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INGR - Q3 2014 Ingredion Incorporated Earnings Call

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OVERVIEW:

INGR reported 3Q14 sales of about $1.5b, YTD 2014 EPS of $3.89 and 3Q14 EPS of $1.60. Expects 2014 sales to be below prior year and EPS to be $5.35-5.50.

CORPORATE PARTICIPANTS

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Ilene Gordon *Ingredion Incorporated - Chairman, President, and CEO*

Jack Fortnum *Ingredion Incorporated - EVP and CFO*

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Robert Moskow *Credit Suisse - Analyst*

Kenneth Zaslow *BMO Capital Markets - Analyst*

Brett Hundley *BB&T Capital Markets - Analyst*

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Ingredion third-quarter 2014 earnings conference call. For the conference, all participant lines are in a listen-only mode. There will be an opportunity for your questions. Instructions will be given at that time. (Operator Instructions) As a reminder, today's call is being recorded.

With that, I'll turn the conference over to Mr. Steve Latreille, Vice President of Corporate Finance. Please go ahead.

Steve Latreille - *Ingredion Incorporated - VP of Corporate Finance*

Thank you, John. Good morning, and welcome to Ingredion's third-quarter 2014 earnings call. This is Steve Latreille, Vice President of Corporate Finance. And joining me on the call this morning are Ilene Gordon, our Chairman and CEO; and Jack Fortnum, our CFO.

Our results were issued this morning in a press release that can be found on our website, ingredion.com. The slides accompanying this presentation can also be found on the website, and were posted about an hour ago for your convenience.

As a reminder, our comments within this presentation may contain forward-looking statements. These statements are subject to various risks and uncertainties. Actual results could differ materially from those predicted in the forward-looking statements, and Ingredion is under no obligation to update them in the future as or if circumstances change. Additional information concerning factors that could cause actual results to differ materially from those discussed today during today's conference call, or in this morning's press release, can be found in the Company's most recently filed Annual Report on Form 10-K and subsequent Reports on Forms 10-Q and 8-K.

Now I'm pleased to turn the call over to Ilene.

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

Thanks, Steve. And let me add my welcome to everyone joining us today. We appreciate your time and interest.

We delivered another quarter of strong performance, and our business momentum continues. Three of our four regions in North America, Asia-Pacific, and EMEA delivered good volume growth. Although overall volume was down slightly in South America, we saw nice volume recovery and growth throughout the region, except in Brazil, where the economy is stagnating.

Operating income grew 30% and the growth was broad-based. Every region delivered double-digit growth for the first time since we acquired National Starch four years ago. The strong operating income performance translated into a 45% increase in earnings per share. We said that the third quarter was going to be our strongest, and it certainly was.

We have consistently commented that our solid cash flow from operations and our strong balance sheet enabled us to strategically deploy cash to generate excellent shareholder returns. Over the course of this year, and especially in the last few months, we've demonstrated this commitment through our actions, which are well-aligned with our strategic blueprint.

During the last quarterly earnings call, we announced an accelerated share repurchase program of approximately $300 million, which will be accretive to earnings per share this year and going forward. Now, since then, we committed about $100 million in capital investments to drive organic growth. Furtherly, these investments will increase capacity for our fast-growing specialty ingredient portfolio, specifically in the areas of texture and clean label ingredients. These products deliver against key consumer trends, and are areas in which we have considerable expertise.

And a couple of weeks ago, we announced our pending acquisition of Penford Corporation, a leader in specialty potato-based starches. This will nicely round out our product portfolio with complementary specialty ingredient solutions. I'm very excited about the opportunities the Penford acquisition will bring us, and I'll talk more about this later on the call.

Now let's spend a moment on each region's performance in the quarter. In North America, volumes rose 3% behind good demand in the US and Canada. This more than offset expected modest volume declines in Mexico, resulting from the government-imposed obesity taxes. Meanwhile, our specialty business in Mexico grew double-digits again this quarter.

Operating income in the region was up 17%, with strong performance in every country. In fact, North America's operating income of $113 million is a record quarter for the region. In the US and Canada, volume growth and strong cost-containment initiatives contributed to the gains, while improved product mix from our specialty growth in Mexico also added to the good operating income growth in the quarter.

We remain enthusiastic about our long-term prospects in Mexico, our second-largest market behind the US. We have a strong manufacturing and distribution presence in the country, and the long-term outlook for economic development in Mexico is excellent.

Turning to South America, we saw good volume across the entire region with the exception of Brazil, which more than offset the growth in the rest of the region. The economic outlook in Brazil has softened from earlier official estimates, with GDP forecast to be close to flat in 2014, and our business there is seeing the effect. Overall in South America, volume was down 2%.

Operating income increased 46% in the region. And the increase was broad-based across our operating units, including Brazil, despite volume weakness. Operating income in Brazil was up double-digits, as our local leadership team effectively managed pricing and product mix as volume declined. Our Southern Cone region also managed double-digit operating income gains through good volume growth and price mix management, which more than offset currency headwinds and higher input costs.

Argentina remains a very challenging business environment, but our management team has been able to adjust to the difficult operating conditions. And our business performance has generally been playing out as we expected from the beginning of the year. Rounding out South America, the Andean region continues to perform well, with good volume growth in line with a healthy GDP.

Moving on to Asia-Pacific, we generated 4% volume growth, which was broad-based throughout the region. This performance reflects solid specialty growth in key markets. In addition, operating income in Asia-Pacific was up 14%. In EMEA, continued strong demand for specialty products resulted in a 3% volume gain and a 28% operating income gain. In Europe, we continue to see excellent returns from our capacity investments in specialty starches, which are now fully operational, and enabling us to meet growing demand, while improving our manufacturing cost profile.

Our European capacity investments have helped us optimize our global specialty starch manufacturing network to leverage growing demand throughout the world. And our upcoming investments of about $100 million in our specialty starch capacity, in Asia-Pacific and North America, fully support our organic growth strategy while improving our manufacturing network for these high-value products.

Our business in Pakistan managed a difficult environment extremely well, with damaging floods and political unrest during the quarter, both of which interrupted logistics activities in the country. Pakistan is another example in which solid economic growth is translating into good business performance, despite some unique challenges along the way.

Both the Asia-Pacific and EMEA regions have consistently delivered strong operating results each quarter this year. This performance is in line with our expectations, given our specialty product portfolio and local manufacturing presence in key countries.

That concludes my review of strong third-quarter operations across our regions. With that, I'll turn it over to Jack for a review of the financials. Jack?

Jack Fortnum - *Ingredion Incorporated - EVP and CFO*

Thank you, Ilene. Good morning, everyone. Let me start with covering some of the highlights of the income statement. Although sales were down $152 million, it was largely the result of passing through lower-priced corn in our selling prices. You'll see this effect in our nine-month results too.

Gross profit was up $39 million, which is a 15% increase, reflecting good volume growth and price mix gains. Similarly, the gross profit gains translated to the operating income growth of $41 million, including lower corporate expenses. On the earnings per share line, we delivered $1.60 per share or about 45% more than last year.

Moving on to the net sales bridge, our sales of about $1.5 billion are lower than last year by about $150 million. Volume growth across most of our regions contributed $35 million to net sales growth, but this was offset by a $34 million negative impact from foreign exchange, primarily in Argentina. The remaining reduction in net sales is due to lower pricing from passing along lower corn costs.

As we look more closely by region, you can see the foreign exchange headwinds in South America were offset by good volume growth in North America, Asia-Pacific, and EMEA. Lower pricing primarily reflects lower corn costs in North America.

As we look at operating income across the regions, you see solid growth in every region and lower corporate expenses. The lower corporate expenses are the results of a combination of good cost management and a reimbursement we recorded related to an indemnification payment from a previous acquisition. The underlying liability is reflected in higher tax expense. The impact on the net income and earnings per share is zero.

Turning to the drivers of our earnings per share improvement of $0.50 per share, operating income -- operational items represented a $0.40 improvement, primarily from margins and volume. Foreign exchange was a small drag on earnings, while other income contributed $0.06, primarily related to the tax indemnification payment mentioned previously.

Below the line, nonoperational items contributed $0.10, driven by lower financing costs of $0.03 and lower shares outstanding, which was a $0.07 favorable impact. The lower shares outstanding relate primarily to repurchases we made at the end of 2013, but we are also starting to see the benefit from the approximately $300 million accelerated share repurchase program we began to execute this quarter. The ASR program will favorably impact our fourth quarter, and next year, diluted earnings per share on a comparable basis as well.

As we turn to year-to-date figures, I mentioned the impact of lower corn costs on sales. But importantly, gross profit dollars are slightly up from last year. This reflects solid gains in the second and third quarters. These gains are now offsetting the decline in gross profit we faced in the first quarter related to severe weather in North America and a significant currency devaluation in Argentina.

Operating income is slightly above last year on a year-to-date basis, as the regions continued to gain momentum. Earnings per share is above last year at $3.89 per share compared to $3.71 a year ago.

For the first nine months, net sales were down about $500 million, primarily reflecting the pass-through of lower input costs on selling prices. Foreign exchange also negatively impacted net sales, and was partially offset by the contribution from solid volume growth. When we look by region, you can see the currency translation, primarily from Argentina and South America, continues to weigh on net sales, while volume is positive across the board. Price mix is unfavorable, due to the pass-through of lower corn costs in North America, Asia-Pacific, primarily Korea.

Operating income in North America and South America on a year-to-date basis remains below last year, despite sequential improvements in these regions in the third quarter. North America's nine-month results are weighted down by an extremely difficult first quarter. South America reflects a difficult comparison, driven by good results early in 2013, just prior to the rapid deterioration of the economic and political conditions in Argentina, which persists to this day. I would also like to point out that we continue to actively manage our overhead costs, driving spending efficiencies to offset inflationary pressures in our selling, general and administrative expenses.

Through the nine months, earnings per share are up $0.18 to $3.89, with operations contributing $0.10 and nonoperational items having an $0.08 impact. As we like to see, volume growth is the largest contributor to operational gains, adding an estimated $0.21 to earnings per share. But this is partially offset by a foreign exchange impact of a negative $0.16. We still expect the full-year impact from foreign exchange to be about $0.20 to $0.25 negative impact on earnings per share.

Turning to our full-year income statement guidance, sales will be below prior-year, as we mentioned numerous times, as selling prices reflect the pass-through of lower corn costs. Earnings per share is now expected to be in the range of $5.35 to $5.50, which is a narrower range and slightly lower than our previous guidance provided in July. You will recall that our original guidance at the beginning of the year was in the range of $5.35 to $5.75.

As Ilene mentioned in her opening comments, we feel very good about the momentum of our business in all regions. We are performing about at the level we had anticipated when we started the year, but we have not been able to make up for the challenges we encountered in the first quarter.

Simply put, our second and third quarters, and our forecast for the fourth quarter, are in line with the expectations we set forth in the original guidance at the beginning of the year. But as a result of weaker results earlier in the year, we have adjusted our full-year earnings per share guidance accordingly. Financing costs are anticipated to be slightly below last year, and our -- the effective annual tax rate is expected to be between 27% and 28%.

Turning to the outlook by region, I'll start with North America. The good volume growth we have had in the US and Canada is expected to continue in Q4. We expect this volume growth to be partially offset by declines in Mexico, as has been the case all year, resulting from the government-imposed obesity taxes. Operating income is expected to be up slightly in the fourth quarter, which will mark the third consecutive quarter of growth. However, due to the challenges from the first quarter, the full-year outlook for operating income will be down slightly in North America.

In South America, where they are entering the summer season, we expect volumes to become stronger sequentially in the fourth quarter, as modest recovery in the Southern Cone and the Andean region is offset by volume softness in Brazil, due to the weak economy there. In terms of operating income, we expect the fourth quarter to be largely in line with last year's fourth quarter, which puts the anticipated full-year operating income in South America down slightly year-over-year.

The story in South America has not changed. Southern Cone is a challenging environment, but we are managing through it as expected. Brazil's economy has been sluggish and disappointing, but we will continue to seek opportunities for growth. And finally, the Andean region is a bright spot in an otherwise difficult region, with solid, consistent growth this year.

We move to Asia-Pacific, we expect a consistent solid volume growth throughout the region to continue into the fourth quarter. This volume growth, effective price mix management, and anticipated lower input costs, are expected to result in good operating income growth in the region for the full-year.

In EMEA, similar to the Asia-Pacific region, we expect solid volume growth to continue in the fourth quarter. We expect this to be fueled by the benefits of prior capacity investments and good economic growth in Pakistan, as well as a strong specialty starch demand in Europe. Full-year operating income in EMEA is expected to be up double-digits due to anticipated volume growth across the region, good price mix, and effective cost management. Our Asia-Pacific and EMEA businesses have performed consistently well all year, and we are encouraged about the momentum in these regions.

Turning to cash flow, our cash generated by operations was $462 million, which is about $100 million more than this time last year, primarily a result of lower working capital use versus last year. We have put our cash to work in the form of capital investments, dividends to shareholders, and significant share repurchase under the accelerated share repurchase program.

Looking to the full-year, we continue to expect another year for -- we expect another strong year for cash from operations, which is still expected to be in the range of $700 million to $750 million. And while we are continuing to invest in capital projects for growth as well as cost and process improvements around the world, we now expect full-year capital spending to be slightly below the $300 million this year.

Finally, although we have made recent strategic actions to deploy our cash, our strong balance sheet and solid cash flow enable us to make other strategic investments should the opportunity arise.

That brings my section of the presentation to a close, so I will now turn it back to Ilene.

Ilene Gordon *- Ingredion Incorporated - Chairman, President, and CEO*

Thanks, Jack. Let me take a moment to discuss our announcement on Penford. This acquisition expands our higher-value specialty portfolio, which addresses growing consumer trends, including nutrition, gluten-free, food textures, and sustainable green solutions. Additionally, it builds our presence in nature-based hydrocolloid ingredients, and brings other capabilities, which will enhance our efforts to deliver new ingredient solutions to the marketplace.

The economic benefits are quite evident as well. And one thing in particular, which we have not talked as much about, is that there is a real opportunity to drive operating and supply chain efficiencies as we leverage the combined manufacturing network in the US, and better service our customers. We also anticipate at least $20 million in annual synergies, primarily from eliminating redundant public company costs, procurement and supply chain efficiencies, and savings in other general and administrative areas.

Excluding one-time costs, we expect the acquisition to be accretive to earnings by about $0.10 to $0.15 in the first year from Penford's underlying earnings and partial synergy realization. In the second year and beyond, we expect the earnings accretion to be even greater.

In summary, this acquisition is very well-aligned with our strategic blueprint.

So, as we wrap up nine months of the year, we feel quite good about where we are today. Our strategic blueprint continues to drive our commitments, actions, and performance. We have excellent momentum overall in APAC and EMEA. In North America, we are very clearly on track after a difficult first quarter. And in South America, we continue to manage through an extremely difficult business environment in Argentina and low economic growth in Brazil.

With the recent strategic actions we have taken, such as planned investments for organic growth and accelerated share repurchase programs, and now an attractive acquisition, we are confident that we will continue to create shareholder value.

And now we'd be happy to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Robert Moskow, Credit Suisse.

Robert Moskow - *Credit Suisse - Analyst*

A couple of questions. Ilene -- Penford. That's been a public company for many years; it's been around. And I think you've been talking about making acquisitions for a long time. Why buy it now?

It seems like it was -- it's something that Ingredion could've done before. What was the catalyst for it?

And then secondly, I guess more for Jack, South America is coming in roughly according to plan, maybe a little bit below plan for the year. But I think consensus and most people had been hoping for a much fuller recovery in 2015. It doesn't look like the macro is helping anybody out in that regard. Can you give us any look into 2015 and what to expect?

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

Okay, thanks for the question. I'll start out. So, Penford -- it's interesting, why now? The consumer trends are really growing in the area of gluten-free, some non-GMO, the whole area of texture and sustainability. And the Penford's portfolio really addresses those trends.

So I think that we saw that as these trends were increasing, and Penford's capability, which are extensive in R&D and product development, made it a great fit for our capabilities in texture using other raw materials. So for us, it was a great opportunity to expand our portfolio of high-value specialty products. And then, having the manufacturing capability along with that, and the ability to formulate, really made it very timely.

So I'll turn it to Jack on the South America question.

Jack Fortnum - *Ingredion Incorporated - EVP and CFO*

Yes, Robert. Obviously, we won't be commenting on -- we're not giving guidance for 2015 at this point in time. But just to add my reflection on South America. If you think of Argentina, it's still in a very difficult situation and the election is not until next fall, really, in 2015 -- fall of 2015. Brazil just had their elections. And you know, I think that there, there was some conciliatory type of comments made after the election. And so, there is some stability there going forward.

And so I still look at South America with optimism, I'll say; whether it happens right through -- ultimately through 2015, but I do think that they've kind of got to the point where they are stable. Brazil still has great growth potential from my vantage point, particularly in our product offerings. And then again in South America, I would -- I mean in Southern Cone, I think we are stable there. And I don't know how long that's going to take. We are still looking for a devaluation to really correct the problems in Argentina.

And then when you go up to the Andean region, that region this year has performed very well for us. We've been very pleased with the growth there.

So I know that's not giving you a 2015 forecast, because we're not going to do that at this point in time, but I would say that we've seen stability now. We've seen a little bit of softness in Brazil, but I do think Brazil will start to come back a little bit as time progresses. And then the Andean region is working very well for us.

Do you have anything to add to that, Ilene?

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

Well, I guess I would also say that if you look at countries like Peru and Chile, and as you said, that Colombia has a GDP forecast of next year 4.5%, so that whole western side of South America seems to be very driven by these consumer trends, even in healthy eating. So I think that our products and our capabilities are well-aligned towards that.

Robert Moskow - *Credit Suisse - Analyst*

Okay. Thanks a lot.

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

You're welcome.

Operator

Kenneth Zaslow, BMO Capital Markets.

Kenneth Zaslow - *BMO Capital Markets - Analyst*

I have a bigger picture question. You set out long-term growth targets from 2012. And you can argue that since that time, certain things -- you know, South America, Mexico -- have clearly underperformed relative to your expectations. But yet, you remain firm in your long-term growth algorithms. And my question is, is which part of your portfolio -- what are you doing better to compensate for the shortfall that you could not have forecasted?

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

Well, this is Ilene and I'll start out. You know, the -- as you say, we are committed to our strategic blueprint and our long-term algorithm. And I think that if you look organically, obviously we've addressed different issues by adding capacity where there is growth around the world. And the specialty, I think, portfolio really answers that.

And so, committing an incremental $100 million in specialty capacity will support that, as it takes a few years to build that out. But I think, Ken, the other important part of the algorithm -- and we'll, in fact, talk about this more at our Analyst Day on November 18th -- is that, when you take our balance sheet capacity, we always said from the algorithm that two-thirds would come from what I call the organic part of our story, and the other one- third would come from using our balance sheet.

And so I think Penford and some of the share repurchase, the uses of cash as an example, how we are going to be using our balance sheet capacity to be part of that algorithm. And so at Penford, when you bring it on with its profitable sales and specialty ingredients and ability to grow not only in North America, but to take that portfolio to other parts of the world, that is the piece that will also continue to support the algorithm.

Kenneth Zaslow - *BMO Capital Markets - Analyst*

Okay. And then can you talk about the North American environment? Going forward, there is still the issue in Mexico that's unresolved. Are the high fructose corn syrup negotiations being delayed? Are there thoughts that, given how low corn prices are, that you can still keep your -- manage your dollar profitability? Can you just give an outlook on how you are thinking about how the development of the high fructose corn syrup negotiations will go?

Jack Fortnum - *Ingredion Incorporated - EVP and CFO*

Ken, this is Jack. And again, we are not going to comment on contracting, but I'll give you some broad items in terms of the marketplace. As you know, there was some discussions pertaining to the different sugar parties pertaining to countervailing duties and anti-dumping duties coming from sugar coming into the US from Mexico. And our understanding is that that was resolved and announced yesterday, actually.

And I think that that resolution kind of has a nice boding, which means that we've always been in support of free trade. And effectively to a large extent, that means that the borders will remain open for all of us. And you know I think the good part about that is the fact that we have a network which goes from Canada down into Mexico, and essentially we can utilize and maximize our network very effectively with the open borders.

The other piece is, as you know, capacity utilization in the industry continues to be very strong as well. I know that there has been a different announcement in the industry pertaining to that. But we still see the industry being highly utilized as we go forward into next year.

We -- I think in the past, we've commented that the industry is running at mid-80s type of range, and I think that it will probably even tighten up as we move into next year. So I think in general, the outside mechanisms, as well as lower corn costs actually improving competitiveness with other ingredients, really does drive -- start to drive growth there.

Maybe I'll just ask if Ilene has any other comments?

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

Yes. The other thing I would add is -- and I know you're talking about the beverage environment, but if you look at the food environment in Mexico, you know the obesity taxes that we've talked about, I think that, recently, one of the customers recommended that --announced that there was about a 3% decrease in the higher calorie snacks, which is less than I think people thought.

And for us, when I talked about our double-digit growth in ingredients for -- specialty ingredients for the food industry, I think that's the other dynamic in Mexico that makes it exciting, along with, if you look at next year, the GDP forecast for 2015 is 3.5%. So I think, as what Jack said, the North America Free Trade Agreement, that whole scenario seems to be working. And then on top of that, you have the dynamics for Mexico as a country and the demand by consumers for healthy specialty ingredients and foods.

Kenneth Zaslow - *BMO Capital Markets - Analyst*

Great. I really appreciate it, thank you.

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

Thank you.

Operator

Brett Hundley, BB&T Capital Markets.

Brett Hundley - *BB&T Capital Markets - Analyst*

Jack, I have a question for you on guidance. Admittedly, just a little confused. So just allow me to push back a little bit and get your thoughts. So, you talk about North America and you talk about the weak start to this year, which is very obvious. Yet, as of your comments today where you said that Q2 and Q3 came in, in line with your internal expectations, and then your comments as of your Q2 call where you had full-year guidance at $5.40 to $5.70.

Presumably you had the ASR that's going to offset some of that Q1 weakness. Your Q2 guidance on North America was still flat to up. So, I'm just wondering if I'm missing anything. You are talking to Q1, but I'm wondering if it's more something to Q4? If I'm not mistaken, I think you guys had said that you were expecting to have a very favorable corn environment in Q4. Is that going to go away? Or is there something more here? Am I just missing something?

Jack Fortnum - *Ingredion Incorporated - EVP and CFO*

Brett, I think -- just let me kind of bring you back to what I said, just to make sure it's clear. What I said when we started the year, we were looking at the North American environment and we thought it would roll out as kind of forecasted at that point in time.

In the second quarter, what we had looked at is, is we kind of -- we thought that the margin improvement and the mix improvement may be a little bit better in North America. And some of that was being driven by Mexico, because it was growing within specialty areas. And what we found is, is that we really didn't get the improvement we thought would happen in the North American environment during -- primarily in the third quarter and a little bit into the fourth quarter that we expected.

It's still a record quarter. So it was a great quarter from our perspective. But we'd actually thought that we would be getting a little bit more out of that business. And part of the reason is, is you might say it's a mix issue in terms of product and customer, because it's really focused on the US and Canadian components.

But it's also the fact that I think, in our forecast, when we were looking at it, maybe we took too much of a progressive perspective in terms of how we looked at the prior year, in terms of the incremental costs that hit us pertaining to our corn, with respect to the drought. Because I think we maybe managed that a little bit better than we had anticipated. And we've reflected more costs coming out in our quarterly numbers because of that drought.

And so there was some tweaking to the forecast, particularly in North America, in the second and third quarter, but we -- I mean, third and fourth quarter from the second quarter look at this point in time. Does that help you?

Brett Hundley - *BB&T Capital Markets - Analyst*

No, that's very helpful. And just so I'm crystal-clear, so that's more that Q3 and early part of Q4 is more broader margin mix across North America? Or you are talking specifically more to Mexico?

Jack Fortnum - *Ingredion Incorporated - EVP and CFO*

Well, the broader margin mix is primarily with respect to Mexico but I think it's pretty broad right across the whole category in North America.

Brett Hundley - *BB&T Capital Markets - Analyst*

Okay, okay, that helps. And then, Ilene, I just had two questions for you. First on Penford, it's been growing well in the specialty food ingredients business. And I think some of that is due to M&A. And I'm just curious if you can give us maybe a good organic growth rate for this business or this industry going forward?

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

Well, I don't have a specific number, but obviously, when we look at acquisitions, we are looking to buy them not just for what they've done in the past, but capabilities for future growth. And so as we looked at Penford and modeled how the future may look, we look at our total Company. And so I would think that as we put the two together, it goes back to Ken's question on the five-year algorithm.

We think that we can grow in mature economies, we say 1% to 2% in emerging nations a little bit faster, more of the 2% to 3% to 4%. And so we'd be looking at the specialty ingredients of Penford, along with our current capabilities, especially in the R&D and product development area, to be put together and to continue to grow in the specialty products. And of course, we're aspiring for specialty products to grow twice kind of the baseline. But we haven't said specifically how that lays out by particular item or company.

Brett Hundley - *BB&T Capital Markets - Analyst*

Okay, that's helpful, though. And then just my last question is on Brazil. We watch some brewing and soft drink data in that country, and the brewing data that we watch continues to show a lot of weakness through October. It looks like October numbers are going to decline year-on-year, similar to September. And we were hoping for some overall improvement as we move into their summer.

But I'm just curious as it relates to Brazil overall. Is it more -- is it specifically a brewing sector issue for you, i.e., are you concerned about a move back toward the grid or anything like that? Or is it much broader than that? It's just general macro weakness across the Brazilian economy? Thank you.

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

Okay. Yes. No, it's definitely a general economic slowdown. The brewing side -- you've seen the same numbers we have. The first half, it was up 12%. I think the third quarter, it was recorded as minus 2%. And I think the fourth quarter, I've seen articles saying similarly, so maybe for the full-year, it will be up 5%.

And in fact, the high maltose corn syrup that we produce in that part of the industry continues to gain share from grits, because as we've said before, the brewers see that as a more efficient product. And I think some of the grit people have slowed down a bit in terms of their own operations.

So, the reality in Brazil is the general economy. And as we said in after the second quarter, during the World Cup, people were drinking beer but they weren't doing much food shopping. And that hasn't come back in a large way. And so I think it's just general economic weakness in a lot of different areas.

On the other hand, medium/long-term, I think that it's a very exciting place, and consumers are starting to eat yogurts and healthy foods. The employment rate is pretty good. And so I think, long-term, we believe in Brazil. And that's why we've put in the appropriate capacity over time. But I think generally right now, we have to accept the fact that the economy is a little slow and we'll push on our places where we have a competitive advantage.

Brett Hundley - *BB&T Capital Markets - Analyst*

Thanks, Ilene.

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

You're welcome.

Operator

Akshay Jagdale, KeyBanc.

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

So my question is regarding your specialty business. So you announced this $100 million CapEx spend. It's been really hard to judge, in a way, your CapEx spending, because the volume growth tends to be choppy; sales growth, obviously, is driven by the pricing relative to corn, et cetera.

So with specialty, it's going to be even harder for us to judge your CapEx spending and how the returns are trending, because you don't report it separately. So, can you -- in light of that, I mean, can you help us understand how -- what's a good way to judge your returns on these spending? And how are you going to help us with that? Is there a thought to maybe start reporting a business unit that's specialty?

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

Well, this is Ilene. I'll start out and then I'll turn it to Jack on some of the parts of the reporting question. I think when you think about our specialty growth, again, we are driven very much by these consumer trends, people wanting to eat healthy, lower calorie, but yet they want taste.

And so we've talked about the growth in Europe. And, in fact, on the capital side, we had talked about our capital investments in Europe, and you can see the returns that are coming in Europe based on those investments that we talked about over the last couple of years. So now we come out and say, look, we are going to spend some more of our $300 million capital, and we are going to commit it, over the next couple of years, to a couple of other regions where we see the same trends.

And we talk about Asia. And, of course, we talk about the tapioca base there, which has a texture rising, which is non -- which is gluten-free, so it's a little different than it is in some other areas. And we talk about an investment in specialty in the North America region, which again answers the consumer trends of wanting gluten-free and healthy and non-GMO.

So, all of those investments are supporting these growing consumer trends. So I think that you can look at some of the data that we've developed by the overall region. In other words, talking about Europe as mainly a specialty region, and take that and translate it to where you lay out how you see our business.

But at this point, we run our business by region. And that's where the money is made. And every region has a different makeup. And it's very important that the ingredients we deliver are adjusted to -- for that region for what the consumers want and need. And therefore, the algorithm -- to use an earlier word -- is a little different by region, depending on what the consumer trends are and the makeup there.

And therefore, we have not gone to the point by saying a one specialty BU around the world, because that's not really a truism. It's different by region.

So, now I'll turn it to Jack.

Jack Fortnum - *Ingredion Incorporated - EVP and CFO*

No -- and really, I think you hit it very well in terms of stating the fact that we manage our business by region. There is different trends in each region. And effectively, while there is different pieces that we can look at -- but even some of the facilities that we operate produce those specialties as well as core ingredients, and so it's very difficult to look at the true GPs from that vantage point.

And so I think we'll give you probably some indication of some of the growth trends we are seeing in our specialties. And our aspiration is, from a revenue perspective, in terms of how we're going to grow that specialty business, because it's a very important piece of our algorithm. But we are not going to break it out from a P&L perspective, because that's not how we manage our business.

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

That's fair. And then just on Penford, can you help us understand longer-term what that could add to the earnings stream? Or just give us some sense, maybe a little bit more detail on the synergy number that is included in your guidance? And you talked briefly about some additional operational efficiencies. It seems to me, generally speaking, that there's cornstarch business, if I may, that's not specialty, should have meaningful upside in terms of margins when it's rolled into your network.

And then on the specialty side, it's complementary to your portfolio and should be high-growth area. Is that the right way to think about it? And can you help us at all understand maybe what the financial impact would be longer-term?

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

Well, again, this is Ilene. And we've announced the acquisition and we're obviously going through closing. So I can only speak in generalities right now, and because we're not digging into the data until we are closed. But from -- our excitement is really about the portfolio of products that Penford has in a number of different areas. And we talked about the food area and the trends that are focused on gluten-free and non-GMO, and the food textures.

And then on the industrial side, there are quite a few applications that are very exciting in bio-based adhesives and liquid natural polymers and bioplastics, and those areas that actually Ingredion has worked on. So we believe that the two of us together are going to find and drive value for our customers.

So, I think in terms of numbers, I mean, we said that we see at least $20 million in synergies. I always like to beat those numbers. But at this point, we've laid out how it will be accretive in year-one to $0.10 to $0.15. And then, of course, in year-two, we would get -- and that included about half the synergies, so year-two would be another $0.10 from those synergies. Of course one expects to continue to have it part of our algorithm going forward beyond year-two. I don't call it a synergy if it's after year-two, because that makes it further out, and I like to get those in the first two years.

But again, I think that the companies together, when you think about those synergies, we talked about, as I said, the public company costs and some of the G&A. But I think that the supply chain optimization, in terms of how we serve customers better, and having specs out of the right facilities, and having a whole new equation is very exciting and a way to create value. And then at the same time, the product development side, when you bring two great companies together, you have the opportunity to look at creating solutions for customers. And that's the longer-term. That's beyond the $20 million.

That's -- you know people talk about revenue synergies, which I think are -- we don't state exactly what we think they'll be, but that could be beyond the two years. But yet our $20 million was definitely costs synergies. So it's the revenue synergy piece of having two great R&D companies come together and develop products for customers. So I think, that should give you enough facts for you to model as you put it all together, and we become one company as soon as we can.

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

That's helpful. And one last one just on North America. I think there were some questions that were asked but I'm just asking in a different way. So, North America, you are going to end up being down slightly in operating income. While corn costs were down significantly and utilization rates were pretty good, I understand there were some issues in Mexico that won't persist next year.

But can you just walk us through sort of what are the puts and takes next year to get North America to operating income to grow sort of in line with your algorithm? Because obviously that's important for the organic part of your business. So, what is -- what are some of the positive -- or what are the tailwinds and what are the headwinds next year as you look at them?

Jack Fortnum - *Ingredion Incorporated - EVP and CFO*

Well, Akshay, I think we probably should defer this conversation until we are actually ready to give guidance for next year, because we have a long way to go in terms of our contracting and a number of different variables that are entering into the accounts. But from a macro perspective, you know I do think there's a few good things. And Mexico continues to grow. And in the US and Canada, our specialty portfolio is still very positive on a growth trajectory.

And then, you complement that with our Penford acquisition, and I actually think that you'll see some significant growth in North America next year. But you know, it's still too early to really comment on any financials or anything like that, at this point in time.

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

Okay, perfect. That's excellent. Thank you.

Operator

Farha Aslam, Stephens.

Farha Aslam - *Stephens Inc. - Analyst*

Again, my question is going to be around North America and Mexico. You did have that agreement signed between the Mexican sugar industry and the US Trade Commission. And essentially, it keeps more sugar in Mexico and prevents it from coming into the US. Do you believe -- and that will artificially depress prices of sugar in Mexico.

Are you concerned that that agreement will therefore cause an incremental pressure on your high fructose corn syrup use in Mexico? Or do you think you can maintain or possibly even grow that high fructose in Mexico for next year?

Jack Fortnum - *Ingredion Incorporated - EVP and CFO*

All right, let me answer that question. I would say that, obviously, our first component is that I think the agreement -- we are very happy with the agreement, because it's really supportive of our free trade perspective where we have a NAFTA environment as much as possible. You mentioned there are some restrictions, I'm sure, coming into the US.

I think that if you go back to what originated some of the issues surrounding the sugar coming into the US was predicated on the fact that there was a bumper sugar crop in Mexico that had to move out of Mexico. Now that they've got a more normalized crop in that 6 million ton type of range, I don't think that there's going to be the same type of issues surrounding the trade. And I think that's one of the reasons why the two sugar industries could get together and come to an agreement as well. Because I do think that was an anomaly that caused some of the distortions.

But coming back to HFCS in Mexico, I think that the outlook is kind of neutral from my vantage point. We have the obesity taxes on there. There's always going to be competition. But with lower corn costs, we are competitive with sugar no matter where we are at this point in time.

And so, I think -- the agreement itself I think is positive, because it takes away any uncertainty in terms of people, how they are thinking about booking business or anything like that, and keeps the free trade basically in place between the US and Mexico. Even though there is a little bit of constraints in the volume coming up from Mexico, I think it's relatively uneventful from our perspective.

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

The other thing I would add is that we have a great footprint when you look at the NAFTA countries. And having three local facilities in Mexico, as well as our US and Canada footprint, has really given us the ability to optimize how we deliver to customers and create value in the supply chain. And so, I think, along with what Jack said, it positions us well to deliver more value to customers, including the specialty growth.

Farha Aslam - *Stephens Inc. - Analyst*

Right. And then a bigger picture question, regarding your balance sheet. I mean, clearly, you've just announced Penford, but your balance sheet is still very, very strong, even after Penford, with significant kind of dry powder. Post-Penford, could you share with us your desire to do incremental acquisitions? And then your kind of priorities on share buybacks versus dividends? Kind of your capital allocations thoughts.

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

Okay. You know, always happy to answer that question. You know, we were very happy that we were able to announce our intent with Penford. And we still have our pipeline that we've been working. And as I've talked about over the past six months, with our strong balance sheet, we continue to use the strategic blueprint to guide us.

And so, we continue -- we are excited with our strong balance sheet because we see opportunities both geographically -- I talked about Asia, some of the opportunities there -- as well as broadening our portfolio. And I think Penford is just the first step in these bolt-on acquisitions that we intend to pursue -- again, being very disciplined on creating value for shareholders, to finding the right price value creation equation.

And with Penford, we feel that we've made a good decision. And with the other ones that we are looking at down the pike, where -- they're still in the pipeline, so we don't need a whole new pipeline. We just need to continue to work it, meeting with people and looking at those value equations, and pursuing how we broaden the portfolio from both a texturizer point of view to, again, other healthy ingredients that will help us formulate and deliver value to our customers.

So, going to your question about the uses of cash, we've been very strategic in the past 90 days. Because I've always said, with a strategic blueprint, we want to, number one, fund our organic growth where we have strength and capabilities. And so we continue to do that. And the capital side, occasionally we'll call out some kind of specialty investment, which is what we did back in September. But we also feel that we want to look at opportunities to create and deliver value to shareholders with shareholder-friendly actions.

So we right-sized the dividend, remember last year? So, we felt very committed to that dividend level and our payout. And then the share buyback, where we said we always want to buy back dilution. And we are committed to that. And then, of course, if there are opportunities to do more where we're not finding the right acquisition proposition and creating value, we do share buybacks, and at the same time acquisitions.

So I like all three levers -- maybe there is a fourth level, if you call dividend the fourth lever and organic growth part of the fourth lever. I think we want to use all those levers simultaneously to deliver value.

I know, Jack, you support that allocation.

Jack Fortnum - *Ingredion Incorporated - EVP and CFO*

Yes, very much, actually.

Farha Aslam - *Stephens Inc. - Analyst*

Great. Thanks for the added color.

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

Welcome.

Operator

David Driscoll, Citi.

Cornell Burnette - *Citigroup - Analyst*

This is Cornell Burnette with a few corrections for David. (multiple speakers) Jack, I just was hoping you could talk a little bit more about -- how does Ingredion -- you know, what's the path of growth maybe over the next couple of quarters in South America?

I know that the Andean region is doing good, but still, Brazil and Argentina are about 75% of sales there. And it appears that economists continue to lower their GDP forecast in both countries. I believe the Brazilian real has weakened about 10% relative to the dollar since September. And in Argentina, farmers continue to hold onto crops pretty tightly.

So kind of how do you manage through that? And what gives you confidence that maybe you can start to turn things positive in those markets over the next couple of quarters?

Jack Fortnum - *Ingredion Incorporated - EVP and CFO*

Yes, Cornell, let me start with Argentina, because our premise really hasn't changed that dramatically there. The only thing that's changed is that we are probably further along in this -- what I would call a long-and-gated process there, where we are waiting for further devaluations to take place.

And even in our guidance, we are still factoring in a potential devaluation, it doesn't have very much impact on the translation, because it's a short period of time between now and the end of the year. But if you think about Argentina, you're right -- they're holding onto the corn. And what we've been trying to do is just manage that more effectively. And people become more used to inflation and how prices will pass through, and our volumes are starting to, I would say, stabilize, I would call it. Because people still eat and drink in Argentina despite a challenging environment.

And so I would say that our situation in Argentina hasn't really changed, and it won't until there's more dramatic impact on it, other than the fact that we are probably managing through it a little bit more diligently, I'll call it. And that's just because the economy itself is becoming more used to the conditions down there.

When you go over to Brazil, that's still one of those ones where the -- I actually attribute some of it back down to just the general commodity prices coming down, and it slowed down some of the inputs of cash coming into Brazil, it slowed down the economy. And so now they're -- I think they are getting to the point where they are saying, okay, how do we move forward? They just had their elections and so you have a new President --

well, not a new President; it's the same President in power. But effectively, they'll be setting their agenda to get growth moving through that economy as well.

And if you think the fundamentals of Brazil, I've always been very positive on Brazil from a country perspective. I actually think it has great opportunities. And we've gone through these slowdowns in the past in Brazil and they've always come back, sometimes slower than other times. But you know I do think that over a period of time, as the distribution of wealth, particularly in the Northeast in Brazil, continues to improve, we will see continued growth in Brazil.

We pre-invested a little bit a few years back in terms of making sure that we have the capacity is not filling out quite as quickly as we would like it to, but effectively, we are positioned very well for the future growth in Brazil as well. And so that's one of the opportunities as we move forward. You know it is taking longer than we anticipated. That's all because the economies are a little bit slower.

Ilene, do you have any other color on those (multiple speakers) that you wanted to --?

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

Well, and I think that as I said -- what I call medium and longer-term, the desire in the Brazilian population for healthy products, when you look at some of the dairy trends there, there should be opportunities for our specialty ingredients. And we take solutions from one region and then we make adjustments for, let's say, a Brazilian taste and desires. And so that's the other part of the opportunity that we see in Brazil with our modified starches and capabilities.

So I think that we are starting to see some of those trends. It's a small piece but it is growing.

Cornell Burnette - *Citigroup - Analyst*

Okay, great. And in North America, Jack, can you just talk about maybe where utilization rates for corn wet milling are currently versus maybe this time last year? I know that shipments of US fructose to Mexico are down about 11% year-to-date through August, so that appears to be a headwind. But are there things that are -- offset -- that may be offsetting that? And so are we kind of flat up or down versus last year?

Jack Fortnum - *Ingredion Incorporated - EVP and CFO*

As you go into the -- obviously, the resolution of the sugar ratio helps in terms of shipments down to Mexico. But even -- we looked at the utilization rates and they are in the mid-80s. That's what we've commented in the past. And you've probably seen some announcements in the industry where some capacity has been closed and things. And so it's really pushing up the utilization rates a little bit.

And so, that's why I think this year is one of those years where the industry will be running fairly tight in terms of capacity, not particularly on a seasonal basis. And so I would say that it's all very positive from that vantage point.

Cornell Burnette - *Citigroup - Analyst*

And then lastly, with the new guidance range being narrowed, it's still a pretty wide spread, I guess, $0.15 given that we just have one quarter left in the year. So I just was wondering kind of what are some of the key variables that you would look for, relative to coming out towards the bottom end of that range or the top end, as we think about some of the things that occur in the fourth quarter? Thank you

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Jack Fortnum - *Ingredion Incorporated - EVP and CFO*

Yes, you know the bottom end, we've always stated that the bottom end always incorporates the devaluation in Argentina because of the fact that we are always sensitive to that. The magnitude of that impact would be much smaller now because, essentially, what would end up happening is, is the -- you know, you've only got the translation over the last couple of months that would transpire.

The upper ends would really be dictated by sharp volume growth, for example. As you go through, the fourth quarter is always a challenging one in North America because of the fact that you've got corn prices changing, people contracting into next year. Your volumes can either pick up or slow down. And so, essentially. I'd say the volume growth -- unexpected volume growth or slowdowns will impact the range.

And that's true around the world. So I pointed out North America, but it's basically around the world and it's really volume-driven. In terms of the cost components and things, you know, obviously, there's a few items that could impact us pluses and minuses that we are trying to factor in. Now, obviously, some of the -- and I hate to talk about co-products because most of them just pass through, but there is some falloff in those with corn, because corn prices have come down in the current year.

And so you try to model all those different components into your forecast. And it doesn't take that much of a movement in any of those different variables to really be there. But I would say that the upper end really is on volume and mix is the -- where we'd have to get very strong volumes and very positive mix components to take us up to our upper end. And it'd probably be Argentina or a very sluggish volume that came through in the fourth quarter.

Cornell Burnette - *Citigroup - Analyst*

Very good. Thank you.

Operator

That concludes the Q&A session. I'll turn it back to the presenters for any closing comments.

Ilene Gordon - *Ingredion Incorporated - Chairman, President, and CEO*

Good. Well, thank you. And I know we are short on time, but before we sign off, I'll reiterate our confidence in our long-term outlook and our business model. We remain sharply focused on shareholder value-creation, and we are committed to deliver it, as we have in the past. So, that brings our third-quarter 2014 earnings call to a close. And we'd like to thank you again for your time today. Thank you.

Operator

Ladies and gentlemen, that does conclude your conference. Thank you for your participation. You may now disconnect.
