Barclays 17th Annual Global Consumer Conference
Ingredion Fireside Chat

September 4, 2024
9:45 AM EDT

Benjamin Theurer: Thanks for joining us again this morning. Next on stage we have Ingredion. Pleased to have with us Jim Zallie. He's President and CEO of Ingredion since January of 2018. Also was part of the Board of Directors already since 2017. He previously served as Executive Vice President., Group Specialties, and President of the Americas. And he joined the company actually back in 2010 when Ingredion acquired National Starch, a $1.2 billion leader in specialty starches. Jim will kick it off with a few prepared remarks and a couple of slides, and we'll then go into some Q&A. Jim?

Jim Zallie: Thank you, Ben. It's a pleasure to be back in Boston with all of you. I look forward to, Ben, our discussion here in a few minutes. I wanted to give a brief update on Ingredion and how we're performing, what are focus and what our priorities are, and how things are shaping up for us in the second half. Let's get right into it.

First, everything that I'm going to say now and everything that I'm going to say in the sit-down fireside chat will be covered by our safe harbor provisions.

For those of you that are not that familiar with Ingredion, we're a leading, global, plant-based ingredient solutions provider. We have wide geographic reach. We have 18,000 customers that we sell to in more than 120 countries. And the ingredient portfolio that we supply has a lot of relevance to food formulating. The way to think about it is that of all the products that we supply, they have broad reach to new product formulation. And so 70% of the kinds of products we produce, or the categories, find their way into new products. A lot of relevance with customers, which gives us that broad customer reach.

We are a company that's really known for our technical service and innovation and customer intimacy to help them get to market to drive consumer preferred innovation. And one of the things that we have committed to is to have our Tier 1 priority crops, which account for approximately 97% of all the crops that we source from, to be sustainably sourced by 2025, and we're on track to hit that target. We're headquartered outside of Chicago in Western Cook County. One other interesting factoid is that we've been listed -- I think we're the 13th longest listed company on the New York Stock Exchange and coming up on 122 years.

In 2023, our sales reached $8.2 billion. It was a record year for profitability last year.

54% of our sales go to food and the other 15% go to beverages, soft drinks and a variety of beverages in brewing. And that accounts for about 70% of our revenue. And 21% goes into papermaking, primarily US/Canada, in Asia, as well as in LatAm. And then we grind corn, and we sell coproducts. And those coproducts are then sold for animal nutrition purposes, both poultry as well as cattle as well for example, and that's about 10% of our revenue.

Over the last 3 years, we've delivered pretty strong sales growth at a compounded annual growth rate of 11% and our adjusted EPS has grown over that same period, compounded annual growth of 15%. One of the things that we are particularly proud of, that we feel very strong about, is the work that we have done incrementally across the business to reduce earnings volatility. It's one of the things that the team has been extremely focused on, dissecting every piece of our business. What we purchase, customer contracts, how they're structured, where risks lie, our hedging programs, both for not just the raw material, but also the coproducts, and what we can do to mitigate risk. Also, to improve forecasting accuracy with customers and scheduling adherence. In addition, our pricing centers of excellence, which again have helped with customer contracting, and again, diversifying and spreading our risks. And that has helped as well.

And then of course, we're very committed to financial discipline and consistent capital allocation, and I'll share with you those priorities in a moment.

One of the things that we did is announce in November of last year the intent in 2024 to re-segment our business. And we re-segmented and have been reporting now in 2024 based on these 4 business segments. One is a global segment which is Texture & Healthful Solutions which comprises the majority of what were formerly called our specialties ingredients. But really, it's around texturants, specialty starches, hydrocolloids. And then leveraging our very strong positions in more basic food ingredients that again find their way into so many different food products, Food & Industrial Ingredients in US/Canada. Food & Industrial Ingredients LatAm, and then another category which I'll describe a little bit. I'm sure Ben will ask me, but 2 growth operating units. One around sugar reduction, leveraging our position as the world's leader in stevia as well as protein fortification and plant-based proteins are in that Other category. I'll talk more about the segmentation, but this was all done to help us become more intimate with customers, help us look at our innovation opportunities, leveraging the ingredients in those portfolios aligned with customers and what they produce and how our ingredients line up best. And also, how to reallocate our R&D investment as well as our capital investments across the segments. It is helping drive efficiency and I'll talk more about that.

Really, for us, these 2 categories of segments, one is around the food industrial ingredients, which is primarily starches and sweeteners, and the focus on supplying really better ingredients to that customer category. These are large and mature markets, more mature markets. The revenue growth is lower than on the texture, global Texture & Healthful Solutions. But still, I had a former boss who used to say 1% of a large number is still a big number. Still an opportunity to drive revenue growth.

The margins are pretty steady. As I said, we've really done a lot of work to reduce earnings volatility, and they are very cash generative from a standpoint of those assets and how we're leveraging and investing in reliability. It's focused on CapEx and cost savings as well. Whereas on the solutions opportunity side, for Texture & Healthful Solutions, these are larger, faster growing segments. The revenue growth is mid-single digits to higher single digits is what's targeted. They can have the opportunity to deliver higher gross profit margins. Typically, our aspiration is 2x the level on the food and industrial ingredient side from a gross profit standpoint. And that's where a lot of our organic investments, and I'll share with you the amount of organic investments we've made, they went primarily more towards the global Texture & Healthful Solutions. About $850 million over the last say 5 to 6 years. And not all of that is paying back yet, so there's opportunities to grow.

One of the big things that we're focused on in the Texture & Healthful Solutions ingredients segment is to leverage how consumers and CPG companies and private label companies are thinking about texture as a differentiator. You can see some of the statistics in relationship to how texture impacts a consumer's preference for their purchasing decisions, and the enjoyment of a food from a standpoint of the fun experience. Multi-textured foods actually are preferred by consumers from an enjoyment standpoint. Also, texture plays into consumers' moods, and focus on times of day or dealing with stress or wanting to feel calm. All of that is an opportunity beyond the significant role that I think we're all very familiar with that flavors play on consumer preference.

And here's just an example of the texture attributes. You see all the banners there, can drive 70% of consumer preference. It's a large and growing market, $20 billion. We're the global leader in specialty starches across a realm of base types. 7 types of specialty corn types which we modify chemically, enzymatically, physically with hundreds of permeations that we know how to dial in the texture. We're the leader in tapioca starches. We have potato starches, rice starches, so very broad, very deep. And those products are very affordable and pretty ubiquitous across the food formulating spectrum. They find their way into many, many new product introductions. In addition, we supply hydrocolloids that are kind of tweaking agents to perfect textures. And equally, our plant-based proteins, proteins also influence texture, so we're very, very focused on the texturizing market.

The role texture plays also influences how consumers perceive the healthfulness of a product. Think about a rice cracker for example, being very light in texture, it's perceived as being healthier. As we focus on our wining aspiration that came out of a lot of strategy work over the last 2 years, which is to be the go-to provider for Texture & Healthful Solutions that make healthy taste better, that is demonstrating the importance of connecting the dots between texture and offering healthful ingredients. All with understanding the impact on taste and preference.

The other aspect of our Texture & Healthful Solutions segment, which by the way is about $2.4 billion, $2.5 billion in revenue, operating income margins targeted between 14% and 17%, and we think we can over time get to the higher end of those operating income margin aspects, this segment involves more of the depreciation and amortization associated with the CapEx that we've made. But also, the majority of our R&D spend. But it's focused in 3 areas, really. Sugar reduction and metabolic health, protein fortification for plant-based diets, and fiber fortification for digestive health.

The markets themselves are very large despite the lull that protein fortification has hit over the last few years. Everybody is very familiar with the alternative meat space and the headwinds that that has hit for a variety of reasons. But the alternative dairy category is still very large. Protein fortified snacks, protein fortified dairy products, alternative dairy, still very large segment at $10 billion, growing at 6% to 8% compounded annual growth. Sugar reduction, still a very significant market, growing. There's added focus for consumers on now labeling requirements to call out added sugars for example in the United States and having 10% of your calories come from added sugars. That is a market segment that has tailwinds behind it.

And then fiber fortification as well for digestive health. Our portfolio of ingredients really lends itself very well where we focus on delivering those consumer benefits. But again, Ingredion has a very wide and deep portfolio of stevia-based, high intensity natural sweeteners. Stevia is about 300x sweeter than sucrose, and we supply it from a leaf extract standpoint. We bio convert it to -- basically treat it with an enzyme, the leaves themselves, to get a better tasting, non-bitter tasting stevia. And then also true fermentation which is using sugar as a substrate to form a Reb M. Protein fortification as well, we are supplying pea protein isolates as well as a variety of concentrates and flours from a variety of different pulses. And again, fiber fortification, we sell a product called resistance starch which makes its way into the large intestine undigested. Functions physiologically, analyses its fiber, but gives improved textural benefits, and then Fructooligosaccharides, which is a prebiotic.

The Food & Industrial Ingredients businesses are 2 very significantly sized businesses as you can see. The US/Canada business at $2.3 billion to $2.4 billion, 12% to 14% operating income margins. This is a business I think that for years in our portfolio had been misunderstood. It's one of the values of re-segmenting the business to shine a light on this. And right now, this year, the business is trading at operating income margins at the high end of this, even above the 14%, and so it's a very solid, stable cash generative business. We have very good market positions.

And our Food & Industrial Ingredients LatAm business is really a jewel of a business for us. It's about $2.56 billion. We're the market leader in Mexico, Brazil, as well as Columbia, and have a very solid joint venture with a market leader down in Argentina. And again, growth there has been very strong and our operating income margins are very solid.

What you should take away in regards to those businesses is, they really have high barriers to entry. We can source the raw material from a variety of farmers. There's few competitors again in the relative, in the markets that we operate, US/Canada or in LatAm. And we have many, many customers to sell to. The focus there is on making sure our plants are reliable and cash generative. And then we're looking always selectively at how we can increasingly valorize the grind, trade up, looking very discerningly across customers where there's a finite amount of grind that needs to be incrementally valorized.

The US/Canada business, what you should take away there is, we're the only corn wet miller in Canada. It's not an insignificant market for us. It's a profitable market for us. And we're a very strong number one player in industrial starch. This goes to one of those aspects of where I think we were very misunderstood as a company for years. And this is helping shine a light. And only about 8% of our revenue today comes from high fructose corn syrup and a lower percentage of our gross profit comes from high fructose corn syrup. It's a market that again is trading at the higher end of the operating income target margins for us, this year based on our market position, customer relationships, and the positions we have in those segments.

Again, the LatAm business for us is a jewel. Our Mexico business the last number of years is delivering record profitability and sales. We're a very large supplier to the brewing industry. It is a market that is projected based on modeling and statistics from a standpoint of beer consumption locally, based on GDP per capita, will not peak until 2035. It also is a large export market for brewing and beer. We have a great position there. But also, with all of the customers.

And in this market, we have 10 manufacturing facilities throughout LatAm which is Mexico, Brazil, as well as Peru as well as Columbia. That compares to 4 for our peer companies across that same sector. It tells you the strength of the competitive moat that we have in LatAm and that we're very, very focused on sustainable sourcing and we have a great position in industrial starch as well down in LatAm.

Again, we've invested a significant amount of capital over the last say 5 to 6 years. Most of those investments going to Texture & Healthful Solutions. You can see the acquisition of PureCircle which gave us the leadership position in stevia. Potato based ingredients, expanding our potato franchise in the U.S, which is a great franchise. The investment we made in plant-based proteins, and again, that's a turnaround story where its best days are still we believe ahead of us, and this year is a year of turnaround and promise and some green shoots that we're seeing. I'll talk about that.

We also have not so small businesses in pharma which are very profitable where we sell ingredients for pharmaceutical based excipients. Mannitol, specialty starches, dextrose for IV bags which has grown very nicely, and we're one of the few suppliers that supply that. But also, products for skin and hair care as well.

Our capital allocation priorities are as you see here. Really, we have a pipeline of organic growth investments and that's first and foremost where we look to deploy our capital. We've had a strong and consistent dividend. We just increased our dividend I think for the 10th consecutive year. Most recently a dividend payout ratio that ranges from 35% to 40%. We're a little bit below that right now, so there's some room there over time. And then focused on value accretive M&A, but we're very disciplined from a standpoint of the hurdles that we have. But we do look to do M&A, and we have over the years, as we've transitioned to become more of a solutions provider. And that will continue to be our focus in line with the strategy and in line with the re-segmentation.

And then of course, this year we're on track to deliver about $800 million, $950 million in cash and we'll look very carefully about where our shares are trading compared to the intrinsic value. In the first half, we bought back about $66 million of shares. We committed to buy back about $100 million of shares this entire year. But with the amount of cash that we're generating, we'll look at that very carefully to look at incremental opportunities to potentially buy back more shares if the opportunity presents itself.

We had a nice quarter 2. It was a record quarter 2 for us and we've had continued -- we've seen continued pickup in volume, and primarily in the Texture & Healthful Solutions segment, volumes picked up nicely. We're seeing continued year-over-year volume growth anticipated in half two and we had a pretty nice lap I would say in the second half in comparison to even the first half. We feel pretty confident about volumes in the second half. We see distributors, which were down a lot in 2023 as they were dealing with destocking, we see that completely out of the system right now, the entire chain, and distributors are restocking. Distributors are pretty profitable for us as well, primarily in the U.S. and in Europe. And our customer pipeline projects related to the re-segmentation we believe and the way we're segmenting our customers, and driving customer intimacy, those are improving. We hope to see the benefits of that from an innovation pipeline going forward. And all of that volume increase that we expect to see, which we saw in quarter 2 and we expect to see in half 2, will help with fixed cost absorption. We run large fixed assets, large plants. Last year with the destocking, we suffered from fixed cost under absorption. This year we are going to see and we are seeing the benefits of fixed cost absorption. And that generates strong cashflow just purely from the operating income and the EBITDA.

And then in addition, with corn prices coming down, our working capital is lower, so it's kind of a favorable set of circumstances in relationship to the cash generation. We have a solid balance sheet to deploy the cash and we really are, as I said, on track to meet our share buyback.

And what I would just want to leave you with is, it's been pretty significant for us to have re-segmented our business focus on Texture & Healthful Solutions. We have challenged ourselves as a company to really make sure that we can be viewed as a credible supplier, an idea spotter, a real co-creator within the whole textural realm. We hope to put this on display for many of you at our Texture Innovation Day November 14th at our World Technical Headquarters in Bridgewater, New Jersey. And again, that's our winning aspiration. With that, I will head over to Ben who will grill me I'm sure.

Benjamin Theurer: Well, I'll fire at you. All right. Very good, Jim. Thanks for that. A couple of follow-ups. Maybe to start off with the business reorganization and the benefits you've gotten from it, I mean obviously, you had many years of like just that regional approach of looking at the markets from like just a geographic point of view. Now, you still have a little bit of geography split in there, like the North America/South America business. But clearly, Texture & Healthful Solutions is global. Help us understand, how does this help you with your customers? Can you maybe share a few examples of excellence in execution with your customers where you win given the restructure?

Jim Zallie: Yes. The exciting thing about the re-segmentation is, we're really in the infancy of it. The benefits are just in the infancy. We just I think reported out in May for the first time the clean financial results based on the re-segmentation. And then the organizational focus to operate according to the segments with the leaderships that we've had to deploy, etc. We did this all coinciding with a strategic refresh using the play to win framework. And as it relates to global Texture & Healthful Solutions, the benefits really are about segmenting our customers. Looking at our global key accounts, our multinationals, where we do sell them on a global basis, so they procure on a global basis. Us being able to make decisions that have no regional parochialism is extremely important. But also, looking at just innovative opportunities that these customers represent across textural innovation, across sugar reduction innovation, protein fortification, and being able to segment how we see, based on their declared priorities, along with their categories, along with their market positions, along with their growth rates, how our ingredients line up and then how we can deploy best our resources to work on customer briefs which are increasing, which we reported in quarter 2. All of that is helping.

Also, what it's helping with is how we want to look at our R&D investments. And we are reallocating R&D spend across the business in comparison to how we restructured previously. And also, our capital investment priorities across the entire business, including food and industrial ingredients, is helping us make better choices for investments in reliability, the criticality of reliability in food and industrial ingredients, versus growth. We're having really robust, intense conversations that are allowing us to make wise capital investment decisions I think better than we had before.

And all of this is also enabling us to leverage a global operating model. About 3 years ago, we implemented a global operating model, maybe 5 if you go back to shared service centers. Originally for finance, but now aspects of HR are in there as well as marketing insights for example is done globally. And then of course, the big move was global operations, global procurement. And we're getting benefits from that that is able to be leveraged across now the new operating segments.

But just example of a customer situation is just where customers in the snacking category are looking really to innovate new, novel snacking textures. And it's allowing us to be seen differently, be viewed differently on what our total capabilities are to bring textural solutions and innovation there. Also, to quick service restaurants that have promotional offerings that differentiate based on texture. Really, it's helping us a lot, and the exciting thing is we're just really in the early phases or early stages of this.

Benjamin Theurer: Okay. You had in your prepared remarks a few comments on volume and how the momentum improved. Clearly, over the last call it 6 quarters prior to that, we had like this message still of destocking issue, and obviously a nice ramp up, particularly in Texture & Healthful Solutions, but also the other segments showed nice trend changes. How is the third quarter coming together? Is that still carrying over what you had in the second quarter? And how do you think about just the volume into the back half and then maybe a little bit of a sneak preview into 2025?

Jim Zallie: Yeah. It's too early to report volumes for quarter 3 because we just literally reported the volumes in quarter 2. But all that being said, we're sticking with what we said on the last earnings call which is we have volume momentum. And the volume momentum we believe will continue into the second half. And that's based on, again, also the trend line that we indicated in the last earnings call, 3 consecutive quarters where we're seeing pickups. And the customer briefs that we've talked about and the innovation that we see, the cocreation with customers. And we're also encouraged by the data that we're seeing from Neilsen, the data that we're seeing from Circana over the last 4, 8, 12 weeks that are showing, in the categories where our ingredients do find their way into, prepared meals, salad dressings, products like that, the volumes are picking up. And we also supply into all customer channels. Our ingredients find their way, again, into consumer-packaged goods companies, obviously the large multinational companies, the large global key accounts. But also, into private label. As consumers economize, and the other thing that I would say is that I don't think that what you're reading about or hearing about consumers economizing is something that's new. I think that what we believe is, consumers were economizing all throughout 2023. They continue to be ingenious in regards to how they're going to continue to economize. But that's been going on, and the movement to you may say more private label, or eating at home, for the ingredients that we supply, actually we can benefit from that. Because a lot of our products do find their way into products that are prepared at home and cooked at home. Volumes, we feel pretty confident, along with what we said at the earnings call, that the second half that it will continue into the second half.

Benjamin Theurer: Perfect. Obviously, you've talked about it, corn is an important input cost and prices have come down in a nice way. You tend to pass a lot of that onto customers. Help us understand a little bit the dynamic, cost versus pricing, and your new hedging strategy. Because you really managed to kind of flatten out that volatility to keep it minimal. What's different to a couple of years ago? And how do you kind of play this out going forward what you're seeing in the market?

Jim Zallie: Yeah, corn price obviously is important. Corn is obviously a major input cost for us. Corn prices have kind of settled into a range, just around $4, a little bit above $4. They're down for the second consecutive year from 2022, but regardless of where corn moves, our business model allows us to -- in the U.S., about 50% of our customer contracts -- and by the way, the US., when you think about it, the U.S. is 20%, 25% of our revenue. It's not -- we're a global company. But where the hedging kind of gets focused, just to bring clarity to it, about 50% of our contracts in the U.S. are fee based or toll based. And when we secure that contract, we hedge the corn, and we take out any risk associated to our margins associated with that. And then 50% is fixed, and then we buy corn forward and we have extended our hedging equally, both on what we call our head products as well as the coproducts over the last few years to take even more of the volatility out.

In the rest of the world, we still buy a lot of corn in Mexico, we buy a lot of corn in Brazil, and we pass along the pricing through adjustments every 3 to 6 months. There, the business models inherently have been strengthened in recent years to really protect our margins or manage our margins very steadily. Regardless of where corn moves, our business model enables us to secure our margins. Really, that's not something that we obsess about, is corn. We do obviously this year, I think in the first half or first quarter, or the second quarter I think, our revenues were down a bit because of adjustments in corn pricing. so that will happen. But our profitability was up 8%. That gives you an example of how corn tends to impact us.

Benjamin Theurer: Okay. You had this in the presentation and you pointed out you wanted me to ask more questions in digging into the Other businesses. There were a lot of things in it. And obviously it was different demand drivers, different trends. Maybe particularly in the plant-based, meat alternatives is not growing that much right now as was maybe hoped for. But at the same time, you have a lot of like the sugar reduction business in there, etc. Help us maybe understand a little bit where you are in the journey of these Other business lines and what kind of expected profitability you are seeing in this segment?

Jim Zallie: Remember, we have 4 segments. And one segment that can be a little bit viewed by an audience like you as a stepchild would be the Other category. It's not just a descriptive name, Other, but for SEC reporting purposes, the way the ingredients that are in there get categorized into this other category. But I want to make sure you don't misunderstand. The revenue in that Other category is about $400 million to $500 million. And it's comprised really of only 3 businesses. One is we have a 71% stake in a really gem of a business in Pakistan where we are the clear market leader in Pakistan. And that business is very profitable for us, it's about a $300 million business, so it's a very profitable business for us. It's significant.

And then we have a business in sugar reduction which is also profitable. The business that's been the drag on the P&L has been the investments that we made, a couple hundred million dollars in protein fortification. And we need to drive the revenue and we need to expand the utility usage of protein fortification. The good news on the protein fortification side is that there were tariffs that were imposed on Chinese imports of pea protein isolate earlier in the year. And the tariffs were very significant, 400%, north of 400%. And so not only prices, but availability has helped us with significant customer wins recently. We talked about that, that we reduced our operating loss nicely in quarter 2 and we expect for the full year we'll meet our target for the reduction in operating loss from that business.

But the Other category, again, strong business in Pakistan, very strong business in sugar reduction with high growth rates. We think protein fortification has high growth rates as well. The issue there is getting the leverage on the fixed costs by getting the volume growth, and that's coming after a couple of tough years. That hopefully clarifies the enigma a little around Other.

Benjamin Theurer: Okay, then I want to squeeze in one last one. LatAm, obviously it's a large business, $2.5 billion roughly of revenues, we've seen more recently a little bit more FX volatility, both the BRL and particularly the Mexico peso which you pointed out is a very important business for you. Clearly, that makes exports from Mexico more attractive because it's production, but then also for you from a reporting perspective likely a little bit of negative headwind because it's worth less in dollars. How should we think about the FX implication, particularly BRL and MXN, on your results and how it helps your business because it's exported?

Jim Zallie: The functional currency in Mexico pretty much is the U.S. dollar, so a little bit devalued peso actually helps us because of our cost base. When the peso gets a little bit stronger, it helps our EPS from a tax basis standpoint. It really doesn't have a significant material impact to our overall results historically. But the Mexico business, again, is very, very solid business for us. And the Brazilian reais, the movement there, we've had a lot of experience in passing through price increase, again, with the adjustments every 3 to 6 months. The LatAm business, again, for us is really very strong given number one market positions in those 3 regions, those 3 countries, within the LatAm region. It has -- the overall region, 670 million people, the average age is 31 years, and we're benefitting also in Mexico from nearshoring as well. Again, that is a real competitive advantage for us, the LatAm business. Super cash generative and we're very, very pleased with that position down there.

Benjamin Theurer: All right. Well, I guess we'll leave it here. Jim, Thank you very much.

Jim Zallie: Thanks. Thanks, everybody.