REFINITIV STREETEVENTS

EDITED TRANSCRIPT

INGR.N - Q1 2022 Ingredion Inc Earnings Call

EVENT DATE/TIME: MAY 05, 2022 / 3:00PM GMT

OVERVIEW:

Co. reported 1Q22 net sales of $1.892b, reported operating income of $210m and reported EPS of $1.92. Expects 2022 and 2Q22 net sales to increase low double-digits. Also expects 2022 adjusted EPS to be $6.85-7.45.

CORPORATE PARTICIPANTS

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

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

Jason Payant *Ingredion Incorporated - Interim VP Investor Relations*

CONFERENCE CALL PARTICIPANTS

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

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

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

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

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

Seth Goldstein *Morningstar Inc., Research Division - Equity Analyst*

PRESENTATION

Operator

Thank you for standing by, and welcome to the First Quarter 2022 Ingredion Incorporated Earnings Conference Call. (Operator Instructions) As a reminder, today's program may be recorded.

I would now like to introduce your host for today's program, Jason Payant, Vice President of Corporate Finance and interim Vice President of Investor Relations. Please go ahead.

Jason Payant *- Ingredion Incorporated - Interim VP Investor Relations*

Thank you. Good morning, and welcome to Ingredion's First Quarter 2022 Earnings Call. I'm Jason Payant, Vice President of Corporate Finance and interim Vice President of Investor Relations.

On today's call are Jim Zallie, our President and CEO; and Jim Gray, our Executive Vice President and CFO. We issued our results today in a press release that can be found on our website, ingredion.com, in the Investors section. The slides accompanying this presentation can also be found on the website and were posted today 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 and include expectations and assumptions regarding the company's future operations and financial performance including the impact of the COVID-19 pandemic. 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 Forms 10-Q and 8-K.

During this call, we also refer to certain non-GAAP financial measures, including adjusted earnings per share, adjusted operating income and adjusted effective tax rate, which are reconciled to U.S. GAAP measures in Note 2 non-GAAP information included in our press release and in today's presentation's appendix.

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

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

Thank you, Jason, and good morning, everyone. We had a strong start to 2022, delivering outstanding top line performance of 17% net sales growth for the quarter. Our results were driven by excellent sales execution that led to $278 million of incremental sales, enabling us to more than offset inflationary impacts, and our supply chain responded to higher-than-expected customer demand. As a result, full year adjusted operating income grew 6% versus the prior year. And it's worth noting that this was the strongest first quarter result in operating income in our company's history.

Turning to our top line performance. Across all four regions, we grew comparable net sales for the first quarter by high double digits. Our operating teams actively managed the terms of our customer contracts, which enabled them to address higher corn and input costs and deliver both core sales growth and a stronger specialty mix. Recognizing the contribution last August of our Argentina business to the Arcor JV, on a comparable basis, our Brazil and Andean quarter 1 net sales combined were up 23% versus prior year.

Turning to Slide 7. You can see just how critical our pricing centers of excellence were in delivering strong price mix gains across each region. In the quarter, we delivered greater than $280 million of price mix improvement to successfully offset the significant increases in raw material and input costs that we experienced. Combined with favorable product mix and organic volume growth, we were also able to grow operating income by 6%.

Now moving on to the strategic pillars. We continue to make great progress against each of the four pillars that shape our strategy. To start, global specialties once again led our top line growth, up 20% in the quarter. Specialties growth was robust across all growth platforms with texturizing ingredients and sugar reduction leading net sales dollar growth. Plant-based protein sales were up more than 250% in the quarter. And I'll speak more to our progress with plant-based protein in a moment.

Moving to commercial excellence. Our sales teams around the world coordinated closely with our customers and our supply chain to most effectively navigate product delivery challenges. We also operated with a dynamic approach to pricing to reflect timely changes in our freight and input costs, enabled by more flexible contract terms. These strong commercial efforts enabled us to largely offset inflationary impacts, continue to improve our product mix and organically grow volumes on a comparable basis.

We also drove cost competitiveness through operational excellence as our teams worked hard to increase production while managing continued disruptions in global supply chains. We expanded our commodity risk coverage and continue to develop our approach toward commodity risk management to further reduce the impact of raw material cost volatility in the current environment.

All of this progress continues to be underpinned by our fourth strategic pillar, accelerating a purpose- and values-driven growth culture. We are pleased to announce that Nancy Wolfe joined Ingredion as our Chief Human Resources Officer. Nancy brings more than 20 years of executive HR experience, most recently joining us from Bayer Corporation, where she served in business partnering roles to both the innovation and commercial teams. Nancy is already driving a people-centric HR agenda. And we are looking forward to her leadership contributions.

Turning our focus to sustainability. We have been recognized by the Science Based Targets initiative as committed for our emissions reductions targets by 2030 that we put forward in our sustainability plan. Additionally, we continue to engage with customers and growers to advance regenerative agriculture and sustainable sourcing for our Tier 1 priority crops.

Now let me spend a moment to update you on plant-based proteins. We grew net sales by greater than 250% in the quarter. Our customer pipeline remains robust and diversified across different categories, and it continues to grow. We are overcoming the manufacturing challenges typically associated with new plant startups and are pleased to report that production accelerated last quarter at South Sioux City with overall output of pea protein isolate doubling over the last 3 months. Both production and sales are improving and results for the quarter were ahead of prior estimates.

Despite the strong start to 2022, there were, of course, new challenges that surfaced early in the quarter, which we will need to continue to monitor and manage throughout the year. With sales in over 120 countries, it is important to point out that less than 0.5% of our global sales were into Ukraine and Russia. Like everyone else, we are saddened by the toll the conflict is taking on Ukraine's citizens and the resulting humanitarian crisis that continues to unfold. We have a small number of employees in Ukraine and have provided support for them and their families during this terrible time.

To help those impacted by the crisis, we are supporting the World Central Kitchen, which is operating in Poland by serving refugees. And in addition, our employees in Europe are contributing to the United Nations Refugee Agency and the company is matching those contributions. Inflation, already a significant factor coming into the year, was exacerbated by the Ukraine conflict.

Agricultural and energy supply flows across Europe have been impacted, leading to higher prices. In limited circumstances, supply disruptions have impacted availability of key product lines. And to meet customers' changing needs, we have either moved product or reallocated available supply to keep our customers operating.

Lastly, while we all hoped we would be moving beyond the pandemic after 2 challenging years, difficulties remain, particularly in China. However, our team at our Shanghai specialty starch facility has been operating throughout the lockdown since the beginning of April. And we continue to ship ingredients critical to the local food supply chain, albeit at a slower pace.

In addition, our commissioning team for our modified starch expansion in Shandong province continues to progress the mechanical completion of this strategic investment. At this point, we cannot predict the countrywide scope and duration of the pandemic's resurgence in China. Therefore, with reduced consumer mobility and foodservice spending, we are likely to see an impact on sales volume in the second quarter.

And now let me hand it over to Jim Gray for the financial overview.

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

Thank you, Jim, and good morning to everyone. Starting first with our Q1 regional performance. North America net sales were up 24% when compared to the same period in 2021. The increase was driven by strong price mix, primarily as a result of successful contracting for 2022 and higher-than-expected volumes. North America operating income was $156 million, up 16% versus the prior year. As Jim mentioned previously, the increase in operating income was driven by strong price mix that more than offset inflationary input costs, including higher corn.

In South America, reported net sales were down 8% versus prior year, driven by the Arcor JV net sales presentation change. This change was the result of the inclusion of our Argentina sales in our regional results last year and the exclusion of Argentina sales in this quarter due to the contribution of Argentina to the Arcor joint venture. On a comparable basis, net sales would have been up 23% versus prior year, primarily driven by strong price mix.

South America's operating income was $38 million, down $2 million. Results were impacted in the quarter by the change in presentation of the Arcor JV results. The combined results for Andean and Brazil were up as strong price mix in both offset weaker volumes and net corn inflation in Brazil. Including foreign exchange impacts, adjusted operating income was down 8% in the quarter.

Moving to Asia-Pacific. Net sales were up 16% in the quarter. The increase was driven by higher sales volume across the region, including PureCircle, and by favorable price mix, partially offset by negative 5 points of foreign currency impact. Asia-Pacific operating income was $22 million, down $3 million versus prior year as Korea faced challenging raw material and natural gas inflation, which outpaced the price mix.

In EMEA, net sales increased 20% for the quarter. The increase was due to favorable price mix and higher volumes, including KaTech. Absent foreign exchange, sales were up 28%. EMEA operating income was $31 million, flat compared to the prior year quarter. European operating income was up in the quarter led by strong price mix. Higher manufacturing costs in Pakistan, primarily energy costs, and foreign exchange headwinds more than offset favorable price mix in the country.

Moving to our income statement. Net sales of $1.892 billion were up 17% for the quarter versus prior year. Gross profit dollars were higher year-over-year while gross margin was 20%, down 170 basis points, mostly attributable to price mix lagging higher corn and input costs, primarily in Pakistan and Korea. Reported operating income was $210 million and adjusted operating income was $213 million. Reported operating income was lower than adjusted operating income primarily due to restructuring and acquisition integration expenses. Our first quarter reported earnings per share was $1.92 and adjusted earnings per share was $1.95.

Turning to our Q1 net sales bridge. We achieved strong price mix of $283 million, largely attributable to the pass-through of higher corn costs in each of our four regions, particularly North America and South America. The sales volume increase of $19 million was driven by volume increases in North America, Asia-Pac and EMEA, including KaTech, partially offset by the impact of the presentation change related to the Arcor joint venture.

On the next slide, we highlight net sales drivers. Of note, foreign exchange was a 2% headwind in the quarter. South America results include the impact of the presentation change of the Arcor joint venture.

Turning to our earnings bridge. On the left side of the page, you can see the reconciliation from reported to adjusted earnings per share. On the right side, operationally, we saw an increase of $0.12 per share for the quarter. The increase was driven by operating margin increase of $0.19, partially offset by unfavorable foreign exchange of minus $0.04 and lower volumes of minus $0.03.

Moving to our nonoperational items. We saw a decrease of minus $0.02 per share for the quarter, primarily driven by higher financing costs of minus $0.04 per share, partially offset by a lower adjusted effective tax rate of $0.01 a share and shares outstanding impact of a positive $0.01 per share.

Moving to cash flow. First quarter cash provided by operations was a negative $52 million. Cash from operations decreased versus prior year, driven by higher working capital usage. Working capital balances were impacted by the pricing increase in net sales, reflecting higher receivable balances and higher corn costs reflected in inventory values as compared to the prior year.

Capital expenditures were $85 million, up $17 million from the prior year period due to the timing of spend. We are in line with expectations for new capital commitments in 2022. During the quarter, we paid $43 million of dividends to Ingredion shareholders and repurchased $39 million of outstanding common shares.

We are maintaining full year 2022 adjusted EPS range of $6.85 to $7.45. This excludes the impact of acquisition-related integration and restructuring costs as well as any potential impairment costs. We expect net sales to be up low double digits, driven by strong price mix, the pass-through of higher corn costs 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 $340 million net asset impairment charge related to the contribution of the company's Argentina operations to the Arcor joint venture.

And to call out, as I've highlighted on this slide, we expect adjusted operating income to be up low double digits compared to last year, which is an increase to our previous guidance. We have expanded raw material risk coverage to limit volatility in the quarter and for the remainder of the year. While the full impact of inflation is yet to be seen on both input costs and consumer demand, we believe we are well positioned and are reaffirming our guidance.

2022 financing costs are expected to be in the range of $83 million to $88 million, reflecting higher foreign exchange losses and incremental borrowing costs. Our anticipated adjusted effective annual tax rate has increased and is expected to be between 28% and 29.5%, reflecting the impact of new U.S. tax regulations, which reduced the company's ability to credit certain foreign taxes. The expected 1% increase will have a negative $0.10 impact to adjusted full year EPS versus our previous guidance.

Cash flow from operations is now expected to be in the range of $580 million to $660 million, reflecting higher working capital investments. We expect greater investment into working capital as net sales grow and we began to rebuild inventories. Capital investment commitments are expected to be between $300 million and $335 million, of which approximately $90 million will be invested to drive specialty growth. We expect total diluted weighted average shares outstanding to be in the range of 67 million to 68 million for the year.

In terms of our regional outlook, North America net sales are expected to be up 10% to 15%, driven by favorable price mix and higher volumes. Operating income is now expected to be up low double digits to mid-double digits, driven by favorable product mix and higher volumes. For South America, we now expect net sales to be down low to mid-single digits reflecting the impact of the Arcor joint venture, partially offset by favorable price mix. South America operating income, including the impact of the Arcor joint venture, is now expected to be up low single 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 flat to prior year, driven by higher corn costs in Korea related to the Ukraine conflict. For EMEA, we expect net sales to be up 10% to 15%, which includes KaTech, and operating income to be up low single digits, driven by favorable price mix. For the second quarter of 2022, we expect total net sales to increase low double digits and operating income growth to be relatively flat when both are compared to prior year.

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

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

Thanks, Jim. Before concluding, I would like to let everyone know that on May 11th, we will be publishing our 2021 sustainability report. We look forward to sharing more with you about our continued progress against our 2030 All Life commitments. For more on our purpose-driven commitment to healthy and sustainable growth, you can also access my message to shareholders in our annual report, which was released on April 7.

In summary, Ingredion had a very strong start to 2022. We grew our top and bottom line during the quarter despite significant inflation, all while advancing our strategic pillars and executing against our Driving Growth Roadmap. While the rest of the year will no doubt bring new challenges, our team stands ready to take these head on as we continue to operate with an owner's mindset and adapt and engage each day to create value for our stakeholders. We look forward to delivering a year of meaningful growth.

And now let's open the call for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question comes from the line of Ben Theurer from Barclays.

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

Jim and Jim, congrats on the strong start to this year. First question is -- and I remember you gave us an outlook a few months back in regards to how you think about profitability and just growth evolving throughout the year. And if I remember right, it was talked a lot about the first half actually being a little weaker within the year and then the second half to be the one that looks better.

Now obviously, a lot of things have changed since February since we talked in your presentation at CAGNY. Can you give us an update on how you feel about the cadence throughout the year and how you think about the need to potentially look into further pricing actions, just given how the grain cost environment or corn in specific has changed in the last 2 months?

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

Sure. Ben, let me take the first part of the question just in terms of how the profit lays out for the year. And then maybe we can take a little bit more, expand on that second question in terms of kind of in-year pricing actions. So just -- what we had laid out is that -- and when we looked at really the first half of 2022, lapping the first half of 2021, coming out of Delta, we really had a strong spring in 2021, so a lot of volume recovery, the first time people are out and about, a lot of foodservice volume recovery. And we saw that in multiple regions.

So we knew that coming into this year. However, we also had a challenge that we had to catch up on some of our annual pricing to cover how costs of corn had risen in last year. So putting all those together, we really looked at first half and thought that we would have somewhat modest profit growth versus the lap. When we look to the second half of 2022, we knew that the pricing -- new pricing levels would carry through. And we had generally had experienced higher corn costs in the second half of 2021.

Looking forward to 2022, we had factored that layout of the corn into our outlook. I would say that maybe what's changed just is that we've been a bit more expansive on our coverage of both our gross corn hedges as well as introducing new hedges in terms of co-products. And that, I think, is dampening the impact that we would expect in the second half of this year from how corn futures have really run up since the Ukraine-Russia conflict began.

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

And then as far as the ability to price through in-year inflation, which we anticipate we will continue to see, we have worked diligently with customers through our pricing centers of excellence to increase the flexibility in those contract terms. And that gives us the ability to pass through certainly the increases we're seeing in freight and fuel charges to customers. And so we feel more confident to be able to navigate those increases in-year. And those increases are now a matter of routine to be able to put those through within the year. And that's what we refer to as the dynamic pricing as opposed to everything, it's an all-or-nothing as it relates to contracting.

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

Okay. Perfect. That was very clear. Thank you very much. And then my second question, just if you could give and share a little more detail about the pea protein isolate production ramp-up and what you've been seeing maybe into April then and into May. I mean you've nicely laid out the cadence from the end of last year until the end of March. But just to get an understanding on how you've been doing further and what your expectations are for that particular contribution in 2022 and what you're seeing on the demand side for plant-based.

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

Sure. So I think it's important just to remind everyone that we have two facilities: one is in South Sioux City, Nebraska, which produces pea protein isolate; and the other facility produces pulse-based flours, a range of those pulses, flours and concentrates and specialty concentrates in Vanscoy, Saskatchewan. Both facilities are operating well. The facility that we were referring to in quarter 4 that had typical plant start-up issues was the pea protein isolate facility in South Sioux City. And anytime you start up a new facility, especially a protein facility to get control of all of the parameters to be able to produce reliably the highest-quality food-grade material, a lot of details have to be managed concurrently.

And the team has worked incredibly diligently to systematically do all that they need to do to improve first-time quality for the highest-grade food-grade pea protein isolates, which sell for the highest average selling price, also to improve the yields of the protein that we extract from the peas, and every percent is worth a lot of money in relationship to that, and to increase just the overall production of food-grade salable pea protein isolate. And we've seen just a steady increase in all of those attributes since we spoke to you last. From the month of December, for example, we've seen significant increases and a tremendous increase in output.

But not only that, in order for our commercial teams to be able to commit to customers the volume that they want to purchase from us, from the robust pipeline we have, there needs to be that confidence in that production and a sufficient amount of inventory that we have to build. We've done all of that. And so that's why the sales have actually begun to ramp up as well. So we have momentum where the production is meeting now with the commercial demands. And we're hopeful that, that's going to continue because we do see a very robust demand outlook for plant-based proteins. The Vanscoy facility also continues to run very well. And again, we have a bullish outlook on the flours and concentrates from that facility.

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

Perfect. Thank you very much.

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

Ben, let me just add. I mean I know that we had put out a kind of an improvement in the operating loss. And we're still really expecting at least a $10 million improvement year-over-year as we're looking at our plant-based protein kind of business unit, just feeling pretty good about it right now.

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

Yep.

Operator

Thank you. Our next question comes from the line of Ben Bienvenu from Stephens. Your question please.

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

Hey, thanks good morning.

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

Hey Ben.

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

Good morning Ben.

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

I want to ask, within the updated guidance that you provided by geography, you touched on volume expectations across a handful of geographies. Could you kind of take us around the world and talk about what you're seeing in terms of volume demand and your expectation for the layout for the balance of the year and maybe the things that we should be monitoring with respect to geopolitical uncertainty and inflation and how that might impact the volume demand dynamics in your business?

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

I'll try to take a shot at that and then Jim will add some color commentary.

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

And I'll cover South America just because it's a little tricky...

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

It's a little tricky in relationship to the Arcor JV, yes. So first of all, North America, we're seeing still very strong demand throughout all of North America. And again, we can sell everything that we produce and logistically be able to supply with a very strong order book going forward. And I believe that's going to continue certainly through the end of the summer. That's my own view related to the fact that we see a strong consumer, and we just see strong demand overall with foodservice being very strong as well.

As it relates to South America, very strong demand in the Andean region and exceptionally strong pricing. In Brazil, volume was a little weak in the quarter. And we are watching that because inflation is really rearing its head again in Brazil. And there's less government stimulus and they're raising interest rates to try to curb inflation. And we're a little bit cautious on the outlook in relationship to Brazil volumes, even though we think some of the volume softness in quarter 1 was related to just a pretty cool weather pattern down in Brazil in quarter 1. So we think that will improve.

From Asia-Pacific standpoint, obviously China is the watchout. The COVID lockdowns will definitely impact and are impacting consumer mobility and foodservice demand. And so we think volumes there may be challenged, at least in the second quarter, but should see a bounce-back, assuming COVID settles. But we have to also watch obviously the logistics issues around just being able to get product in and out of the country and also within country. The rest of Asia looks actually very strong. Our ASEANI business looks very strong. Our tapioca business looks very strong. Our rice-based business looks very, very strong. So overall, the rest of Asia, the watchout is China.

And in EMEA, similar for the European perspective to the United States, the outlook for demand is very strong. At least again, we would say through the end of the summer, that's where we kind of -- we think have visibility. Pakistan demand also looks solid. But the watchout there is corn prices and energy prices basically. So Jim, do you want to add some comments maybe on South America just in relationship to Arcor and the JV?

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

Yes, I just want to make sure that in the presentation for Q1 and as we go into Q2 and then less so to Q3 that the segment is going to just be the reported volume. And so as the Argentina volume and net sales have come out of this year, it's still in the base for next year. And so the reported numbers will always be reflecting that. And then we'll help you with what we think the comparable net sales growth is to that point. So hopefully, that's laid out in the presentation and noted in the footnotes.

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

So Ben, was that helpful?

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

Very, very. Thank you. That helps us kind of get additional context on what's going on. I want to ask, you covered the pea protein isolate, how production is ramping. I think both Jim and you covered how the operating loss dynamic is improving as we move through this year and into next year. Could you give us an update, too, on PureCircle? It sounds like pea protein isolate is going well in terms of recovering operating losses and getting to scale. How is recovering operating losses and improving profitability at PureCircle going? And that's all I have. Thanks so much.

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

Yes. Thank you, Ben. We are extremely happy with the progress we're making at PureCircle. PureCircle results for the first quarter were in line with our expectations, delivering double-digit net sales growth and positive operating income for the full quarter. We expect PureCircle to have year-over-year growth in net sales and operating income in 2022 as well as positive operating income for the full year of 2022. For Asia-Pacific operating income, we are indicating that to be up high single digits, which anticipates a $6 million to $8 million improvement for PureCircle's bottom line.

So again, it's really a tremendous turnaround story of a business that we bought that was distressed that had a great product line, great technology, great intellectual property, and that we are really leveraging it and we're making significant investments right now to expand capacity of the highest-value products that PureCircle produces just based on the bullish prospects that we have for sugar reduction.

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

That's great, thanks so much.

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

Thanks Ben.

Operator

Thank you. Our next question comes from the line of Ken Zaslow from BMO, your question please.

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

Hey, Good morning guys.

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

Hi Ken.

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

This environment was probably a little bit more shocking as an external shock to the environment. When you kind of think about how you navigated this environment, does it give you more or less or no change to your ability to hit your long-term growth targets as you laid them out back at CAGNY?

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

Well, I think you continue to -- when you're working in an environment like this, collectively, as a multifunctional-faceted business, people continue to develop stronger and stronger muscles to be able to navigate the dynamics. And again, as it relates to some of the things that we did collectively with our customers in relationship to contract terms and conditions, being able to determine how to navigate supply chain issues and how we provide that outlook, we feel confident we can navigate complex dynamic environments, given what we have already been through, along with the $700 million of capital investments that we featured at CAGNY in relationship to all of our growth platforms and the fact that we're seeing those deliver in the case of PureCircle, which I just spoke about.

The promise that we still see with plant-based proteins, the growth in texturizers, which has to do with the investments that we've made in starch-based texturizers and the diversification beyond corn with the strength in tapioca, rice, potato. So from a standpoint of all of that being taken into account with the long-term outlook that we have, we are more -- we're every bit as optimistic as we were as it relates to what we just said at CAGNY in February.

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

Yes. Ken, let me just add, right, because obviously corn went up a lot in 2021, 20%, 25%. And so sometimes we get questions from investors like, "My gosh, I mean, will you be able to put that type of pricing through? That seems extraordinary relative to what we're hearing about inflation rates being lower for other types of inputs or services." So look, our customers understand that rising agricultural costs are a significant cost component of our products. And that needs to be passed through in our pricing.

And just to remind everyone, the cost of our ingredients relative to the total cost of the packaged food or beverage usually represents a very small percentage. And our ingredients play really an indispensable role that impacts both product quality, texture and taste, right? So there's high value relative to a lower cost of the ingredient. And so customers tend to understand like, "Well, yes, there's a raw material component here, be it tapioca or corn or something, and that moves every year, and Ingredion is going to bring to us a very clear communication on that."

I think on top of that, what we've done recently through our pricing centers of excellence and looking at the environment that Jim just mentioned is really segment our customers based upon their strategic long-term value creation opportunity to us and adjust contract terms and conditions to be able to react more flexibly to the current inflationary environment. And I think that refined approach -- look, we're in the first, second steps of this, but that refined approach is showing up in our strong price mix. And I think that is a capability that we're building that's going to be just very complementary to the long-term investments that we put forward on specialty.

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

And lastly, what I would just say to build on what Jim just said is what's important to remember is that the value propositions that are inherent in the ingredients we supply do enable affordable formulating. So for example, right now, what we're seeing is increased demand for specialty starches to replace expensive milk and dairy proteins, which have accelerated greatly in price. So from a standpoint of the value propositions that are inherent, from an affordable formulating standpoint, in an inflationary environment, our customers are coming to us looking for the unique functionality and the ability to either replace or extend more expensive ingredients.

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

Great. I'm going to ask a follow-up to this. If I think about it -- I don't know if this is a fair question, but I'm going to try it anyway. If you go back 2 or 3 years ago before you had this pricing centers of excellence, what type of pricing do you think you would be able to have gotten in this environment?

And then when you go into 2023, how much more do you think that you would have been able to get, given this whole change in environment? And is it enough to offset the rise of input costs? So it's past, present and future on your pricing model and how that plays out. And then I'll leave it there, and I appreciate it.

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

Well, Jim and I are going to tag team on this answer. What I just wanted to say is that as it relates to pricing, it's something that I think a lot about. Because when I started into this role, in my first 3 years, we endured and had to offset more than $950 million of foreign exchange headwinds through pricing. So for us as a company, the ability to price through and offset foreign exchange devaluation was critical before inflation reared its head.

So we took the progress that we made there and formalized it in anticipation of inflation but to become even better ahead of inflation by formalizing the pricing centers of excellence. So I think that we were, out of necessity, needing to be proficient with pricing, formalizing and standing up and sharing best practice across regions with pricing centers of excellence and then advancing that through renegotiation of customers' supply terms and conditions, this past year has really, I think, put us in good stead. And Jim, did you want to add anything to that?

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

I would just say that, hey, Ken, if you look back 3 years -- I mean, it's tough to quantify, right? But if you look back 3 years and you just said, "Each sales team came to a customer relationship and had precedent, right? This is where we've been. This is the change in corn." And really, what is now the approach is a holistic approach across the portfolio, saying, "What product do we have available? And which customers are going to be the longer term -- in the longer term, creating more value for us and for them?" And that's where we're both going to price as well as allocate product. So we're just inserting, I think, a layer where we just look holistically across the product line and all of the customer demand and then basically finding the fairest way to allocate that product.

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

Great. I appreciate it. Thank you

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

Thank you Ken.

Operator

Thank you. Our next question comes from the line of Robert Moskow from Credit Suisse, your question please.

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

Hi. My apologies if you might have answered this already. But I remember at the end of last year, you had some numbers about capacity utilization in the industry and how it had improved substantially with a rebound in foodservice demand. Do you have an update on where you think it is right now? I would imagine it's only getting better. And is that also giving you more confidence about pricing power for the future?

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

Rob, I'll just note kind of two trends that I think continue. So one, overall in terms of wet mill grind, there continues to be a demand for kind of industrial either glucose or syrups and that, really as feedstocks into sustainable needs. And that's been a trend that continues to go and is actually probably even more stimulated during the last year, during 2021 that's kind of pushed towards sustainability, and it's up, right? There's also now -- I mean, there's going to be summer demand for ethanol, right? So the administration went out and kind of allowed ethanol to be sold throughout the summer. So that's going to pull off of the wet mills at least.

And then very specifically to the types of food and beverage ingredients that we sell, I do think that you're still seeing a nice strong pull from just syrup, right, just honestly, as you've expanded all of these food service outlets. And not just the restaurants that we talked about last year, but every sporting venue, all the universities are back, your educational -- kids in high school are back in school, at schools, on-premise. And you're seeing, I think, that fleshes out really what we used to talk about in terms of limited consumer mobility. Consumer mobility is fully back. And that's in U.S. as an example, but we're actually seeing that in other countries as well, except for China.

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

Right. Okay. So no numbers that you can share at this point? Do you think you can give us one at some point during the year on utilization?

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

Yes, probably better mid-year. Yes, just to get a read on that, right?

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

Okay. That's it for me.

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

Thank you Rob.

Operator

Thank you. Our next question comes from the line of Adam Samuelson from Goldman Sachs, your question please.

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

Hi thanks. Good morning everyone.

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

Hi Adam.

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

Just a question, sort of got touched earlier, but thinking about maybe the non-corn inflation dynamics and maybe how those may have accelerated year-to-date since some of your major contracting, thinking specifically in North America on the energy side, whether it's natural gas or coal-powered energy, freight with diesel prices and some of the surcharges that would flow through there, just how you think about those as you go through the balance of the year.

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

Well, I think that's part of that dynamic in-year pricing flexibility that we have built into many of our contracts, specifically the ability to price through increases in diesel that you referred to or packaging and supplies to some degree. So yes, we're watching that very closely, but we can pass through in-year portions of that, those increases.

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

Yes. Hey, Adam, it depends on which kind of energy source you're talking about. So if it's oil, oil is going to obviously work through in terms of fuel costs. And probably, the largest dollar exposure we have is just what are those fuel surcharges that come through from either trucking or from rail. Our vendors have those established. They usually have triggers when we pass through those. And we have also worked really diligently, at least in markets like the U.S., where we have exposure on the freight cost to the customer, to make sure that we specifically have fuel surcharges identified in our contract terms.

I think secondarily or maybe even tertiary is some modest impact to maybe some chem costs, maybe some plastic packaging costs. But really then, the other side of the complex is really nat gas. And obviously, we use nat gas in a number of our facilities within North America as well as elsewhere. And generally, we have a policy where we are pretty well hedged in the prior year before we get into the fiscal year with regard to what our gas usage needs are. So really, not as concerned about the conversion cost of the energy because we were very hedged. And obviously then, as we look forward to 2023, that's one consideration that I think every company will face as they're thinking about their fiscal '23.

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

Okay. That's really helpful. And then maybe just switching gears on capital allocation, I mean, you did buy back a little bit of stock in the quarter. Just talk about the M&A landscape. And are you seeing opportunities on the specialty ingredient side for more bolt-ons, maybe things like KaTech, PureCircle? Or is there anything maybe a little bigger that might be in the pipeline and how that would sit today?

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

Yes. Jim, do you want to take the buyback?

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

Yes. Hey, Adam, so one of the things that we are really committed to is thinking about total shareholder return. Clearly, we have a dividend, and we've been very clear about our dividend payout, right around 40%. We look at our dividend relative to our adjusted EPS expectations as we go forward.

And then also, look, to the extent that we have room in our balance sheet and we're looking at our anticipation for strategic cash flow, we are going to consider repurchase when we think it's a very attractive return to shareholders. I don't think that precludes us at all nor takes away anything from how we're looking at our M&A.

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

Yes, not at all. And in fact, it shouldn't be misinterpreted as an alternative to pursuing M&A as our -- one of our top priorities as it relates to our capital allocation. Clearly, we have shown a commitment to invest in the business organically for growth. But equally, we're always looking for opportunities to enhance the portfolio capabilities, geographic breadth and just again, the inherent value propositions of the five growth platforms with M&A.

So what I would say is that M&A is still a very important priority for us as a business, and it will remain so. That all being said, we will remain financially disciplined to make sure that we can create value for shareholders. But we're not discouraged by the M&A landscape. We see opportunities out there. We're actively pursuing them. But we'll be disciplined in our approach.

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

I really appreciate all of the color. I will pass it on. Thank you

---

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

Thank you.

Operator

Thank you. Our next question comes from the line of Seth Goldstein from Morningstar, your question please.

Seth Goldstein - *Morningstar Inc., Research Division - Equity Analyst*

Hi, good morning everyone. Thank you for taking my question. Just had a quick clarification -- a quick clarification on the new updated pricing. And I appreciate all the details so far. How often do the prices reset to your customers?

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

It's a great question, Seth. Generally, around the world, we are looking at pricing that's anywhere between like a 3- to 6-month type of horizon. And that's usually because our teams are looking out and saying, "Hey, how far out can they secure corn?" We know and we have a lot of discussion around the North America business, and particularly the U.S./Canada business, where a large number of our customers represents a little bit less than half of our revenue is on an annual contract basis. And so that's why it's important for us to talk about, "Hey, did corn go up?" And when we reset our contracting season, which is in the fall, that's where we're reestablishing the new price points that are recognizing the cost of corn that occurred within that year.

Seth Goldstein - *Morningstar Inc., Research Division - Equity Analyst*

Okay, great. I appreciate that detail. And then for the customers who are switching to your starches as a substitute for things like dairy products, are these specialty starches they're buying? And is this something where they can easily shift back and forth? Or do they have to reformulate the entire product to switch to your starches?

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

Typically, we have developed recipes that guide customers on how to either extend their products with our ingredients. They are specialty ingredients. They are the higher-margin specialty starches. And that's one of the things that we saw in the quarter is a very strong specialty mix as well.

So it's something that has already been demonstrated that we work through our technical service teams with customers on, say, quick recipe reformulation. And customers are more receptive than ever, given the concerns about inflation and the outlook but also just about reliable supply of ingredients right now to work to reformulate with us.

Seth Goldstein - *Morningstar Inc., Research Division - Equity Analyst*

Okay, great. Thanks for taking my questions.

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

Thank you.

Operator

Thank you. This does conclude the question-and-answer session of today's program. I'd like to hand the program back to Jim Zallie, President and CEO.

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

Well, I wanted to thank everyone for joining us this morning. We look forward to seeing you at our Investor Day on June 2, which will be held at our global innovation center in Bridgewater, New Jersey. For those of you who are able to attend in person, after the presentation, we'll have a tour demonstrating our innovation capabilities and provide you with a tasty lunch, which will feature our ingredients in action. So I wanted to thank everyone for your continued interest in Ingredion.

Operator

Thank you, ladies and gentlemen, for your participation in today's conference. This does conclude the program. You may now disconnect. Good day.