Ingredion
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Benjamin Theurer: Welcome back. Next on stage we've got Ingredion, leading global ingredient solutions provider which sells plant-based ingredients into a wide range of foods and beverages to personal care, pharmaceuticals and papermaking applications. Besides its core ingredients platform, which includes glucose syrup for confectionary and sweeteners for beverages, Ingredion is focused on growing its specialty ingredients platform which consists of starch-based texturizes, clean and simple ingredients, plant-based proteins, specialty sweeteners and ingredients to enable sugar reduction.

The company aims to showcase purpose-driven and sustainable sourcing as it brings together the potential people, nature and technology all for a common goal; to make life better. We're excited to have Jim Zallie, Ingredion's President and CEO as well as Jim Gray, Executive Vice President and CFO joining us for today's session. Jim Zallie joined Ingredion in 2010, was appointed CEO eight years later. He previously served as Executive Vice President of Global Specialties and President of the America's. Following a 12-year tenor with PepsiCo, Jim Gray teamed up with Ingredion back in 2014 and formally served as Vice President of Corporate Finance and as Chief Financial Officer in North America.

Jim will give a quick 10-minute overview of the current environment and will then take it deeper into Q&A. Thank you very much. Jim?

Jim Zallie: I want to thank everybody for coming this afternoon and for your interest in Ingredion. I'm going to just go through about 10, 12 slides to give a brief introduction for those of you that may not be intimately familiar with the company and then we'll do the fireside chat. So, what I'm going to say will be protected by our forward-looking statements and Safe Harbor provisions. Last week, Jim Gray and I were in New York City and we had the honor, which we've done a couple of times, and that it is to ring the opening bell at the New York Stock Exchange and we were reminded by the New York Stock Exchange that we are, believe it or not, the 13th oldest company through derivations of the origins of the company listed on the New York Stock Exchange.

So, from that standpoint, we are a long-standing, long-serving ingredient supplier to the food industry with a reputation that it's pretty established around the world as a high-quality ingredient supplier to the food industry to the food industry.

We have 12,000 employees. We have 18,000 customers, two locations around the world. One of the things we pride ourselves on is controlling the supply chain so that we can certify the origins of our products from a standpoint of whether or not they are sustainably sourced, whether they are organic, whether they are non-GM, etc. So, we have a goal which we are on target to meet to have 100% of our Tier 1 crop sustainable resource by 2025. And a breadth of ingredients that we supply, where we have transformed our portfolio to be at much more relevant ingredient supplier to the food industry. 70% of the new product launches globally that were launched in the food industry contain the kind of ingredients, the categories of ingredients that Ingredion supplies.

So, from a standpoint, again, of the relevance of us to be a valued supplier to the customer base, we're very, very relevant. We operate 32, what we call Idea Labs, which are co-creation centers where we engage with customers around the world locally. Food is a very local business, and we are a technology-based company with 502 technologists, R&D scientists.

We finished last year with approximately $8 billion in sales, 54% into food, 16% in beverages and growing. So, in total, food and bev, 70% of our sales are into food and bev. 19% goes to a combination of papermaking, packaging for corrugated board. Also, into the pharma space, we made two acquisitions in the pharma space for pharmaceutical grade recipients at the end of last year, but we had an established partner business prior to that, but see that as a growth factor for higher margin growth as well as sales of texturizers for skin and haircare for clean beauty as well. And we sell, obviously, agriproducts, co-products that go into animal nutrition as well.

And the most recent quarterly results or a set of results that we released have our (inaudible) for the full year projected to grow at mid-single digits, $8.3 billion to $8.6 billion and our adjusted EPS, we took up our full year guidance to a range of $8.80 to $9.40, which we project out to approximately a 22% increase year-on-year on adjusted earnings per share. And quarter two was the second strongest quarter or was the strongest second quarter in the company's history where we delivered 4% increase in constant currency in net sales.

Our operating income increased 17%, and we delivered a 9% increase in adjusted earnings per share. And we did also increase for the ninth consecutive year, our dividend or raised our dividend 10%. And when you think about Ingredion and if you think about the company that we are today in comparison to the company we were, say, 5 or 6 months ago, and I'm going to show you a slide on the investments that we made to transform our portfolio, think of us as a leader in texturizing of foods with really a tremendously deep understanding of how our ingredients impact texture for taste; the whole eating experience.

Also, we are a very respectable player in plant-based proteins with a range of concentrates, protein-based flours as well as isolates, the highest protein content ingredients for a range of protein fortification and for texturizing of foods for dairy alternatives as well as snacks and as well as sports nutrition products, for example. And we are a leader in high-intensity natural sweeteners to reduce sugar and in part mouthfeel which is typically lost when you replace sugar.

And again, we work with customers to co-create, to bring ideas to them, to bring concepts to them and really partner on how we can influence their front-of-pack claims to deliver consumer-preferred innovation on behalf of our customers. And we do that by working at our Idea Labs, which are positioned in many countries around the world. For a company of our size, we're very international with pretty sizable positions in Asia Pacific, which is about a $1 billion business, in EMEA, about $1 billion business. North of $1 billion business in South America. Mexico is a very -- we have a very respectable and large position there as well.

So, we're not really reliant on the United States because we have a market leadership position in many segments in the United States, especially large-based texturizers. Our specialties platforms, we had four leading platforms and then a fifth growth platform, which is combining the ingredients in these four into something called food systems, which is formulating more complete solutions for customers to deliver clean label enabled systems, sugar reduction solutions, ingredients like that where it’s all based on what we consider to be enduring sustainable megatrends and starch-based texturizers driven by affordability and convenience, clean simple ingredients, which is about, again, labeling transparency, the authenticity where a product has been supplied from. Plant-based protein certainly is driven by such things as mindful consumption as well as health and wellness, the sugar reduction certainly driven by the avoidance of disease prevention as it relates to obesity, diabetes, etc.

And those market segments in which we play are large and growing segments. So we do have headroom for growth when it comes to the texturizers market, which is an $18 billion market and where we believe there's an opportunity for us to continue to innovate, continue to differentiate and deliver texture for taste as an opportunity for food companies to differentiate their offerings with unique taste profiles that are based on interest in textual experiences that a consumer could enjoy.

And sugar reduction is a large and growing market. It's being driven by regulations. It's driven by government positions towards labeling, towards taxes and just the overarching interest in avoiding sugar in the diet as well as concerns over high-intensity artificial sweeteners. And we've seen some of the news around those only in the last few months, and that bodes well for our position with high-intensity natural sweeteners where we're the largest supplier of Stevia, for example.

And certainly, the plant-based protein segment, it's going through a little bit of an adjustment right now. Our long-term projections are still positive, but still an already established market that we see an opportunity over the long term to continue to grow and penetrate. Our position, our heritage as a company has been a leader in providing starch-based texturizers based on eight different varieties of corn. We're the leading producer of tapioca in the world. We're a very large player when it comes to potato starch as well as rice starch.

And we really have an unmatched knowledge of how to modify those products, physically, chemically, enzymatically to import unique functionality to foods and to other nonfood applications for functionality, whether it be imparting a unique mouthfeel, stabilization, shelf life stability or emulsification. And these trends that you're seeing highlighted here were some of the drivers that caused us to decide to double down and invest and reinsure -- to ensure that our leadership position in starch-based texturizers endure for long term because what the pandemic exposed is obviously challenges to supply chains.

So, we have localized over the last few with more of our supply chains through investment in China, in Thailand, in Mexico, in the United States, in Europe, and we've expanded our capacities. And one of the reasons why this is so strategically important to have supply is because customers increasingly want to know what is the environmental footprint of the product that you're supplying to me and making sure that it is being produced in a sustainable way from regenerative agricultural practices, sustainable sourcing, but also in how far the product has had to ship to get to them on a local delivered cost basis.

So, this has been a significant part of our investments and as well as with high-intensity artificial sweeteners, we made an acquisition in 2020 which was the PureCircle business, which was the leader in high-intensity natural stevia-based products. We've supplemented that with physicians in what we call bioconverted Reb M, which is the best tasting It's called a glycoside of the stevia molecule as well as producing that same molecule for fermentation.

So, we're the only company that has what we call perfectly sweet trifecta of those three products, which really are in high demand right now, given the concerns over some of the high intensity artificial sweeteners. And because of our global network and infrastructure, we've been able to increase the customer base of the PureCircle business since we acquired it by 185 customers. And we are commissioning a significant expansion in bioconverted Reb M to meet market demand in Quarter 3 at our facility in Kuala Lumpur. But it's a very large market industry growing at 6%.

Over the last six years, we have invested $850 million in growth capital. And the important takeaway from that is that only 60% of that has begun generating returns in the last one to two years. And an example would be $100 million of investment in China. China is the largest modified food starch market in the world. We are a very significant, the largest specialty modified food starch supplier in China. We've just commissioned that facility at the end of last year. So, the returns on that are just starting.

Plant-based proteins, we made significant investment. We don't even have the returns on that yet. That's a tremendous opportunity for us to get leverage. It's a challenged market segment right now. But nonetheless, the opportunity for an increase there. So that's the key there. And we have a very active M&A pipeline. As you can see, we've been very successful over the years, bolting on different businesses to expand our capabilities in any of those growth platforms.

And lastly, we have a very disciplined approach to capital allocation that I'm sure Ben is going to ask us about. We did raise our dividend 10% this past quarter and target to have a dividend payout ratio of about 30% to 40% of our adjusted earnings per share, and we'll talk more about that, but that's a little bit of an introduction, and let's --

Benjamin Theurer: -- take a seat and thanks for already answering Question Number 10. That makes it easier. A lot to unpack here. But maybe let's start off and go a little first short, medium, then long term. You've highlighted, obviously, in your presentation, the strength of growth on the top line, but even more so on the profit side. And interestingly enough, we saw a lot of still positive momentum in pricing. But at the same time, volume has gotten a little under pressure.

So maybe help us understand what the current drivers are? And what's the underlying issue on the volume side and how you think you're going to be able to overcome that as it goes forward into the second half or maybe even into 2024?

Jim Zallie: Okay. I'll start, and I'll turn it over to Jim afterwards. I think that one of the things that we, I believe, have done extremely well, and it was born out of the necessities that the pandemic brought upon the industry at large in relationship to the pressures on the supply chain is that we did a very good job of standing up actually before the pandemic, what we call our pricing centers of excellence. And they really serve us well as we navigated through a 40-year high inflation. But those supply chain disruptions also forced us to look critically at our customer and product-related segmentation.

And given constrained supply, we looked critically at how to prioritize our customers and how to optimize our product mix. And so, we did that collectively as an organization with our commercial organization, with our global operating model, with our global operations, I believe, extremely well. And that's allowed us to optimize price. And as we've demonstrated this past quarter, expand margins for four consecutive quarters.

What has occurred just in the last, I would say, three quarters, that the entire industry is enduring and also scratching their head a bit to try to figure out. But some of this, I believe, is common sensical to understand is the volume impacts. And so, what we said on the earnings call, and we genuinely believe is true, is that customers went from a just in case mentality from a standpoint of their ordering to most recently, the last couple of quarters as interest rates have increased, the cost of carrying inventory has increased to a just in time mentality towards their approach to inventory.

So, we're seeing, we believe, a long tail of inventory rebalancing and destocking that's taking place. And in addition, I think consumers are behaving very rationally to try to economize, given what they've endured in relationship to inflation. So that we all believe is working its way through the system. We believe it's going to be steadily increasing, although we believe that recovery will be somewhat bumpy, but we believe our ingredients be indispensable, ingredients to find their way into so many formulations. And again, I draw you back to that figure that I highlighted on the second slide, which is that the kind of ingredients we supply are in 70% of the new product introductions that are food products that are introduced.

So, we believe that when the volumes pick up that our volumes will obviously increase and pick up because they're also very valuable from an affordable formulating standpoint as well.

Benjamin Theurer: Anything to add?

James Gray: No. I mean I just characterized that when you look at consumers and economies where they're used to high digit -- high single digit, low double-digit inflation, they've seen wage increases, they keep pace with that, you're not seeing as much of a kind of a destocking impact or anything of where a consumer is going from really how are they emptying out their pantry to what Jim really highlighted, which was a sensitivity to extremely rapid food price increases.

So, you go to a developed country like the United States and what we see, and we all try and study in our IRI data, our Nielsen data or you go to Korea, or you go to Western

Europe and traditionally very low inflationary environments and low wage increases. And so, you have this shock of food price increases. You've had it two years in a row now, and you see your packaged food companies keeping pace because they have to take price because price is the most important lever and the consumer is a bit standing back and thinking like, my gosh, look how much it cost me for an animal protein or look at how much it cost me in the center store solution?

And I think that as you realize that wages will eventually catch up, you're going to see a bit more normalization and a return back to what we would call a normal grocery basket, but it just takes time.

Benjamin Theurer: Great. Now if we compare and contrast, health and wellness has been the segment very solid on the growth side and actually also from a volume perspective. So quite the opposite of some of the things we've talked about. What should we expect from the health and wellness exposed products forward? And are there any opportunities how you can accelerate growth?

Jim Zallie: So, I think it depends on the categories. But overwhelmingly, I think, long-term enduring trend in our industry, ingredients and food products that are positioned as healthier offerings are going to continue to be supported by consumers' interest in living more healthy vital lives and avoiding health care costs and all of that. So, I think that is something that we expect to continue to see. That's why you can expect us to continue to invest significantly and expand our capabilities and offerings in sugar reduction, for example.

The other thing is that you may not realize that we do sell ingredients that are used for -- that are sold for use for digestive health, for example, oligosaccharides is a prebiotic, galacto-oligosaccharides is a prebiotic-resistant starches that function literally as a fiber in products. So, we have those ingredients as well. The other thing is that our starch-based franchise enables what we call free from formulating. So, gluten-free, for example. So, tapioca starch, potato starch, rice starch, are all used in gluten-free type offerings, certainly, sugar-free, fat-free, reduced fat.

So free from type offerings, we have a significant presence in. So that's how we're looking to continue to play in, say, healthier offerings, which we which we believe long term will be a great opportunity for us.

Benjamin Theurer: On sugar reduction, can you give us like an example of like what the replacement factors are and what types of sugar you replace and how you actually work with your customers to maybe the sugar content down. We were joking about the potato chips here, but less [fat] in that case. But what are like the steps? How do you need to (inaudible) to ultimate product with your customers to help them reduce sugar?

Jim Zallie: So, it's a great question and try to indicate this as quickly as I can. But on the last earnings call that we had, we talked about the capability that we have developed, which is called our ATLAS Simulation conjoint analysis work that we do with customers, which is basically working with the customer to profile a product and how that product would best resonate with a consumer based on its labeling, based on its front-of-pack claim, based on its label declaration, based on its positioning. And we have access to a proprietary database of consumer insights that we share with customers and then co-create concepts and prototypes.

So very recently, to answer your question specifically as it relates to the kind of offerings we have in our sugar reduction portfolio, we replaced 100% of the sugar in a functional beverage that's used for gut health that would be marketed as completely sugar-free. And that's with one of our high-intensity best tasting stevia products. In addition, we've formulated what was positioned as a light or reduced sugar orange juice that we contain allulose, which is another product that we have in our portfolio for sugar reduction. It is called a rare sugar. It has 70% of sweetness of sucrose, but about 0.4 calories per gram, so 10% of what a typical carbohydrate would have, and that's been used in that orange juice product.

And then we have other sweetener offerings that are labeled as a flavoring ingredient. And so that, we have formulated most recently into another product that we had a 50% reduction in sugar, but it would not have stevia on the label, but would have a natural flavoring declaration. So, it gives you three different examples and three different types of beverages where we work in a very nuanced way with customers to position our products.

James Gray: And just to interject it, while you're going to hear that we're always focused on the functionality, we're also focused on the economics and use. And so, with stevia, it's about 280 times sweeter than sugar. And so, then when you look at, oh, am I going to use a kilogram of stevia, I'm going to use 280 kilograms of sugar to get to the sweetness profile that I want, and we look at the economics and the cost of that and so with sugar prices elevated, our goal of being able to offer a stevia solution that's at equal or lower economics and used in regular sugar, we start to bump against that threshold, particularly in markets like the U.S. where you have a relatively expensive domestic sugar market.

And so, then that's -- then you take an industry where we characterize about $5 billion in terms of revenue demand, and you're going up against a $90 billion market for sugar globally, right? And so sometimes that functionality really, really starts to work, not just in terms of what our mouth and what we taste, but also in terms of the P&L for our customers.

Benjamin Theurer: Okay. Just coming back, you also mentioned during the presentation a little softer environment in plant-based, but still very positive on the medium to long term. So maybe help us understand how you would frame what are the issues in the shorter term? And why you believe the medium-term outlook is still unchanged and favorable?

Jim Zallie: Yes. I think when it comes to the plant-based market opportunity or the market itself, the first thing I think everybody should realize is that it is an already very significant, well-established category plant-based products. When you think about how long soy products have been around and soy protein has been around is a very well-established category first and foremost.

It was a category that saw very, very rapid growth, but has been probably impacted more so than other categories by inflationary input cost increases as a category unto itself, and that has caused those products price points to be increased versus say the alternatives that were dairy-based products and/or, say, meat-based products, animal-based products.

And so, consumers have voted with their wallets. And this past quarter was a tough quarter for the entire segment, where I believe the numbers are dairy alternative and meat alternative volumes were down 10% and 18%, respectively, for the category in the quarter year-on-year. So, what that's providing, is it providing an opportunity for us and our customers to work that much more closely to understand what's needed to drive consumer preference and adoption because I believe it's pretty widely accepted that consumers would like the alternatives from a standpoint of the sustainability element, the health and wellness perceived benefits.

However, there are some things that need to be overcome when it comes to the perception of the labeling being clean label or whether it's not clean label, that affords us an opportunity because one of our growth platforms is clean label formulating. So, we're working to innovate the next generation of plant-based proteins that would be lower in salt, higher in solubility, delivering the right texture and/or say clarity in a beverage. So that's where our focus is. So, we see some opportunities for protein fortification in snacks, sports nutrition.

We think the dairy alternative category is going to be a significant opportunity long term. In the near term, the category is going to remain probably under pressure for another quarter or two. But long term, this is a category that we believe in and that we want to continue to play in. And it opens up doors for innovation for our self-based texturizers. I can't tell you the number of product that we're working on for customers that want to innovate and develop and launch a plant-based offering and also need a starch-based product in there. So, all of this kind of works synergistically for us and our portfolio.

Benjamin Theurer: Perfect. Just another question just around like the commodity volatility. And obviously, you're exposed to that to a degree, but you've done very well more recently just because of expanding the hedge program. So maybe a question for you, Jim, just talk us through what you've changed and how that helps your business as it relates to the stability in the short, medium term versus what might be in the past would have been a little more exposed to volatility in the commodity markets and where you actually expect commodity markets to go?

James Gray: Yes. I mean I think that when we look at our business in terms of mother nature provides an ag input and then we do an arbitrage on that to create a molecule to create an ingredient solution, and there's quite a bit of value-add in between. So, what we need to be able to do is say, okay, in which of our markets, what's the variability of that ag input? And first and foremost, can we price through our contracting to our customers to pass that risk through?

And to the extent that we can't pass that risk through and the customer says, no, we really want that, you to absorb that risk for us. Then how can we either time the purchase of our ag inputs and do that in shorter cycles so we're less exposed or in markets where our customers want a commitment that may be as much as a year, maybe it's even longer, we really have expanded our hedging practices both on both the heads of the corn as well as some of the coproducts and the timing in between with the desire really just to get to a nice portrayal of the profit stream that we think we earn off that business.

And that's the whole idea just to be able to say for our product lines that tend to be a bit more core that we just really earn a nice steady profit stream off of those so that you can focus on the investment and the growth markets that Jim's highlighting and then what we call our specialty ingredients portfolio.

Benjamin Theurer: Okay. Perfect. So, in summary, if we balance short-term headwinds, but also some of the tailwinds, you presented some long-term targets not so long ago, and I think you updated them to a degree in CAGNY just about six months ago. How comfortable are you with those medium-term targets? And where do you see opportunities to maybe in the short term leverage what is a very strong cash flow generation? It's kind of a capital allocation question.

Jim Zallie: Yes, I'll make some quick comments and Jim can make some comments. I think that I would remind everybody that we increased our dividend by 10%, which means we do have confidence in our future cash flows going forward. I think in the near term, we're all watching volumes very closely. But again, we think we have a very pragmatic view towards how volumes will develop going forward. That's how we bake into our guidance. And we see, again, opportunities to continue to drive specialties growth, specifically in those segments around clean and simple labeling, better -- enduring consumer trends, sugar reduction, affordability and convenience, etc.

So, I think the prospects for our business, the company, given our market position and our diversification globally and our diversification across the customer base, given how long we've been an established player in the industry, really bode well for us. We're not just selling high-end niche products, but we are very relevant to customers across a broad spectrum that affords us an opportunity to have a dialogue with customers to solve their needs in many, many ways. Jim, do you want to wrap it up?

James Gray: Yes. I mean we always put out a four-year outlook. And within that outlook, just to clarify, so we don't know what the price of corn or tapioca is going to be Year 2, Year 3 out, right? And so, we assume a constant cost of our ag input. We assume constant pricing and we assume constant FX. And yet, against that four-year outlook, we think, on average, we're going to grow adjusted operating income between 7% and 9%. We're going to use our cash flow to purchase back shares and pay a dividend or we're going to target a TSR that's going to be in the 12%, 13%, 14% range for our shares.

We're coming off of two years of tremendous price and revenue growth, given the underlying commodity input. But the mix of the business towards specialty towards higher value per ton products in our portfolio continues to grow. And that is geometric in terms of its impact on our revenue per ton. And so, I think that's also geometric in terms of our growth in gross profit dollars per ton.

And so I think we feel very confident as we look to -- whether it's next year or the next three years, I think while the ag input cost may change, we may pass through some of that in our revenue, but we're very much desirous of growing the right types of tons and doing so at a gross profit per ton that aggregates and I think fuels our outlook for our business.

Benjamin Theurer: Jim, Jim, thank you very much.

Jim Zallie: Thanks, Ben.

Benjamin Theurer: We'll move to the breakout in case the audience has questions and thank you very much.

Jim Zallie: Thanks very much. Thank you.