prior year due to resilient performance in Europe, which was partially offset by higher corn costs and supply chain challenges in Pakistan as well as foreign exchange headwinds. Excluding foreign exchange impacts, adjusted operating income was up 52% in the quarter.

Moving to our net income statement. Net sales of $2.023 billion were up 15% for the quarter versus prior year. Gross profit dollars and margins were higher year-over-year, up 20 basis points from Q3 last year. Reported operating income was $182 million, and adjusted operating income was $191 million. Reported operating income was lower than adjusted operating income primarily for costs pertaining to the work stoppage at our Cedar Rapids facility. Importantly, the plant is now operating well under our business continuity plan and is steadily increasing production to meet customers' needs.

Our third quarter reported and adjusted earnings per share were $1.59 and $1.73, respectively, for the period.

I'd like to spend a moment highlighting gross profit performance as I think there are some aspects to this part of our story that can be easily missed. As I have mentioned previously, our business model, when measured by gross margin percentage, is impacted by rising and falling corn prices. In rising corn price cycles, historically, our pricing has lagged the change in the cost of corn, and consequently, our gross margin percentage has been impacted.

What was [happening] in this quarter. We have been working pricing and our hedging strategies to flatten the impacts of changing corn values on the quarterly layout of our costs. Here, you can see that we have expanded gross profit margins even though the corn costs increased year-over-year by 16% as measured by the change in the U.S. benchmark.

Turning to our Q3 net sales bridge. We achieved strong price mix of $335 million, including the pass-through of higher corn and input costs. The sales volume increase of $14 million was driven by volume increases in each of the regions and offset by $18 million decrease due to the presentation change related to the Argentina joint venture.

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On Slide 18, we highlight net sales drivers. Of note, foreign exchange was a 4% headwind in the quarter with significant headwinds in EMEA and Asia Pacific. Reported South America results include the impact of the presentation change of the Argentina JV within the volume column. South America net sales grew 21% on a comparable basis, excluding the impact of the Argentina JV noted below.

Turning to our earnings bridge. On the left side, you can see the reconciliation from reported to adjusted earnings per share. On the right side, operationally, we saw an increase of $0.33 per share for the quarter. The increase was driven primarily by operating margin increase of $0.47, partially offset by unfavorable foreign exchange of $0.12 per share.

Moving to our nonoperational items. We had a decrease of $0.27 per share in the quarter. This decrease, compared to the prior year, was primarily driven by a higher adjusted effective tax rate having a $0.23 impact and higher financing costs of $0.04.

Now let's move to a brief review of year-to-date results. Net sales of almost $6 billion were up 16% versus prior year. Year-to-date reported operating income was $605 million and adjusted operating income was $619 million. Reported operating income was lower than adjusted operating income primarily due to restructuring and other costs. Our year-to-date reported earnings per share was $5.63 and adjusted earnings per share was $5.80.

Turning to our year-to-date net sales bridge, 16% net sales growth has been led by $946 million of price mix improvement, primarily from North America. The sales volume increase of $156 million was driven by volume increases in each of the regions, primarily in North and South America, mostly offset by a sales volume decrease of $146 million from the presentation change related to the Argentina JV. These sales increases were offset by significant foreign exchange headwinds of $136 million for the first 9 months of the year.

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 $0.51 per share year-to-date. The increase was driven by margin improvement of $0.89, offset by foreign exchange of $0.23 and lower volumes of $0.14.

Moving to our nonoperational items. We saw a decrease of $0.29 per share year-to-date, driven primarily by a higher tax rate of $0.25 per share and higher financing costs of $0.07.

Moving to cash flow. Year-to-date cash from operations was $80 million. Our cash from operations has benefited from increasing net income and has been offset by rising working capital investment. Our working capital balances are higher due to increased invoice prices reflected in our accounts receivable and rising corn costs reflected in our inventory values. As a reminder, our accounts payable balance does not rise as much as our inventory value due to the very short payment terms when procuring corn.

Net capital expenditures were $196 million, up $10 million from the prior period due to the timing of spend and in line with our 2022 expectations for capital commitments.

With respect to acquisitions and investments, in the quarter, we acquired additional shares of PureCircle, from minority shareholders for $13 million, which, as Jim mentioned, takes our ownership percentage to 85%. In the first 9 months of the year, we paid $133 million of dividends to Ingredion shareholders and repurchased $112 million of outstanding common shares. During the quarter, we also authorized a new stock repurchase program for up to 6 million shares through December 2025, replacing our previous program.

Now I'd like to address our updated outlook. We expect net sales to be up mid double digits driven by strong price mix and volume growth on a comparable basis. We expect full year reported operating income to be up significantly as the prior year reflects the impact of the net asset impairment charge related to the contribution of our Argentina operations to the Arcor joint venture. We expect adjusted operating income to be up low double digits compared to last year.

2022 financing costs are expected to be in the range of $88 million to $93 million, reflecting primarily higher incremental borrowing costs. Our adjusted effective annual tax rate is anticipated to now be between 28.5% and 29.5%.

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Cash flow from operations is now expected to be in the range of $225 million to $275 million, reflecting greater working capital investments as a result of higher invoice prices reflected in our accounts receivable, and higher corn costs reflected in our inventory values. Net capital investment commitments are expected to be between $290 million and $320 million, of which approximately $85 million will be invested to drive specialty growth.

We now expect our full year 2022 adjusted EPS to be in the range of $7 to $7.45, up from the previous range of $6.90 to $7.45. 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 67 million to 68 million for the year.

For our regional outlook, North American net sales are expected to be up 15% to 20%, driven by favorable price mix and higher volumes. Operating income is expected to be up low to mid-double digits driven by favorable price and product mix more than offsetting higher input and corn costs.

For South America, we now expect net sales to be up 10% to 15%, reflecting strong favorable price mix more than offsetting the impact of the presentation change for the Argentina joint venture. South America operating income is also now expected to be up high double digits, driven by favorable price mix.

In Asia Pacific, we anticipate net sales to be up 10% to 15% versus the prior year. We now expect operating income to be up mid-single digits compared to the prior year, driven by PureCircle growth.

For EMEA, we expect net sales to be up 10% to 15%, which includes KaTech, and we now expect operating income to be flat to up low single digits, driven by favorable price mix, partially offset by higher corn and energy costs and negative foreign exchange impacts.

That concludes my comments. Let me hand it back to Jim.

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

Thanks, Jim. Before we open the call for Q&A, I'd like to conclude today's remarks by reflecting on how we perceive both the near-term navigation of the macro environment, while we pursue the long-term opportunities inherent in our driving growth road map.

As I mentioned earlier, our growth road map is centered around the customer. And the breadth and diversity of our customer base is a tremendous asset in times like these. We sell across the many end-use markets of retail, private label and food service and to thousands of local customers as well as large multinational CPG companies. With a broad core and specialty food ingredients portfolio, our products benefit regardless of consumer product price points. For example, when our consumer is economizing, demand for core sweeteners is strong and our customers also find uses for specialty starches when formulating for affordability. Of particular relevance as it applies to the largest component of our specialty sales, the global market for texturants is growing 3% to 5%, and generally experiences consistent demand through different economic cycles. This is due to their versatility, their functionality and their affordability.

Therefore, to ensure we have capacity where we anticipate it will be most needed ahead of growing demand, we are investing $160 million over 3 years to support our texturizer growth. I'm pleased to say that we have already invested about 1/3 of that amount supporting the growth of our clean label franchise, and we are localizing more production in all 4 regions. These investments offer attractive returns with low execution risk.

In closing, our third quarter was very strong and exceeded our expectations. Sales growth, operating efficiencies and our ability to more than offset inflationary headwinds underpinned our performance. As we close out 2022 and we look forward into next year, we are confident that the company is well positioned to deliver long-term growth and value for shareholders.

And now let's open the call for questions.

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QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Ken Zaslow with BMO.

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

A couple of questions I have. The first one is, can you talk about your opportunities for pricing into 2023? If you go through 2022, it looks like you are in the 15% to 20% pricing across your businesses. Do you expect to be able to take another pricing across the business? Will there be ones that have greater pricing ability? How do you think about that into 2023 broadly?

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

All right. Let me take a shot at that first, and then Jim can add some color commentary. So with respect to inflation in the U.S., so my comments are specific to the U.S. We're seeing both corn as well as some other input costs being up. So as it relates to corn inflation, as an example, if you look today at the comparable U.S future strip, it's up about $1 to $1.20, a bushel, which is approximately 20% from our prior year contracting reference point. And so if you look at that and then you look at other input cost inflation, for example, energy and packaging, we're seeing mid-single-digit inflation in chemicals and packaging.

Energy costs will be up considerably, but we're largely hedged for 2023, and that will all be taken into consideration into our 2023 pricing. So as it relates to contracting, and it's early to talk about that, we will be seeking price increases which will pass through the expected cost of inflation. And I think there's general acknowledgment to all of those elements that I just described that those are just real input costs that are going up year-on-year.

The other thing that's, again, very noteworthy is in our industry, grind utilization still is at very high levels of 89%, for example. And typically, when that's the case, along with the environment that I just described, that acknowledgment and that enablement for pricing does continue. So that's how I would describe, I guess, how we're thinking right now about 2023 pricing, Ken.

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

Great. And then just on Pakistan, you were able to deliver a very strong number in EMEA. I'm assuming that the Pakistan -- did you quantify the impact of Pakistan and I'm assuming it's not going to repeat next year? Is that a fair way? And I'll leave it there.

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

I'm going to let Jim Gray take that one.

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

Sure. I think previously, when we're finishing Q2 and we were kind of noting that there have been some significant flooding in Pakistan, we were somewhat cautious. We didn't know how broadly the flooding kind of throughout kind of one of the major rivers in Pakistan would impact both customers. And largely, I think that we've seen that has rolled through September, and we were really modestly impacted. Obviously, there are temporary road closures and some of our customers were closed. But we really worked through that. So really not too much impact, Ken, to your point, maybe less than $1 million of impact to EMEA during the quarter.

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I think maybe more going forward is some of the flooding had an impact on the cotton crop, and a portion of our starches are sold into textile industry in Pakistan, which then exports gray cloth and materials to Europe and to the U.S. And we're going to see that slow down just because of the domestic availability of cotton. So that -- we'll watch that a little bit, but not as concerned about that.

I think more broadly, when we look at Pakistan, we're just concerned about the corn costs. The corn cost has risen significantly. And what we're finding is that our team is quite agile on the ground. As an example, overall inflation is probably in the 23% range in September of this year, and we're probably looking at food inflation that's maybe even north of 50%. So we're just sensitive in terms of watching the cost of corn, watching our energy costs in Pakistan and making sure that we recognize that in our pricing that we need in the country.

Operator

Your 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 guess my first question, as I think about the volume outlook across the business into the fourth quarter and into the first part of 2023. Jim, you just made the allusion to kind of corn grand utilization being high in the -- I think you said 89%, if I heard correct. But can you just talk about what you're seeing kind of by different product types, categories, regions on the volume side and overall volumes in the quarter were flat. I know there's some moving pieces. You have the strike in Cedar Rapids, which is, I can't imagine, helping kind of the utilization throughput. So just maybe some color on what you're seeing in different categories. And any sense on customers that may be looking at their inventories in a different way than they were 6 months ago.

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

Sure. Sure. Thank you for the question, Adam. So I would say, first, just starting from where we just finished. Through quarter 3, volumes have been steady and robust. We're certainly carefully watching the impact of continued inflation on customer demand and the potential that's still out there for a resurfacing, for example, of a rail strike in the U.S. in November. I would say there are some signs that food service demand is bifurcating right now with quick service demand increasing at the expense of full service and fast casual. We're certainly seeing at the retail level that private label is growing both in Europe as well as in the U.S. at the expense of some of the branded type products, which is typical in a somewhat recessionary environment.

Interestingly, corn sweetener demand has been particularly strong. And our starch demand has continued to be very strong. And we believe that those products lend themselves to affordable formulating.

What I would also say is in relationship to your comments around Cedar Rapids, demand for papermaking starches are also robust and that continues. And as it relates specifically to the Cedar Rapids facility, after an adjustment month, I would say, in August, after the work stoppage began August 1. The plant is now operating actually very well under business -- under our robust business continuity plan, and we're steadily increasing production to meet customer needs.

We're currently in active discussions with the union. We continue to bargain in good faith, and we're hopeful that will reach a mutually beneficial agreement there that will allow us to continue to service the papermaking market and also corrugated box market going forward, where again, demand for certainly paper making or an uncoated free sheet remains strong and corrugated, it's a little bit soft, just related to the overall economy, but nonetheless, we're in good shape there.

I would say that it's just important to remember coming back to food that we have a broad customer base, again, and we service both branded, private label, food service, large CPGs, many, many local companies given our breadth in 120 countries around the world. And typically, our products go in at such small levels -- they're very multifunctional and versatile. And I think they weather typically not any kind of feast or famine type demand moves, just based on history of going through different recessions. So hopefully, that gives you some color for how I'm thinking about volume.

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

No, that's all some really helpful color. And then just a follow-up on cash flow. And I know the outlook for cash from ops kind of was trimmed on working capital intensity. And Jim Gray, maybe just help us think about the implications of that into 2023? And is there reason to believe that there's a -- some working capital release that would be likely next year, absent another step-up in corn prices and inflation? Or how does that actually flow through the balance sheet and cash flow statement over the next 12 months?

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

Yes. Sure, Adam. I think what we're seeing is that when we look at the cash from ops really that's in our supporting tables, it's taking the endpoint in 2021. I think at that time, both corn was lower as well as we move through, we've seen corn costs rise globally since the beginning of the Ukraine conflict.

What we're now seeing, I think in our AR is kind of a steady run rate. So if I look at the -- I'm looking at the end of Q1 to Q2, the end of Q2 to end of Q3 and accounts receivable is relatively in line with our quarterly sales. And so I'm encouraged there. I think we are still seeing some of the corn costs pass through our inventory. And also just recognize that this is a seasonal type of the year. So most of the harvest are done in the Northern Hemisphere. And so this is when we have in some markets where we have to buy our corn. And so, for example, like Pakistan, we bought a lot of spring corn, much of that's on our balance sheet.

And so I think as we just roll forward -- and we'll finish out Q4. And then we'll look at the beginning of 2023. Likely, there'll be price increases that will still be rolling through some of our invoicing, but I generally see the net demand for working capital to be much, much less than what we've experienced in the first 9 months. And then -- and that's kind of assuming that the overall global corn market stays elevated, kind of reflecting the U.S. strip price, mid-6s per bushel, right? If -- and just for everybody on the call, post the '23 crop size in the U.S. as we get into a feeling for the carryout in next year or even '24 if we see corn coming down, and that usually is beneficial to our working capital.

Operator

Your next question comes from the line of Rob Moskow with Credit Suisse.

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

I have a few questions. One is on the plant-based business. Can you give us an update on how you're doing versus your internal targets? I know you said 145% sales growth, but that was off a very small base last year. So what I'm interested to know is I think you said it would be a drag on operating profit this year and then maybe better next year. So maybe an update there?

My second question is about your FX outlook for the year. Maybe I missed it, but do you have higher headwinds from FX to your EPS than you thought? But how does that impact your EPS guidance, if at all? And then maybe I'll wait for a follow-up.

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

Right. I'll take the PBP question or plant-based proteins, which is the acronym we use here, and Jim will take the ForEx question. So as it relates to plant-based proteins, specifically as it relates to your direct question, for 2022, our revenues are trending within the range we provided at the beginning of the year, albeit on the lower end, but they are trending within the range that we had provided.

With regards to the anticipated operating income improvement, we continue to improve our production each month. In fact, at 2 facilities in October, we had record production months from a standpoint of quality of inventory and salable product. And we have -- we'll have a much more

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complete look at the go forward in relationship to the operating income improvement at the end of the year and probably be providing an update on that in quarter 1.

As it relates just to the entire plant-based protein category, I would say that I would remind everybody that the approach that we've taken is to build a broad portfolio across protein flowers, concentrates and isolates across 4 types of pulse-based proteins. So we're not dependent, for example, just on P-protein isolate that goes into alternative meats. So it's a systems approach, it's a formulation approach. And while there has been weakness in demand for certain portions of the market, we're not dependent on sales into one product category exclusively, for example, alternative meats. And we were not, from the beginning, a large supplier to any one of the large alternative meat producers.

So we still have a very robust project pipeline with many customers. And we're monitoring the category just like everybody else is. And clearly, price points and perhaps other questions around clean label, formulating, et cetera, for alternative meats have dampened the demand there. But we still believe that this is a trend, not a fad that's supported by significant sustainability drivers and that at the end of the day, it's going to be about formulating great tasting, great texture and highly nutritious products. And we think our formulation approach across flowers, concentrates, isolates along with our fifth growth platform, which is food systems, that whole approach is what ultimately will serve us well in this category.

So we're in it for the long haul, and we're still optimistic. And it does make us a more complete supplier. When you think about us being a leader in texturizing, a leader in sugar reduction and a leader in plant-based proteins, they all support one another from a standpoint of innovative, new product development opportunities for customers.

And some of our wins right now that we're seeing are in alternative snacks, for example, or protein-fortified snacks in bakery and alternative dairy as opposed to, say, dependent upon alternative meats.

So again, more fulsome update in quarter 1 on the exact financials. Rob, but that's how I would answer that. And I'll turn it over to Jim on the ForEx question. Yes.

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

Rob, you had a follow-up on plant-based proteins?

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

No, go ahead, please.

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

Okay. Just -- so on FX, I think as we have seen the dollar really strengthen is obviously, we're absorbing that foreign exchange impact, and we're pretty clear on our tables. I would say that our full year updated outlook does kind of include where the dollar is at today relative to kind of other foreign currencies that are key in our markets.

It's part of our business model, and we've consistently been able to try and offset foreign exchange headwinds because it impacts the cost of corn, which is traded globally in dollars. And so that's going to show up in our local pricing models as we're looking at changes in the value of corn, I think it's somewhat well understood by our customer base.

And maybe just to highlight. It's pretty noteworthy that both South America and EMEA, which had a fair amount of foreign exchange weakness, had expand in gross margins. So what we're trying to do, Rob, is really become tight and resilient on seeing that FX change, seeing that impact on our raw materials, which is either energy or corn and then being able to be pretty agile and in passing that through. We're still going to have lags, but just -- I think we have built some roll motels on our execution around that.

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

Okay. Actually, my follow-up. You said that you're now at the lower end of your range for your plant protein revenue target. Is that because the alternative meat category has softened?

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

Not specifically. Because again, our projections were across the entire platform of applications that I described and customer base. So we were never entering the space to supply a magic bullet for one product for one category. That again has not been our approach or strategy.

I just think that if you remember, we had at the beginning of the year, a little bit of challenges just ramping up into an entirely new product category for us. But we've demonstrated each and every month improvements in our production and our ability to make food-grade products at the highest quality. And so I think it's a timing issue related to that. But look, the category is evolving and going through changes, and we'll continue to monitor it. So for the long term, we're still optimistic about the plant-based protein category.

Operator

Your next question comes from the line of Benjamin Theurer with Barclays.

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

So 2 questions. So one -- and this was just a couple of weeks ago that when you talked about some of the potential risks in EMEA and more specific within Europe. Given the developments that we've seen in some of the countries, be it Germany, be it France and so on and efforts to try to bring electricity prices down, supply to -- support of industries consumers, et cetera. Are you feeling more comfortable within your outlook as to not running into shortages and actually getting some government support? And how do you think this is going to play out, particularly into 1Q, maybe and a little bit into 2Q, if you could give us a little bit of a sneak preview. So just on your expectations on Europe, energy side and the risks associated with that. That will be my first question.

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

Okay. Let me take that. And what I would say is that we're obviously very pleased with our performance in quarter 3 for EMEA in total. As it relates specifically to Europe, we are cautiously optimistic in relationship to the energy situation. As you highlighted, compared to the peak of energy costs in Europe, they have declined sharply since the summer peak. And it is though noteworthy that they still are 2 to 3x higher than they were at the beginning of 2021 prior to the Ukraine conflict, and they still sit 6x the level of the U.S. from a standpoint of gas prices.

What we are seeing, and I think that everybody is encouraged by the fact that the EU in solidarity has built gas storage to levels approaching 90% to 100%, and that is including Germany. At this point, we do not foresee any government curtailment of natural gas in Germany for the winter. And we're anticipating that we will be able to manage through the situation as it continues to develop.

Europe also has been impacted, as you know, by a tough summer drought, and that has impacted the corn crop as well as the wheat crop, for example.

And we, though, one of the comments that we made in the presentation is that we've looked at our contingency plans and business continuity plans to support our customers leveraging and flexing our global network. And we genuinely believe that given some of the decisions we took to say go long on our corn positions and our specialty corn crop positions, not just in Europe but also in the U.S. as well as now the new network capacity from China, all of that allows us to flex and leverage that global network on behalf of our European customers that are concerned about

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potential shortages of, say, grain that can be turned into starch for their needs going forward. We believe we're actually going to be able to support them, leveraging our network.

All that being said, what we are, I think, concerned about is how much of the inflationary increases that we're all reading about that are impacting the EU at 10% just this past month. Today, I believe it was announced that the U.K. just is at 11% inflation in the month. What that's going to do to the consumer ultimately, and how that affects consumer buying behavior. And that's kind of hard to predict at this point in time, except to say that we're in the food industry. And at the end of the day, again, we've weathered recessions based again on the diversity of how diversified our products are that go into all the different elements of food consumption.

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

Perfect. And that actually nicely brings me to my second question. It was kind of interesting to see if we take a look into the volume. So if we think about APAC, also South America, volume growth was definitely on the positive side, while within EMEA and in the U.S., we've seen it on the negative side. And I've heard a lot from some of the other companies out of Lat Am, et cetera. Just talking about how they're -- they've lived with inflation for much longer, right? I mean, if you have operation in Argentina, they know what inflation is about. So the question really is, have you seen significant differences in how your customers accept price increases and actually can pass this on and even consumers just look through it by being a little less sensitive to price increases, lower elasticities, maybe in some of the emerging markets and that, in the end, has been a benefit to you, just given your global footprint between emerging markets, developed markets? And how do you think how resilient that consumer down in South America, in APAC actually is all the price increases you've been pushed through.

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

I'll let Jim take a shot at it, and I'll add any color commentary, Jim.

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

Yes. Ben, as you noted, and I think we've noted. When we think about various economies, particularly some of the South American countries, I'd also add Pakistan to that where we have -- let's like emerging and/or kind of more developing economies. And you've seen inflation. And inflation is an ongoing presence in daily life. You get price changes. Clearly, both our customers are more open to and agile in looking at, wow, the cost of the ingredient from Ingredion has changed, how do I work that into my costing and therefore, how do I think about my pricing going forward?

So to the extent -- unless you have real true economic disparity in one of those more developing economies generally, you're going to see consumer acceptance and kind of absorption of that higher pricing. And definitely have kind of more resilience in the populous as well as some of our customer base. When you move to more of a slower growth economies that may be more developed like you get to the U.S., maybe Northern Asia. And you get these changes in the cost of the underlying raw material and it's a big part of our COGS. We then have to work through those pricing centers of excellence with those customers to introduce and explain why is our cost changing, why does our price to them for ingredients need to change?

And that's what we work on in our commercial teams as well as our pricing centers of excellence and advertising that. And to the extent that I think that our customer base what I'll call lower growth, historically lower inflation economies is now becoming much more agile and accepting that, wow, yes, we're seeing the change in the energy, we're seeing the change in the raw materials. And I think that's kind of contributed to our success in putting pricing through this year.

Operator

Your last question comes from the line of Ben Bienvenu with Stephens.

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

I want to ask about the guidance. And in particular, recognizing that you guys did narrow the range a little bit for the year. It's still -- the implied range for the fourth quarter is still quite wide. And so I want to unpack a little bit of kind of the elements of variability that you see ahead and what ultimately prompted you all to obviously narrow the range, but still leave it as wide as it is?

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

Sure. Ben, I'll take that, and I deserve to be beat up for that one. I think when we look at our business, which largely is manifested in the Northern Hemisphere, and we come through the year, we can look at the layout of the corn, we can look at the spring crops and kind of anticipate what the harvest is going to be. So we get better, I think, consistency in view into the business for Q2 and Q3 in terms of the pull.

Traditionally or at least historically, what we've seen in our customer base, as we finish the year, particularly with multinationals, CPG firms has been -- what's their focus on their inventory levels as they're closing out their fiscal year if that happens to coincide with the calendar year. And so particularly in some of our specialty ingredients, what's their stocking behavior. I think one of you asked previously, I do see that I think inventory levels are going to be carried a little bit higher into the end of the year just because there has been some various supply chain disruptions either in moving ingredients, either around a country or continent and/or across oceans.

And so we're a little bit of -- well, so we see somewhat elevated inventory levels. I think some of our procurement officers that our customers are saying, yes, that makes sense. It's prudent. It's smart. It's a little bit against what we've probably seen in maybe the last 5 or 6 years where we've usually seen a little bit of a kind of more of a drawdown on inventory to try and post a lower number.

So we're anticipating that inventories will carry through, but that could be a downside. I think most -- probably more importantly, Ben, is that there still is and in particularly in the U.S., some supply chain issues. We're going to get through the midterm elections, but there is still rail union labor issues to be resolved. And that is -- November 19 is the deadline for a number of the rails in the U.S. to say either they agree, or they don't agree. So you're -- and that causes all sorts of potential truck and intermodal disruption.

And then you still have a port issue on the West Coast. And so those things, I think, are just -- like they're not in our center cut guidance. We think we're going to be able to get through those. But if you look at the range, I think it's also helpful for you all to understand that some of us are looking at that and saying, yes, that could have an impact. Low probability, but it could have an impact.

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

Yes. And that's exactly what I would say. I would say that we just are taking a cautious view towards the -- there's still uncertainty in relationship to that rail situation. Again, November 19 is a big date. We'll see if there is either a slowdown or potentially a strike. Hopefully, the government again can intervene and avoid something like that. Let's say, 4x timing, Jim, right, we say 3 to 6 months, or the dollar continues to remain very strong. So that's kind of factored in, I think, just a timing issue related to that.

And as Jim said, it's just, I think, common sensical to assume that companies will be making some year-end adjustments to their inventory positions, probably for working capital reasons as well. And so we've kind of reflected on all of that and factor that into the go-forward guidance here for the full year.

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

Okay. Great. Makes perfect sense. My second question is just related to margins. The -- taking into account roughly the midpoint of the guidance implied in the fourth quarter, there is still material sequential compression in operating margin. But year-over-year, you seem to be making progress on margin expansion. And I would think that would continue to be a trend as we move into next year, margin expansion year-over-year. So can

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you talk about the things that when you look out on the horizon and the visibility that you have, can you talk about the path back to 2021 or 2020 margins and how you get there?

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

Well, Jim and I can tag on that. Do you want to go first?

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

Yes. I think, Ben, you touched on a great question, and I've had a conversation with a number of you on how we think about the corn layout and how it impacts each quarter. Previously, we talked about a hedging strategy, which may have lapped us a little bit more exposed in Q3 or particularly Q4, which I think is what we felt in the end of 2021 when kind of corn started to rise up. Here, you get into 2022, we're expanding our hedging strategies. And we have not exactly all the kind of the evenness of the coverage over all of the quarters. And so as the Ukraine conflict impacted, as Jim mentioned, corn is probably up between $1 to $1.20 a bushel year-over-year. There's still a little bit of that compression that is in Q4, but largely, largely, we've mitigated a lot of that impact.

As we even further kind of mature and dial in what we're hedging relative to our contracting, particularly for U.S. Canada business into 2023, I really think the layout of that kind of net corn impact is even going to be smoother, right?

So Ben, what we're trying to do with respect to some of the ag movement is really get to a consistent base level of either gross profit ROI that you all can see. And then for us, moving forward, and getting to higher levels of gross margin, it's really focused on where is the value in either specialty ingredients. It can be focused on the value of upgrading some of our core ingredients into new uses as well as really focus on operating and operating efficiencies. I'm going turn it to Jim to...

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

Yes, I would say we have margins as a key performance indicator that is very strongly in focus for our leadership team. And that's about mix enhancement on the specialty side. And we have an intense focus to grow our food systems business which we believe has a lot of things going in its favor from a standpoint of more integrated systems and solutions to offer to customers that typically come with a higher margin threshold.

So upgrades in our specialties, but also upgrades in our core from a standpoint of trading up on the margins there for that grind utilization, which is, again, operating at the higher levels of historical norms in our industry. And we do see opportunities, and we are already capitalizing and pursuing on opportunities for that 2/3 of our business to move up the margins in that core as well. And that's, I think, a very significant point to emphasize in addition to specialties and not just think about it in the specialties way.

And the other thing I would say is that you can't count on ForEx. And certainly, we don't because we've lived for the last x number of years since I've been in my role with significant dollar strength. But at some point, the dollar will moderate and all of the hard work we've put in when that does moderate will also help our margins. So I think that for all those reasons, we think that we will see, certainly, modest improvements in our margins going forward. We're working on it. We're very, very focused on it.

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

Yes. I mean and Ben, as we've said in the past, I mean, we're at the height of a corn price cycle, right? So we're witnessing some of the highest corn costs that we've seen in years, right? And then as we get, hopefully, that higher corn price and sent farmers to grow relative to other ag inputs. And as we get better carryouts and maybe crop sizes, right, that's going to help us. I think as we've seen -- it makes our products more attractive because we do pass through some of that corn cost decrease when that occurs. But generally, it's also then we're holding on to our gross profit dollars per ton and then that is gross margin expensive.

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Operator

There are no further questions in the queue. I will now turn the call back over to Jim Zallie for closing remarks.

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

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

Operator

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

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