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American Vanguard Corp. (AVD)

Q3 2023 Earnings Call

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MANAGEMENT DISCUSSION SECTION

[Abrupt Start]

Operator: ...conference call. At this time, all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, Bill Kuser, Vice President of Investor Relations. Thank you, Bill. You may begin.

William A. Kuser
Director of Investor Relations, American Vanguard Corp.

Well, thank you very much, Alicia. Welcome, everyone, to American Vanguard's Third Quarter and Nine-Month Earnings Review. Our speakers today will be Mr. Eric Wintemute, the Chairman and CEO of American Vanguard; Mr. David Johnson, the company's Chief Financial Officer. Also assisting in answering your questions, Mr. Bob Trogele, the company's Chief Operating Officer.

Before beginning, let's take a moment for our usual cautionary reminder. In today's call, the company may discuss forward-looking information. Such information and statements are based on estimates and assumptions by the company's management and are subject to various risks and uncertainties that may cause actual results to differ from management's current expectations.

Such factors could include weather conditions, changes in regulatory policy, competitive pressures, and a variety of other risks that are detailed in the company's SEC reports and filings. All forward-looking statements represent the company's best judgment as of this date. Such information will not necessarily be updated by the company.

With that said, we turn the call over to Eric.

Eric Glenn Wintemute

Chairman & Chief Executive Officer, American Vanguard Corp.

Thank you, Bill. Hello, everyone. Thank you for joining our call today. This is a challenging time for American Vanguard and for our entire sector. Our stock price has been under heavy pressure, as has that of our competitors.

Accordingly, as per slide number 5, I want to first talk about what we are doing to improve our short and long-term profitability. I believe that growing profitability in current market conditions will require us to take strong, calculated measures. We are preparing to take those measures, including cost margin improvement initiatives, digital transformation and structural design review. We are confident that we, and our investors will be rewarded by them. After a discussion of these measures, I will give detail on the full year 2023 targets and our 2024 outlook. In short, we expect a rebound in Q4 and are optimistic about the upcoming year.

First, however, let's get into what we're doing to improve profitability. To start, a bit of background as necessary. Over the past 13 years, we have grown both in size and complexity. 13 years ago, we were essentially a domestic business that was largely dependent on the US corn market. Since then, as you will see on slide number 6, predominantly through acquisitions, our operations have grown into 21 countries, including six manufacturing facilities and three R&D centers. We have developed or acquired over 500 pending or issued patents and have increased our market access into more than 50 countries with a broad balanced product portfolio led by fruits and vegetables.

Due to our rapid growth, our next evolution [ph] area stays (4:09) is to strengthen the support of our enterprise with fully integrated systems and optimal organizational design. To that end, in the second quarter reached out to one of our board members, Mark Bassett, who has a strong history of improving profits in a number of businesses, to take a look at our operations in consultation with our senior management team.

Accordingly, over a 10-week period, Mark had open access to our day-to-day operations and met with executive leaders and business process owners. At the conclusion, Mark provided the company with a comprehensive set of recommendations. And senior management, along with another board member, Pat Gottschalk, crafted a transformation plan designed to drive growth while improving operating leverage.

We're pleased to announce we have begun implementation of the plan as follows. First, as per slide 7, we have reviewed the sales plan and operating expenses on a line item level with each of our department heads. We have focused on driving improvements in gross margin and achieving greater operational efficiency.

Further, I have given each department a target that, when achieved, would collectively add $15 million to operating profit and interest savings to our 2024 internal budget. We will make each manager responsible for these measures, track them over the course of the next year, and assess his or her performance based upon achieving these targets. These measures include a variety of parameters such as working capital management, greater factory efficiency, operating expense control, reduced raws and freight, and lower debt and interest expense.

Second, as you will see on slide number 8, we are implementing a complete digital transformation across all business centers and processes. At present, we have 33 business centers throughout the world. It is imperative that these centers work seamlessly to provide real-time data based on universal standards. To that end, we have chosen QAD's adaptive ERP as our system of choice to drive end to end scalability, standardization and integration across the globe.

Further, we have retained global business consultant Kearney Management to help us define and more streamline an efficient future state for our process owners throughout the business. They will be asking, what do you need to do to your job more effectively. To that end, Kearney and QAD are meeting leaders of our major business processes, including sales and marketing, factory operation, finance and human resources, to establish a business vision, aligned on improvement and priorities and to define the needs and identify the tools and processes that will enable us to meet our growth and business ambitions. This, in turn, will enable us to react faster and make better forecasts in the face of volatile markets and supply chains, climate and geopolitical shifts.

Third, turning to slide number 9, we are launching an organizational transformation in which we evaluate closely the way we are structured, how we are incentivized operate, and how best to gain greater efficiencies and operating leverage. We will need dedicated resources to lead a structural transformation process. To that end, Shirin Khosravi, our recently hired Senior Vice President of Human Resources, is leading the search to hire an experienced Chief Transformation Officer. That person, working with our internal team and external business consultants will evaluate and benchmark the capital requirements, staffing and performance of our various businesses. The CTO will in turn recommend appropriate organizational changes and in collaboration with Shirin will define key performance indicators and align functions and personnel to achieve business results. Through those efforts, over the course of the next 12 months, we will transform our current structure into a more efficient engine for growth.

Next, let's turn to David for his comments on our Q3 and year-to-date 2023 performance.

David T. Johnson

Vice President, Chief Financial Officer & Treasurer, American Vanguard Corp.

Thank you, Eric. Before moving on, we will file our 10-Q this afternoon. Moving to slide 11 with regard to our sales performance for the third quarter of 2023, the company's net sales decreased by 2% to $150 million, as compared to $152 million last year. Within that overall decline in sales, our US sales declined by 1% compared to prior year to $87 million, and our international sales decreased by 3% to $63 million. International sales accounted for 42% of total, which was in line with last year. The decrease in sales can mainly be attributed to destocking by customers managing their working capital levels due to high interest rates, the unavailability of one of our premium herbicides and, in our businesses in Central and South America, the influence of low cost generic products exported to multiple markets from China-based suppliers working within a strained economy.

Turning to slide 12. Overall cost of sales, which include higher – slightly higher net manufacturing costs increased by 4% and were 71% of sales in 2023 as compared to 67% for the same period of 2022. This resulted in a 13% decrease in gross profit to $43.084 million in 2023 from $49.638 million in 2022 and a consequent gross margin declined to 29% of net sales in 2023, from 33% in the same period of last year. The decline in gross profit for the three months ended September 30 is due to slightly lower sales as we managed through the global destocking process, unavailability of DACTHAL for the US crop business, and pressure from low cost Chinese-produced generic products in Brazil and Central America.

On to slide 13, which shows operating expenses for the quarter that were in line with the same period of the prior year. In the third quarter of 2023, as compared to the same period of the prior year, we experienced inflation-related higher wages, increased spending related to our SIMPAS system, and expanded state product registrations in Brazil, offset by lower legal expenses, reduced travel costs, and incentive compensation expenses reflecting our financial performance.

As you will see on slide 14, as a result of factors Eric and I have discussed, our Q3 2023 operating income amounted to $4.2 million as compared to $11.2 million last year. We recorded significantly higher interest expense as compared to last year due to both higher average debt and higher interest rates. The increase in debt level – levels is primarily a result of customer decisions to slow down purchasing from buying early to now buying as close to time of use as possible, effectively pushing working capital pressure back to manufacturers, such as ourselves as the markets are departing from the practice of holding greater safety stocks formed during COVID.

Key market participants such as big distributors and retailers are now vigorously resetting business practices such as inventory management to get back to pre-pandemic practices in the face of significant escalation in global interest rates. As the company has pointed out, this inflection point is driving markets we serve to extremely low levels of channel inventory that logically must soon start to refill in order to serve customer needs for the 2023/2024 season.

From a tax perspective, our effective tax rate increased to 158% from 31% last year. The change is primarily attributable to the low level of underlying profitability for the reasons just described and as a result of losses incurred at certain entities, primarily in Brazil, which did not result in a benefit for income tax purposes, as these entities continue to maintain valuation allowances against their net deferred tax assets. All these factors together resulted in a net loss of $325,000 this quarter compared to net income of $6.7 million last year.

On slide 15, you can see that for the nine months of 2023, our sales are down 10% and gross profit decreased by 17%. Our domestic sales suffered a decline in sales of 14%, while our international sales were down 3% as compared to the comparable period last year. The reduction in gross profit for the nine months ended September 30 is consistent with the three months and resulted from lower overall sales reflecting global destocking, unavailability of our premium herbicide, DACTHAL, and the effect of Chinese produced low priced generic products in our markets in Central and South America.

Operating expenses during the nine months to September 30, 2023 were flat as compared to the same period of 2022. We experienced an increase in wages due to inflation, increased travel activities at the start of the year that have since reduced, higher R&D expenses associated with in-field activities in support of our proprietary delivery systems, and international product defense and registration expenses supporting strong expectation – expectations for sales growth in 2024 and beyond.

These increases were offset by lower incentive compensation expenses related to our financial performance, lower legal expenses, as well as beneficial movements in foreign currencies in markets we operate versus the US dollar. Year to date interest expense increased significantly to $8.3 million from $2.3 million due to average debt levels, which increased by 33% as a result of elevated working capitals and interest rates that were more than double last year's effective rates.

Our effective income tax rate increased to 79% from 30% last year, primarily due to low underlying profitability, losses incurred at certain entities which did not result in a benefit for income tax purposes as well as certain withholding taxes. Overall, net income amounted to $540,000 compared to $23.5 million last year.

On Slide 16, you can see that at the end of September 2023 we reported inventories at $248 million as compared to $184 million last year. Inventory management is a significant focus, but the unprecedented destocking of products in our industry more than offset these efforts.

Furthermore, during the last four quarters, the company has suffered from some logistics challenges resulting in the unavailability of two of our premium products, Aztec and DACTHAL. Our customers were unable to buy these products during this break in supply. This year, the company has dealt with those logistics and regulatory challenges and is in position to supply all market needs for the 2023-2024 season. The graph shows inventory expressed as a percentage of the trailing 12-month sales. We believe that we will be able to reduce inventory to more normal levels as sales demand normalizes.

I'd next like to turn to the subject of cash and liquidity. As you are aware and we have depicted on slide number 17, interest rates have risen sharply over the past two years. As Eric has mentioned, this has given rise to global destocking activity. In light of these higher rates, adverse market conditions and supply chain disruption, about 45 days ago we approached our senior lenders, led by BMO, to negotiate an expansion of our financial covenant – covenants. As in the past, our lending group, which includes banks and farm credits that are very familiar with the global agricultural industry, was supportive and acted quickly to amend the senior credit facility to give us a secure runway through to September of 2024. During this period, interest costs will be half a percentage higher than normal; however, we will be able to revert to lower interest rates before the end of the period as our financial performance improves.

I will note that for the duration of the amendment period, we will not be repurchasing shares of common stock. Once we revert to the lower interest schedule, however, we will be poised to execute the $7.5 million share repurchase plan that the board had authorized earlier this year. We thank BMO and our lender group for their continued support.

With that, I will hand back to Eric.

Eric Glenn Wintemute

Chairman & Chief Executive Officer, American Vanguard Corp.

Thank you, David. As we mentioned in our earnings release and as reflected in slide number 18, we expect to see a rebound in the fourth quarter. We are 70% complete on our production of Aztec, our leading corn soil insecticide and sales are strong for the quarter. Similarly, we expect to begin supplying DACTHAL to our customers this week. These will be our first DACTHAL shipments in over a year. Again, these and other products are at historic lows with channel inventory.

In light of market conditions and our sales trends, we are targeting full-year 2023 revenue of between $580 million and $590 million, gross margins of 30% to 31%, operating expenses between $152 million and $154 million, and adjusted EBITDA between $55 million and $59 million. We will suspend judgment on net income for now and in further analysis of our full year global tax impact.

To put forth our performance in perspective and depicted on slide number 19, we reviewed recent financial statements of a set of our publicly traded peers and found that with respect to Q3 2023, those peers averaged a decline in net sales of 21%, while we were down 2%. With respect to net sales for year-to-date, those peers averaged a decline of about 13% while we were down about 10%. Extrapolating from our previous slide, we expect to be down about 3% to 5% year-over-year.

Before I turning to 2024, I want to give a few quick thoughts on the other growth initiatives. As you may have noticed from our press release yesterday and appearing on slide number 20, our Green Solutions business has announced an expansion of its partnership with NewLeaf Symbiotics, by which we will be collaborating to bring innovative biological solutions to key markets in Argentina, Brazil, Ukraine and China. NewLeaf brings us – brings to us its proprietary microbial library, proven research and development capabilities and best-in-class product offering of naturally occurring microbes. I'll also note that we expect that sales of our Green Solutions business will increase by about 10% in 2023 as compared to 2022. The addition of NewLeaf products will bolster Green Solutions growth in future years.

On the SIMPAS front, as per slide number 21, we're delivering 18 units to Brazil, which will be used by several of the largest growers in the country in this upcoming December-January planting. Further, we anticipate that north of 250 SIMPAS units will be utilized in the United States to deliver SIMPAS applied solutions in the upcoming 2024 season.

Let's close with my thoughts on the 2024 outlook. Within our industry, there has been a great sense of optimism about 2024. That said, I note that some of our peers have indicated continued channel inventory headwinds in certain geographical locations. However, according to a survey conducted by Umpqua Bank of 1250 executives at small and middle market agricultural companies, over half of the respondents expect improvement in overall economic conditions. Nearly 60% of that group expect increased revenues over 2024, and nearly 70% expect improved profitability during that same period. Granted, surveys are not the final word on how the future will unfold; however, there is good reason for sharing this optimism as we have in slide number 22.

First, the farm economy is strong, with relatively stable commodity pricing. Second, although the distribution channel has shifted its procurement patterns closer to time of use and they, and more important, growers need crop inputs to meet the demand for food, which is unchanged. Third, as a result of the 2023 destocking activity by our customers on the whole, channel inventory of many of our products remains low. Fourth, while not immune to the pressure of generic products, we feature a range of higher margin proprietary products that have kept their value and appeal in variable market conditions. In short, while there has been a recalibration of markets in certain regions and a shift in timing of sales order, the market is sound.

Consequently, based upon recent sales activity, preceding the 2024 planting season and the factors that I have just discussed, we're targeting 8% to 12% growth in net sales and 25% to 35% growth and adjusted EBITDA for full-year 2024. A closing note after measuring our performance initiatives, getting a more definitive sense of Q4 and refining our outlook on 2024 and beyond, we'll be holding a call in January to provide a further update.

With that, I'll turn the call over to our operator, Alicia, for any questions you may have.

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now be conducting a question-and-answer session. [Operator Instructions] Our first question comes from the line of Brandon Rogers with ROTH Capital Partners. Please proceed with your question.

Brandon Rogers
Analyst, ROTH Capital Partners LLC

Q

Hello. This is Brandon Rodgers on for Gerry Sweeney at ROTH Capital. I just had a few questions around the destocking progress. Do you have any visibility into how this is progressing? And do you feel you're through the majority of it? And what will it take to get inventories to expand again? Was it purely low interest rates or service requirements come into play?

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

A

Okay. Good question. So with regard to inventories and all – I can start with the US. We have pretty good visibility of what is in the channels we counted backwards with [indiscernible] (25:51) before it actually went out to the retail levels and the use of our products were up in 2023 versus 2022. And just Brandon maybe you might go on mute because we can hear you're typing. I think it's you.

Brandon Rogers
Analyst, ROTH Capital Partners LLC

Q

Oh, okay.

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

A

No problem. And as such again, you know our corn soil insecticides are extremely low, particularly our Aztec was down to about 7.5% and normal is probably in that 27% to 28% range. Our DACTHAL we mentioned that's been out. We haven't had product for sale for over a year, so that's very low.

As we look across our cotton products, again, you know, it was a decent year and we did not – we do not have much left in the channels. Our herbicide impact, I think we do have some inventory in the channel there. That's we did have [indiscernible] (27:05). But I think, you know, the initial issues of where inventories were large globally, I think herbicides were kind of up there along with nutrition.

So we have a little, a little effect there. But across the vast amount of our product line in the US, again, inventories are low. As we go outside or let's just say in the US with our non-crop business, our distributors have gone again as we mentioned, from maybe 120 to 180-day stocking down to 20 to 40 days. So, clearly, inventories are very low. We're seeing lots of orders coming in each day. But they're – they add up to be nice, but there are a lot of smaller orders. Same – similar in Brazil. What we might – and we're probably triple the orders that we're seeing on a daily basis. So, people are ordering kind of just what they need. And that's okay as long as the demand actually used is normalized, then it just means that we've got a lot more individual orders. So, I think that as you look globally. I'd look at some of the comments of our peers. I think that there is still pressure probably in Central and South America where we have seen more challenge to our margin in the last couple of cycles as lower cost of goods or goods that are oversupplied move through the channel. So, I don't know if I answered your question.

Brandon Rogers
Analyst, ROTH Capital Partners LLC

Q

Thank you for that color. And then if I could just ask one more kind of going off that. So, the Aztec and DACTHAL low inventory impacted the 2023 results, you said that you have – are in position to supply DACTHAL and Aztec for 2024. Can you quantify the total impacts for 2023, and do you believe this is recoverable in 2024?

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

A

So, 2023 on DACTHAL was in the $20 million range. The normal for Aztec might be in the $45 million to $50 million – maybe $50 million range. And so we had zero DACTHAL available since third quarter last year. We did have a pretty good third quarter of last year, which definitely affected this year's profitability if you look at the margins. And then, on Aztec, we basically had nothing available in Q4, and we had just under 30% of the market that we needed or the volume that we needed to service the 2023 season.

So, those are kind of the sales numbers. And the $20 million DACTHAL is probably a little higher than normal because, we knew we were having a supply channel issue and so it might be more normalized into the $15 million to $16 million range. But combined, it's a – it's a big number when you look at a company our size.

Brandon Rogers
Analyst, ROTH Capital Partners LLC

Q

Awesome. Thank you. I'll hop back in the queue.

Operator: Thank you. Our next question comes from the line of Chris Kapsch with Loop Capital Markets. Please proceed with your question.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Yeah. Good afternoon. So, I got a few buckets of questions, I guess. But curious on – on the gross margin degradation on a year-over-year basis, 33% to 29%. If you have a sense for if this was mostly a function of I don't know if you can parse it, but a function of your volumes being lower or was it a function of the competitive pressures from either the industry conditions or the aggressive exporting of the Chinese generics and that having an effect on your prices and therefore compressing gross margins. Any way to parse that? Just – and I'm just – I'm curious more generally, if you feel this pressure is purely transient and cyclical and unique, or is it something more structural in nature?

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

A

Okay. Thanks, Chris. If you look at the – let's use the nine-month-to-date, we're looking at about $25 million in margin differential. About half of that is due strictly to the $43 million in sales that we didn't have and a lot of that driven by the two products that we talked about. And then with those products, again, those are higher margin products. And as such, without those in our mix, you know, we're in the 60-plus-percent range. That definitely weighs down the average.

There were – from the Chinese pressures that – we saw that certainly in Central America. I mean, we've got a number of unique products, but there are more generic products that they have. They have products that come again from China. In Brazil,we have kind of an oil product that is a pretty big volume for us. But we – margins on that were very very tight and then also we have copper products that come from Norway. And there was strong generic products on copper that affected their margins down there.

So, I would say, as we look in the greenhouse, I think margins were holding strong. Australia was – has had pressure as well. They don't have a lot of generic pressure, but they do have generic similar chemistries that put pressure on their margins also. So that being said, I think it is a region by region recovery based upon what kind of channel inventories there are. It does look like the cost of generic products coming out of China seem to have stabilized. So I would expect that we would see as inventory does clear the channel and again, there are some pockets of inventory in various areas. I think some certainly and Bob you might comment on them with Asia or Europe. Europe we don't anticipate to any great aid. It's not a big area for us, but Bob just maybe you want to comment...

Ulrich G. Trogele
Chief Operating Officer & Executive Vice President, American Vanguard Corp.

A

Yeah. Hi, Chris. So, you have to realize that over 50% of our business is in the US. We got a pretty good view there, a transparent view on what the channel inventory is, Eric has described it. That's a real positive for us going into 2024, especially with the two products he described. We have a very light footprint in Eurasia where you have a lot of geopolitical disruption and some trade disruption. So we don't have any exposure there, so that's a positive for us.

Our Green Solutions business, as Eric has mentioned, we're launching new products, doing new deals, more to come here potentially in the next few weeks. Our technology is expanding. In the SIMPAS area Brazil, I'm excited about Brazil simply because that's a great market access tool for us. And as the systems go down there, we're going to see the yield results in the spring. As you know, they're in a different cycle than we are. We expect good results. And so, there'll be a lot of potential going into the end of 2024 in Brazil.

And then the market is down. So if you really read some of the text of the market in general I think we're going to see good acquisition opportunities both on the business front, but also on the talent front because some people will be downsizing, so we can strengthen our team where necessary. So, lots of good things happening, I think, for us in that sense.

I mean, we're cautiously optimistic simply because there is still a different buying behavior in the channel and the market has to reset with the higher inflation, and we're in the process of doing that. Sorry. Bill, I'll hand it back to you.

William A. Kuser
Director of Investor Relations, American Vanguard Corp.

A

Great. Chris?

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Yeah. So, questions on – thanks for that color, by the way. But focused on sort of the progression in fourth quarter and then into next year. The implied sales run rate is one that's never been achieved before for the fourth quarter against the backdrop where the buyer behavior is closer to time of use. So, I want to reconcile that. But then, even if you do, say, have that strong fourth quarter and then you're – you've given preliminary indication of EBITDA expectations or growth expectations for next year on that recovering EBITDA. So, I'm curious about the visibility around the fourth quarter. But then on 2024, if you take the midpoint of your range on EBITDA growth for next year of 30%, that would imply if you reach the call it $57 million in EBITDA this year, you get this – at 30%, $74 million next year. I'm sure – so that's a $17 million improvement. You're expecting $15 million, I think from the transformation plan. Maybe that's not day one, January 1, for a full run rate. So, I'm just wondering if you could parse these numbers, how much of the visibility and confidence around the fourth quarter run rate and what, if you achieve that level with just the confidence, what needs to happen to meet that 30% EBITDA growth and how much of this expected savings from a transformation plan feeds into that?

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.
A

So, again – fourth quarter, again, having not hit our estimates for the last four periods, again, we emphasize to our team, you've got to put more focus into understanding those numbers, communicating more with our customers, getting commitments, doing supply plans and obviously can't predict geopolitical problems that may occur. But just taking the fact that we had no Aztec in fourth quarter at all, and that's really generally our biggest quarter for Aztec. By not having DACTHAL for the last four quarters, those two alone lead us to be very strong on what we're going to see in Q4. I will say in October, you know, in our OHP and our AMGUARD lines, we saw a very strong quarters. We saw a good strong quarter in LatAm and Mexico in October. So, we've got a pretty good optimism of the outlook for Q4.

Going forward, yeah, the $15 million, there are some areas that we've identified that will be in place by January 1, but a number of them will be implemented during the course of the year and phased in so that we would see kind of the full effect of that in 2025 year. We also – we've got – we have a plan. We are – we're kind of really into our third year of trying to get our entire fleet on board with the same QAD system.

We're now focused more on pushing forward at a faster rate on that in 2024 so that by the time we get to end of 2024, we will be essentially where we want to be. So, yeah, there are potential upsides in what we've mentioned, if we're more attuned at implementing these cost saving measures as well as we'll have a better outlook of how well the 2024 years going to unfold, which is why we're scheduling that call probably the later half of January so that we can update on kind of the KPIs we've put in place to measure how we're tracking versus that $15 million, and what that outlook looks like for the balance of the year.

And then as well, our team gives a forecast, every business unit does the 10th of each month. So with regards to our 2024 outlook. And, again, budgets are – are begun in July of the previous year, we've been tuning that budget based the measures that we're taking. But then as we get into January, we'll know what happened in Q4, at least as far as revenue is concerned. And have a much better view of how that 2024 year is going to shape up.

Chris Kapsch
Analyst, Loop Capital Markets LLC
Q

Okay. That's helpful. And I had also maybe just a quick one for David on the covenant amendments. If you achieved that $74 million, I'm assuming you're in full compliance with the pre-amendment covenants. Is that accurate? I'm just wondering, like, what the nature of the amendments were and what you see in terms of – what needs to happen in order to get fully back in compliance. And just, if you could just talk about what the cost is for these amendments? Eric?

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.
A

So I'll just – just sort of clarify for David.

Chris Kapsch
Analyst, Loop Capital Markets LLC
Q

Yeah.

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.
A

So the amendments are essentially giving us more leeway on the debt to EBITDA ratio. I guess we we've set this up purposely so that if our Q4 goes according to plan, that we're in a position to pull ourselves out of that...

Chris Kapsch
Analyst, Loop Capital Markets LLC
Q

Right.

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.
A

...which would – which would save us 0.5%.

Chris Kapsch
Analyst, Loop Capital Markets LLC
Q

Right.

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.
A

So, again, kind of a function too of how much cash we collect at the year-end.

Chris Kapsch
Analyst, Loop Capital Markets LLC
Q

Right.

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.
A

Will determine what our debt to EBITDA ratio is. And then as far as the charge, go ahead and...

David T. Johnson
Vice President, Chief Financial Officer & Treasurer, American Vanguard Corp.
A

So, the cost was about $400,000. And then 0.5% on the interest rate for the duration of the amendment period which, as Eric just described, could be as long as through September of 2024. But we could exit it early if our forecast for Q4 and the start of 2024 come through well.

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.
A

And that $400,000, just so you know, it's not a hit in Q4.

David T. Johnson
Vice President, Chief Financial Officer & Treasurer, American Vanguard Corp.
A

Not in 4Q.

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.
A

It's amortized over the life of the remaining which takes us through 2026.

David T. Johnson
Vice President, Chief Financial Officer & Treasurer, American Vanguard Corp.
A

Yeah.

Chris Kapsch
Analyst, Loop Capital Markets LLC
Q

Okay. Thank you.

Operator: Thank you. Our next question comes from Wayne Pinsent with Gabelli Funds. Please proceed with your question.

Wayne Christopher Pinsent
Analyst, GAMCO Investors, Inc.
Q

Hi. Thanks for taking my question. Eric, so you touched on it a little bit there. Just curious on how quickly we'll be achieving the $15 million of cost savings. And you mentioned that you'll probably see the full amount in 2025, but just the cadence there, how much of it – because I saw in the press release you mentioned it was operational, but also interest savings. So, what's the breakdown there? And then have you identified any onetime or ongoing costs with that program?

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.
A

Yeah. Well, there'll be some capitalization certainly as we move faster on the QAD system. That is capitalized and kind of amortized over a five-year period. If you look at – each one of those comes with a different piece as far as phase in. So, let's just take raw materials for example, we've identified some contracts that we're going to have go in place in the first quarter. And as those benefits

occur in manufacturing, we actually – we'll see that pick up and it would be on margin, but we would see that occur in – as it gets sold. And normally, we kind of figure there's like a 90-day delay time from manufacturing to sale, but obviously, it depends on each SKU.

With regards to onetime charges, we're looking at that now. I think with our with our bank and our agreement with them, we – we can do each year, I think it's $5 million of onetime charge, which does not affect our adjusted EBITDA with regards to the bank, so I don't know if that gives you the color or whether you've got a clarifying question on that?

Wayne Christopher Pinsent
Analyst, GAMCO Investors, Inc.
Q

Okay. So, that – that's kind of what we can expect you going at that $5 million or under run rate in costs for this going forward?

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

A

Right, right.

Wayne Christopher Pinsent
Analyst, GAMCO Investors, Inc.

Q

Okay. Thank you.

Operator: Thank you. [Operator Instructions] Our next question is from [ph] Steve Helton (46:54), a private investor. Please proceed with your question.

Q

Okay. Hi, guys. I just had a quick question with the recent kind of business agreement between AGCO and Trimble. Does this complicate your sales program with your SIMPAS equipment?

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

A

Good question. So, Bob and I have had shares in AGCO but Bob has followed through and has probably a better insight on it than I do.

Ulrich G. Trogele
Chief Operating Officer & Executive Vice President, American Vanguard Corp.

A

So, three quick points, Steve. We see it as a positive. It expands our distribution network. AGCO has over 2,000 distribution points. So therefore, we see much more opportunities. We don't have to wait until the deal goes through. We've already started that process.

Two, we see a lot of cross-selling opportunities between precision planting and our systems. We've been working with AGCO for eight years. So, there is already a relationship in place. We'll just reinforce that.

And then I think, three, there's an action list we've already agreed with management to start in 2024 for the 2025 season. So, I hope that gives you color if you have a follow-up question.

Q

Yeah. No. That helps a lot. I was just kind of curious. I didn't know if AGCO had exactly something similar to the SIMPAS equipment or if you guys might fit in well with them.

Ulrich G. Trogele
Chief Operating Officer & Executive Vice President, American Vanguard Corp.

A

We're symbiotic.

Q

Okay. Sounds good. Thanks for the info.

Operator: Thank you. Our next question comes from Chris Kapsch with Loop Capital Markets. Please proceed with your question.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Yeah. I had a couple of follow-ups. Just so as you look through the fourth quarter and next year, just curious if you achieve these levels, like how much of your inventory will you be able to sort of liquidate and therefore working capital can be turned to or generate sorry, become a source of cash and what are the implications for your debt position either end of this year if you have that strong fourth quarter or through 2024?

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

A

That's a very good question. I mean, I think we're looking to reduce about $30 million in Q4.

David T. Johnson
Vice President, Chief Financial Officer & Treasurer, American Vanguard Corp.

A

Certainly more. $35 million, something like that.

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

A

Okay.

David T. Johnson
Vice President, Chief Financial Officer & Treasurer, American Vanguard Corp.

A

In inventory.

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

A

In Q4. I can tell you that part of the process that we're doing is understanding where we're deploying our working capital. It's not that it's something we shouldn't have been focused on at all times, but it's a completely different picture when you're paying 7% interest versus 2%, 2.75% interest. So, as such, there's been a strong look at each of our inventory items globally and targets that are set to bring those down dramatically from where they have been.

Particularly of concern are products that we may be storing that are lower margin products. And I think all along, as we've acquired some of these distribution businesses, we've told them, essentially we really are not focused on top line all we're driving is bottom line. So, if you've got low margin products, let somebody else sell them. Focus on building higher margin volume products where we need to, we're going to need to improve working capital deployment and deployment across.

So, we'll do a little more granular view and target specifically to each of the entities. And as we mentioned, we'll hold them accountable to get to those numbers.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Sorry. Just as a follow-up to that, would – and I don't know if this – is there any part of the transformation plan that examines and looks at your product SKUs that were – there might be some just simply aren't profitable and therefore might be candidates for rationalization or is the transformation plan really just focused more on operational measures?

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

A

We're focused on all aspects including margin justification of products that we would have in inventory. Again, our customer – a number of our customers kind of have gone to in stocking distributors to [ph] work alongside. And so as such (52:03), we've got to kind of reevaluate what we're going to do with our products. We're not – we're not a bank. We're not set up to be a bank. And we're going to make sure that as we deploy capital, we're getting the best return on our capital that we can. So, yes, we're examining all aspects.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Okay. And then one other question I perused Bayer, Monsanto results. I think it was this morning. And it was interesting they, the Seeds and Traits business is up and healthy and positive pricing and didn't seem subjected to the down – downbeat sort of backdrop. And then obviously for them, pretty pronounced pressures on [ph] quite the seed and (52:55) other crop chemistries. But so, curious, is there any sort of bifurcation in your portfolio along those lines where some of your products are more subject to those pressures than others. That's one question. Then, the second was they also mentioned that, and this is pretty well understood, I guess, by the broader market that given the corn-to-soy ratio that there will be a shift in acreage most likely from corn to soy. Just wondering what the implications of that, if any, on your portfolio on a normal year. Thank you.

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

A

Sure. So, as far as kind of generic, there's not a product that has more generic pressure than [ph] grasses (53:45), I believe, globally, and that's not a product that we play in. They have [ph] geoplasm (53:55) historic that's associated with that molecule. And so I think from a seed standpoint that remains healthy, which tells you that the demand is still there for planting and the crop inputs.

But we do not have a great deal of exposure to the generic. We're not immune to it. Obviously, as I said, we're seeing Central America maybe is having more pressure than some of our other areas. But with regard to your second part of your question, I'm sorry, what was – what was the second piece? I missed it Chris.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

It's on the acreage shift. Yeah.

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

A

Oh, yeah. The shift.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Acreage shift from the corn to soy.

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

A

Yeah. I mean, we're – we're effectively on – with our corn, we're effectively on – those are high pressure areas which typically tend to be corn on corn. They don't shift like you would see in some of the other areas where there are acres of even, let's say, in the south with corn, more corn soybeans shift or even in the cotton.

We have a growing portfolio of products on soybeans and we have our – our SIMPAS or Applied Solutions products on soybeans as well. So, I think that was part of our strategy was to add to our portfolio for SIMPAS soybean products as well as cotton products and peanut products so that people using our SIMPAS system could produce their own multi-crops.

But yeah, I mean going from 90 million acres of corn to 88 million acres of corn on the 2.5 million that we're involved in with our corn and soil insecticide really doesn't have much of a play. And ours is more based upon corn rootworm pressure.

And one of the things we're happy about this year launching into rice. Are we getting off this year with our BioWake product?

William A. Kuser
Director of Investor Relations, American Vanguard Corp.

A

Yes.

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

A

Yeah. Our BioWake product that will – that will also be for low corn rootworm pressure. And this is our first real commercial launch. You know, we did a – we did a trial launch last year and moved a fair amount of product in a very short window. But in addition to corn and soybean specific, we have peanut and cotton BioWake products and then our new product, which would be controlling in light rootworm pressure areas, So...

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Appreciate the color. Yeah.

Operator: Thank you. There are no further questions at this time. I'd like to turn the floor back over to Eric Wintemute for closing comments.

Eric Glenn Wintemute
Chairman & Chief Executive Officer, American Vanguard Corp.

Okay. Well, I hope this is the last quarter for some time to come where we do not meet expectations. It's been a long time, and I appreciate pressure that is upon us and the performance of our company, but we believe we've taken a very nice corrective new approach for – as we head into the Q4 into the 2024 season and look forward to giving you an update report when we get together in January.

So with that, thank you very much for attending. Bye bye.

Operator: This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.