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American Vanguard Corp. (AVD)

Q2 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Greetings. Welcome to the American Vanguard Corporation Second Quarter 2022 Financial Results Conference Call and Webcast. At this time all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions] Please note this conference is being recorded.

I will now turn the conference over to your host, Bill Kuser, Director of Investor Relations. Thank you. You may begin.

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

Thank you very much, Alexa. And welcome, everyone, to American Vanguard's second quarter and mid-year 2022 earnings review. Our speakers today will be Mr. Eric Wintemute, Chairman and CEO of American Vanguard; Mr. David Johnson, the company's Chief Financial Officer; and 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 can include weather conditions, changes in regulatory policy, competitive pressures and various 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 the date of this call and such information will not necessarily be updated by the company.

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

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Eric Glenn Wintemute

Chairman & Chief Executive Officer, American Vanguard Corp.

Thank you, Bill. Moving on to slide 3 on the agenda, but before we begin, I wanted to address our 10-Q filing which we did yesterday afternoon, last evening, and then we did our earnings release this morning. We have in the past been asked to file our 10-Q and give people a chance to read it before the conference call so that they could have more deep, in-depth questions and we also had in the past filed our earnings release prior to the market opening and during our call after the market, and we had advised particularly in times when we had unusual earnings that we should do them simultaneously after the market closed.

And so this year we met – this quarter we met expectations or exceeded expectations. We had our Q ready yesterday. Today is our last day to file the Q timely and we have had some glitches in the past with getting the filing through the system. So obviously we did not expect the kind of reaction that's happened today. We apologize in hindsight, it's definitely a mistake. We will not pre do our 10-Q in the future unless we have some other reason and we'll advise people of that. So with that said, I'm going to make a few comments, turn it over to Bill. I'll touch base on our growth initiatives and then we'll open up for questions.

So moving on to slide 4, the revenue growth is just reiterating the targets that we've stated back in March. Revenue growth in that 8% to 11%, gross profit margin 30% to 38% to 40%, operating expenses in that 31% to 33%, interest expense similar to 2021, tax in the mid-20s, debt to EBITDA ratio without acquisitions at year-end below 1, but with expeditions could be up as high as 2.5. Net income, we said target would be in the 60% to 70% increase. What we have gone ahead and done here on EBITDA is translated that 60% to 70% increase into an EBITDA percentage growth and that would be 24% to 28% for real numbers that would come into 79% to 81%, which coincidentally 79% was our top EBITDA of all time and that was in 2012. So just where we are at at the halfway point, our revenue growth obviously going faster than we had given initial target for.

Gross profit margins are above the profit margin range that we gave. Operating expenses are right in line with target. Interest expense down 40%. And at this point, I think unless we had some rather high acquisition before the balance of the year, we expect to be below our 2021. Tax rate, we're at 30%. I think now we're expected to be kind of at the higher of the mid-range right around 27% is what we're expecting for a full year. Debt to EBITDA currently at 1.33. We would expect to be below that 1, again without acquisitions. Net income for the halfway point, we're up 104%, which exceeds our target, and EBITDA right now we're up 40%, which again is ahead of our target.

Moving on to slide 5, just a couple of highlights to talk about. Again, revenues up $47 million. People have asked, okay, how does that relate to price increases versus volume. Of that $47 million, 45% or $21 million is related to price increases and 55% or $26 million is a result of volume increases. Our gross margins, as I mentioned, is up from 39% to 41%, a 2% increase. The key driver for that is factory performance, which is about 1.5% of that 2% gross margin increase. So factories are running well. It is a scramble that I'll talk about a little bit later, but we're doing well at this point.

Moving on to slide 6, so we've talked about supply chain challenges in each of the past two calls because it continues to be something top of mind. We talked about the availability of even finding the resources, the cost of those resources, if you can find them, and then the actual logistics of trying to get them delivered to the plant on time for manufacturing or for the entity for actual sales. So one of the things that we did and we have, we have schedules that we've laid out and we have schedules for production that are laid out in advance of the year. We're working on the 2023 schedule right now. And in that process, we basically kind of know generally when we're going to be manufacturing certain different products. But as we went through and I listened to peers having all kinds of problems, packaging, bottles, caps, pallets, all the inerts, some of the solvents and the intermediates, and

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again any one of those issues that – any one of those inputs that you don't have can cause delays and missing actual demand.

So what we stated is we were going to place orders for all of the raw materials we needed for the balance of the year and albeit give different delivery dates that were out. Just the concept of we're just not going to do kind of it just in time. We're going to purchase and bring in advance. And so our raw material inventory has actually doubled from where we were in 2021. And a lot of that is packaging and some inerts. The intermediates, we've laid out a schedule for everything through the balance of the year and intend to take those as needed.

So I mentioned before about forecasting cost and timely price increases. I think we've done very well at that particularly as you look at what our cost increases have been for this first half of the year. And in addition, those increases have been in advance and therefore our margins are being maintained well. With a number of oddities, a lot more airfreight, ocean freight being 10x the cost and just calculating all of that by SKU, building that into the cost of and again this is inbound freight, we're not typically doing deliveries by airfreight, but the inbound freight getting that built in so that we understand what our true cost of goods and that filters down to the marketing people and they're able to figure out how they're going to recoup the increased cost and then in-season factory production adjustments.

Again, I think I mentioned before we're having calls basically on a weekly basis looking at the schedules. I look at them every day and we try to make sure that we stay ahead of use, not necessarily ahead of demand, because people are pushing for products sooner than they actually needed just because of scarcity, but making sure that we're sticking with the demand.

Moving on to slide 7, I've got this in there just to kind of show kind of the effect as we entered the 2022 season, which really kind of kicks off in kind of September, October of 2021. We had very high demand from our customer base in the United States domestically, people looking to get ahead of materials. And as such, we carried quite a backlog going into Q1 of this year. So I think we did a very good job at, I'll say, managing the products that we had to our customer base, making sure that no one customer over-purchased what their needs were and therefore put a situation where we couldn't deliver to other customers. So we manage that well. Our customers in the US were extremely happy. We have been told by several customers that we have done the best job of all the suppliers in the US. So we're very proud of what we accomplished there.

Q2 subsequently, domestic was flat with the previous year, but then you see international kicking in in Q2 as we're seeing kind of, I don't call, people trying to buy ahead, but a little bit making sure that they've got product inside and meeting the demands that they have.

So moving on to slide 8, kind of looking out as kind of our core products and where we are, this is kind of the targets, I think, for where we believe we'll end up at the end of this year. Herbicides, which is the number one crop input, had been a weakness area for us, very strong in insecticides. So fumigants, [indiscernible] (00:13:22) kind of biologicals. But our herbicide market was kind of more to the corn market with our impact product line, but we made a concerted effort to expand that base. And as such, over the last four years, we've added 10 new products largely through acquisition. But we've expanded outside of corn to cotton, rice, sugarcane, soybean and canola. We're up quite a bit in the first half and expect year-end to be up about 40%.

So kind of growth in our core segment. Our soil insecticides, we expect up about 17%. It could have been – it could be bigger except we've had to push our factory in Alabama to produce our cotton to [indiscernible] (00:14:20) for an additional four weeks of production to meet kind of excess demand from what we originally thought the market would do. So we have that ability to shift and so doing we're pushing back [indiscernible]

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(00:14:37) from November start date to a December start date. And so we will position that [indiscernible] (00:14:43) that we have produced in December, but we're going to go into 2023 with pretty significant back orders on our soil insecticides.

Cotton, I mentioned [indiscernible] (00:14:56) very strong. And so we're looking to this year to be up about 29% there. So that's kind of the highlights. One of the things that we wanted to make sure of and let you know was with all of the sales that we've done what kind of in-channel inventories we're looking at. And so we have – we won't know for sure until we get the first, second week of September, but we did go out, we know basically what's sitting at the distributor level that we've got track of. But the key retailers we went out and physically spoke with them and talked through theirs. There are some retailers that have more inventory that they say they're going to keep that they do not want to return it. They're happy to have the inventory going in, but therefore that's not going back to distribution. So when we do the overall calculation, our best guess is that inventories in channel will be less going into 2023 than they were going into 2022. And obviously, that overall inventory being down signals a strong 2023 season.

Okay. So with that, David, I'm going to move on to you for your comments about our finances.

David T. Johnson

Chief Financial Offer, American Vanguard Corp.

Thank you, Eric. With regard to the continuing pandemic, a small number of employees around our global business have experienced COVID infections during the last few months. It's good to report that all have followed appropriate safety protocols and isolated, have worked remotely where possible, and have recovered or are recovering. Further, these isolated cases have not interfered with our operations.

Moving to slide 10, with regard to our sales performance for the second quarter of 2022, the company's net sales increased by 10% to $148 million, as compared to $135 million this time last year. Within that overall improvement, our US sales were comparable to the prior year and our international sales increased by 26% to $64 million. International net sales accounted for 43% of total net sales as compared to 38% this time last year.

Turning to slide 11, with regard to gross profit performance, our US crop business recorded an 11% increase in absolute gross profit on approximately the same level of sales as this time last year. This performance was largely the result of price increases that we implemented as inflation was taking hold and in anticipation of both higher costs of goods and increased inbound and outbound freight costs. In addition, as a result of strong, sustained global demand, we were able to run the factories closer to capacity and achieved better overhead recovery than in the same period of 2021. Overall US crop gross margins improved from 43% to 47%.

Our non-crop sales absolute gross margin improved by 3% on sales that were approximately flat quarter over quarter. The main driver for the improvement was related to better factory efficiency which I just mentioned. With regard to our second quarter international sales, we saw increased sales of 26% and an associated 28% improvement in gross margin. The main driver for this performance was strong sales of both the company's products and sales of third-party products through our international distribution businesses in LatAm and Australia.

Our international business has experienced similar increases in the cost of goods that we saw in the US and at the same time absorbed the adverse impact of a strengthening US dollar. The international sales team worked hard negotiating with customers to raise pricing where they thought it was possible and consequently maintained margins in comparison to the prior year. Overall gross margin percentage was at 31% for both the second quarter of 2022 and for the same period of the prior year.

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The graph on slide 12 shows the impact of the factory performance on our overall gross margin. You can see that in Q2 of 2021 the factory cost is 3.3% of sales whereas, as already mentioned, we've been able to run the factories at close to maximum capacity during the second quarter and have, as a result, achieved better overhead recovery. The Q2 2022 factory under-recovery amounted to 1.1% of sales.

Onto slide 13, which shows operating expenses for the quarter that increased by $5.9 million, as compared to the same period of the prior year. Our expenses were 33% when compared to sales. As we disclosed in our public filing, the company spent $1.8 million on proxy defense activities, which we regard as a non-recurring cost. Absent those costs, our operating expenses would have been $47.2 million or 32% of sales. That is an underlying increase of 10% on net sales up about the same percentage. The main driver for the increased operating expenses in addition to the proxy contest costs were $1.3 million in freight costs, which is primarily volume, logistics inflation and destination driven. Further, we have made some head count additions in critical areas and have also incurred spending on various activities that support our growing business.

As you will see in slide 14, our Q2 2022 operating income was 21% higher than the level reported for the same period of 2021. We recorded lower interest expense in the second quarter of 2022 as compared to the same period of 2021. There are two factors. First, we have generated cash in the intervening 12 months while spending very little on fixed assets and other acquisitions and have used the funds to manage working capital needs, continue the development of our precision application systems, investing in our manufacturing assets and in paying dividends. Secondly, we have benefited during the last three months from the tail end of the 2021 annual early pay program, which results in getting cash earlier than the due date for its accounts receivable.

From a tax perspective, our effective tax rate improved from 31.9% last year to 28.5% this year. This positive change was primarily impacted by a mix of jurisdictions where our profits were recorded, plus the impact of the vesting and exercise of stock that happened during the second quarter of 2022. All these factors came together in the bottom line. We are reporting $6.8 million in net income as compared to $5.1 million last year, a quarter-over-quarter increase of 33%.

On slide 15, you can see that for the first six months of 2022 our sales are up 19% and gross margins in absolute terms are up 24%. Both our US and international businesses have contributed to this exciting performance. Operating expenses increased primarily as a result of the proxy contest expenses. The growth of sales affecting freight costs, the adverse impacts of a strengthening US dollar on purchasing inventory for our foreign subsidiaries, increased incentive compensation reflecting improved business performance and increased accruals associated with deferred consideration related to our Australian business that was acquired at the end of 2020. That business has performed very well during the first two years which was the performance period for deferred consideration. Those costs will not be incurred going forward.

Overall operating costs were up 13%, as compared to sales which increased 19%. Operating costs were 32% of net sales, which is a significant improvement in performance when compared to the 34% we reported for the first six months of the prior year. Furthermore, absent the proxy contest expenses, the increase would have been 11% and our operating costs as compared to sales would have been 31%.

Interest expenses reduced by 40%, tax rate improved from 31.4% to 30.1% in 2022, reflecting mix of income in different jurisdictions and tax benefits from vesting and exercise of stock. Overall, net income increased by 104% for the first half of the year.

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Now I want to turn my attention to the balance sheet. Note on slide 16 that during the second quarter we increased cash generated from operations by 6% as compared to the same quarter of the prior year. On the other hand, we increased working capital primarily as a result of making conscious decisions to bring key raw materials and finished goods into the business earlier than previous years to ensure continuity of supply for the balance of this year and into 2023. During the quarter, we continued to follow several aspects of our capital allocation strategy including investing in our next generation packaging systems, SIMPAS, investing in our manufacturing assets and making dividend payments.

Turning to slide 17. At the end of June 2022, we have reported inventories at $182 million as compared to $175 million this time last year. We are working hard at managing inventories in the face of strong demand growth and, as I just noted, made decisions to procure inventories earlier to secure product for the rest of this growing season and into the next. The graph shows inventory expressed as a percentage of trailing 12-month sales, even though inventory increased in the second quarter of 2022 when expressed compared to sales, you can see that we continue to make long-term progress on this important business metric.

As you will see in slide 18, with regard to liquidity under the terms of the credit facility agreement, the company uses consolidated EBITDA as defined in the agreement to determine borrowing capacity. Our consolidated bank EBITDA for the trailing four quarters to June 30, 2022, was $75 million as compared to $59 million for the four quarters to June 30, 2021. At June 30, 2022, our debt is $101 million as compared to $149 million this time last year. The combination of higher bank adjusted EBITDA and lower debt results in a significant improvement in availability under the credit line to $163 million this year as compared to $57 million last year.

Turning to slide 19, here we show our progression on adjusted EBITDA from $31 million in the 12 months ended June 30, 2015, to $76 million this year. That is a compound annual growth rate of 16%. It is pleasing to note that we are close to achieving the company's all-time high which was $79 million in 2012. In fact based on our performance against the targets Eric has detailed, we expect to meet or beat that 2012 performance this year.

In summary, on slide 20, for the first half of 2022, we have increased sales by 19%. This includes having had early conversation with our customers about the near-term impact on finished goods of raw materials and logistics expense and, as a result, secured price increases across our global markets. We've been able to raise output from our factories in the face of strong demand year-to-date and for the forecast for the balance of this growing season and into next and thereby improved overall the recovery of factory costs. These efforts have enabled us not only to maintain but to improve margins, notwithstanding the inflationary and foreign currency pressures we are all experiencing. We have managed operating expenses which increased in absolute terms but declined when expressed as a percentage of sales from 34% last year to 32% this year. Our interest expense is down 40% compared to the first half of the prior year and our tax rate has improved. All these factors have come together to deliver a net income that has improved by 104%.

From a balance sheet perspective, accounts receivable increased driven by strong sales, inventories increased primarily as a hedge against what we see as a midterm challenge for supply chain, and debt is $49 million lower than this time last year with improved availability under the line.

With that, I will hand back to Eric.

Eric Glenn Wintemute

Chairman & Chief Executive Officer, American Vanguard Corp.

Thank you, David. Moving on to slide 21, with SIMPAS in 2022 at 81 new systems, one of those being in Ukraine, believe it or not, that were put into use this year. We're waiting results of yield to show what kind of improvements

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we've done in the fields with the materials that were applied, both prescriptive and full, but certainly more accurately with the new systems and meters. For this upcoming year, we are targeting somewhere between 150 and 200 new systems into operation for the upcoming year. And of course, that tax on on top of the 81 and we had some systems through the year before. We've looked at our forecast and right now it looks like we're still on target to achieve the previously stated forecasts. And we'll discuss that a little bit more in a moment.

Moving to slide 22, again, a lot of what's going to drive the success of SIMPAS is the availability of different products that can go through the system and you can see 2023 will be pretty robust as we add a number of new products that can go through the system. I will say it in 2022, we're very pleased to get iNvigorate and Azotic from [ph] Aveda (00:30:14) and have those available. We think in 2023 use of those on untreated acres is going to be up pretty substantially. One of the reasons, I think, driving these are both nitrogen fixing plant stimulants. And as such, I think the whole carbon piece has moved – continues to move forward carbon reduction. There's going to be higher incentives for growers to show less nitrogen being put on their fields. And as such we've said before, we believe that SIMPAS plus the ULTIMUS system allows the grower to be able to measure, record and validate and will be a key part of them being able to collect those carbon credits.

Moving on now to green solutions, so we had a good Q2 up 62% from where we were in 2021, strong performance. Central America, India, Australia and Mexico all did well. We've targeted going from $40 million last year to $52 million this year and that looks to be on track. And again this is with basically our organic growth. We have had no new acquisitions in that area in 2022.

Moving on to slide 24, I will say that we've had and are having conversations with other biological companies that are looking to us to do marketing and sales of their product lines rather than building out their own team and basically these are geographical arrangements. We look forward to announcing progress there in the near future. I mentioned the Azotic Envita and iNvigorate. We're going to be filling those at our factory in Clackamas, Oregon and making those available for this upcoming season in 2023. Our AMGUARD/Envance technology that we've got for specifically our bio-herbicide trials. The consumer trials are underway right now. The professional trials have been completed, the initial ones, and look very positive. So we're very excited by this non-select bio-herbicide that we think can be a big part of not only consumer but professional use. And we're even comparing this now for crop use as well.

And finally on green plants, which is our micro fertilizer stimulants. We've had sales in China. We've got kind of registrations completed in Spain and we've got more growth initiatives scheduled for 2023. So all in all, green solutions looks to be on track, moving on to our final slide, and we measure out our 2023 to 2025 targets look to be on track from our core business. We are tracking well certainly versus that targets that we've got for 2023 and 2025 for our green solutions. Again we're reiterating that we feel comfortable that we are going to hit that $70 million target next year and be able to double that to $140 million by 2025 given the pipeline that we've got. And then finally, our SIMPAS piece again looking next year for approximately $28 million in sales, growing that dramatically to $113 million over the next couple of years after that.

So with that, that's kind of reiteration of our strategic objectives, and Alexa will open up to any questions that maybe from our audience.

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QUESTION AND ANSWER SECTION

Operator: Thank you. At this time, we will be conducting a question-and-answer session. [Operator Instructions] Our first question comes from the line of Gerry Sweeney with ROTH Capital. Please proceed with your question.

Gerry Sweeney
Analyst, ROTH Capital Partners LLC

Q

Hi. Good afternoon. Thanks for taking my call.

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

A

Hi Gerry.

Gerry Sweeney
Analyst, ROTH Capital Partners LLC

Q

Eric, just in your prepared remarks and actually I do apologize for the drop for a minute [indiscernible] (00:35:27), but it sounds like you have some pretty good confidence in your targets for this year and looking into next year. Maybe you can talk about your visibility that gives you confidence and then the areas that you think you're most excited about and then juxtapose that maybe some of the areas that you might be a little bit concerned about just so we have a little bit better view of the playing field for the next 6, 18 months per se.

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

A

Yeah. So the things that I think make us feel bullish, we made good market share gain in a higher demand market and we delivered well. So we think we're going to have good momentum going into 2023. I mentioned the inventories in channel. At this point, we're not aware of any issues there, which again, I think, bodes well for the upcoming season. Our belief is that commodity prices and therefore demand will continue to be robust. So I feel confident, I guess, at this point as we're getting closer to drilling down on Q3 and Q4, a much better level of confidence as we've gone through each of the SKUs and kind of making sure that we've got adequate supply to meet those demands. It hasn't been easy. I mean we've been shifting back and forth between packaging of certain products and manufacturing of certain technicals. I mentioned earlier that our plant in [indiscernible] (00:37:14) insecticides, but we feel confident we're going to be able to meet the demand for 2023. So those are kind of the drivers that make us have more confidence in our final numbers for the year-end.

Concerns, there's the economy, interest rates, political positions. So I think I mean people out there have some nervousness about where things are going.

Gerry Sweeney
Analyst, ROTH Capital Partners LLC

Q

Yeah.

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

A

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But, these are not luxury goods that we're supplying. We're supplying for food supply. And so we don't see commodity prices dropping dramatically. So we think that growers will continue to do their job. Even in Ukraine, I mean, I think they're expecting 65% of the crop to be harvested and exported or used internally. So the wars are not being fought in the farms and that's obviously the extreme of what we're dealing with elsewhere in the world. So I think farmer health should be strong. And so overall, I guess that's my pluses and minuses.

Gerry Sweeney
Analyst, ROTH Capital Partners LLC

Q

Got you. And then the other thing is, things are going well. It sounded as though maybe capacity or utilization potentially getting tight. Two questions or a question around that what it sounded like I was hearing was, there's some tightness on the capacity. Are you at a point where you need to expand capacity and really the follow-up to that question [indiscernible] (00:39:18) how much does it really cost to drive additional utilization or capacity in some of your facilities? Are we talking big numbers or is it relatively manageable?

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

A

So we have tightness in some areas. Our granule capacity at Axis, the formulation and packaging there. We're not able to make everything there that we would like, but we're going outside for it. So there is outside capacity. We are looking at going from a batch process there to a continuous process which would expand capacity about 25%. That's looking at – that would be maybe a couple of million dollars of CapEx to do that. So, fumigant, we're fine with. We've got additional capacity there. That's our single biggest product both from revenue and from volume.

On the technical side, at Axis, we bought the plant. It manufactured a product called Fortress was kind of the main ingredient that was done there. We've added six other AI synthesis components there, but we're having to make some decisions between our most profitable products there. And so we do need to look at expanding. I think the original product, Fortress, was a granule, 5% granule. We have a 15% granule. But the real growth opportunity there is for our product called [ph] Index (00:41:11), which is a liquid formulation of the Fortress or chlorethoxyfos. That is probably the biggest squeeze point we have. The capacity is not particularly large running through the unit and therefore we're better off from overall profitability on running products like Azotic and the [indiscernible] (00:41:38) through those facilities.

So our Counter and Thimet which again are growing really well. Brazil has gone off in a big way and they're awaiting their soybean registration which we'll take even further. So that's probably the number one performer for nematodes in Brazil, so we expect that to grow quite a bit. It could get to the point where we're at capacity. I think we're maybe about 75% this year. So we've still got room to grow. But those are kind of the overall pieces. But I can tell you, as a manufacturing guy, I love this kind of challenge, much happier with where we are today than where we were in 2014 when all the inventory was sitting in the channel and we were having to deal with two-, three-year plans to get that down into a reasonable position, so we think we'll...

Gerry Sweeney
Analyst, ROTH Capital Partners LLC

Q

Sure. I mean good problems. Good problem, yeah.

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

A

Yeah, exactly, right.

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Gerry Sweeney
Analyst, ROTH Capital Partners LLC
Q

Yeah. Got it. I'll jump back in queue. I appreciate it. Thanks.

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

Okay.

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

Chris Kapsch
Analyst, Loop Capital Markets LLC
Q

Hi. Good afternoon. Just a couple of questions. So the gross margin improvement that you showed, I guess, in the quarter, also year-to-date. Just curious if you could parse out how much of that is from the benefit of better factory overhead absorption because you're also, I think, getting pricing that's ahead of raw material, so I'm wondering how much that contributed and if there's anything else that we should be aware of mix or some other nuance that's contributing to the gross margin lift.

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

So as I said, I think from a pricing standpoint, we've done a very good job at staying ahead. And I think what we're looking at on that slide that showed we got about 1.5% gross margin lift from factory performance. And so that's 75% of it. The balance coming from pricing and mix combination. So we had, I would say, some of our products again inbound freight and some of the things that we did to get products and certainly added to cost. So I don't know that we got 100% of that covered. But if you look at where we are versus some of our peers, I think we did a really remarkable job at getting through the price increases that we needed. We did not – we were not – it was a much more difficult position in some of the international markets. There were inventories of products, I'll call them competitive products not necessarily the same active ingredients, but competitor products that were kind of long in some countries. So for those areas, definitely more delay that pushing through price increases. But overall we are pleased with what we've been able to do.

Chris Kapsch
Analyst, Loop Capital Markets LLC
Q

Okay. That's helpful. And I think in one of the slides you said year-to-date revenues up $47 million versus first half of 2021. Can you parse that out roughly half volume, half pricing? And so that looks like just rounding out around 9% volume, 9% price. So if it's 9% volume growth year-over-year and you expect channel inventories to be kind of lower than they were last year, lower than normal than might even suggest, then the application volume growth year-over-year is better than that. And so my question is that seems like it's definitively above sort of market growth even in a robust year. So wondering what's contributing – which products, what's contributing to that above-market growth, if that's an accurate characterization? And are you gaining share in what areas and just what do you think the ability to sustain some of that perceived market share growth is looking forward?

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

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Yeah. So your assessments are correct in the way we see it. I kind of highlighted one area, which is herbicides that were up 40%. There was a lot of shortage that's in the market this year globally and a lot of shifting around. And that's where, again, it turned out to be very prudent the acquisitions we made 2018 through 2021 and we're in the right place, right time to deliver herbicides. And so these are not the glyphosates and the Glufosinate, although one of our 10 products is taking our Topramezone impact and putting it with Glufosinate. So I think our customer base was very pleased with our ability to deliver herbicides to them. I think also these products are unique in their performance and as such we think we've earned kind of a longer market share. In fact, we believe we can grow them very nicely going forward. So that's going to be a big upside for us is the herbicides that we've invested in. And some of these are investments and some of them are through our core growth message, what we call, IRC program where we've identified opportunities to take our current compounds and marry them with other active ingredient to build out another niche market that separates us from our competition.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

So just to follow up on that, though, so the demand for the herbicides is partly because of shortage of conventional herbicides. I'm thinking it's pretty well known that [indiscernible] (00:48:20) say it was kind of short this year, at least earlier in the season. So are you benefiting from demand for these herbicides solely because of the market being short, some of these conventional herbicides or is it really the efficacy of a differentiated offering that you have that's helping drive kind of above-market growth?

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

A

Yeah. I think what we've been able to do is we've been able to accelerate the penetration with these products, so [indiscernible] (00:48:52). We expanded Canada greatly. We expanded the US greatly with our Envoke product that we took over the second half of 2021 from Syngenta. They had kind of some limited – they watched the kind of market kind of diminish as they weren't focused on it. And as I said, probably you can do a better job with it and we can. We're not – we're down to a few million. Well, we've not only expanded the sugarcane piece, but our team did a really good job of getting this reintroduced back into cotton. And so the results were stunning and the people were thrilled. So I think the shortage of herbicides has helped us move forward the program that we think we'll get to anyway with penetration. But it's just accelerated with the momentum of that we think will carry well into 2023 even with better availability of some of the normal herbicides.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Got it. And then sort of last topic for me, so I appreciate you taking the time, but so you mentioned SIMPAS plus ULTIMUS as a potential for growers to kind of monitor track their – I guess...

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

A

Production [indiscernible] (00:50:27)

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Yeah – the ability for them to decarbonize I guess. So I was just curious the build back [indiscernible] (00:50:36) I guess what they call the Inflation Reduction Act. I mean there's [indiscernible] (00:50:42) what I could and there's some buckets that look like they're targeted towards the ag market and obviously there's a addressing climate change theme to the legislation. And one bucket referred to as climate smart ag, there's a $20 billion they're

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talking about for farmers for various things. But one of the areas is incentivizing sustainable practice. So long way of getting to my question which is, is there a play through this legislation that you see where somehow you could accelerate adoption of SIMPAS plus ULTIMUS as a means for farmers to adopt that practice.

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

A

Yeah. I kind of hit that a little bit when I mentioned the Envita and iNvigorate that helped the uptake of nitrogen. Again I think there people, growers have different mindsets on this, but generally most of them feel their land is their most important asset. There is certainly going to be a lot of upsides to reducing carbon footprint not just from a social standpoint, but actually from a financial standpoint. So I saw that as well that $20 billion I thought, okay, that's another kick start again to farmers is what can you demonstrate and with the high cost of the fertilizer inputs, it's really a win-win for the grower. If he can reduce nitrogen by 50% by putting biologicals that help with nitrogen uptake in the root system and get paid for it on top of it, that's a strong incentive.

And so, yeah, we believe SIMPAS can be a big part of that, not just from being able to apply the products correctly and judiciously. And again, they have – the most farmers have maps of – they're applying somewhat prescriptively now with their nitrogen, but they have areas where they know they've got nitrogen deficiency areas. And if you apply the biologicals, that will help with nitrogen uptake in those areas and reduce your nitrogen, that's a totally different approach than just putting these products out across the whole field. So again, prescriptive application, I think, can give a much higher return on investment for people looking to reduce their carbon footprint.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Interesting. Just to follow up on that. So nitrogen reduction, given the carbon intensity of manufacturing synthetic fertilizers is – I assume that's like a low hanging fruit in terms of decarbonizing the ag end market. And you mentioned a couple like obviously prescriptive application of nitrogen, the biologics that improve the efficiency of the uptake. Just curious, like across the broader industry, what are some of the alternatives. Seem to remember years ago maybe there was some genetics that were going to help the plant consume nitrogen, more efficiency. I don't know if that got anywhere, but what are the other sort of mousetraps that you would be competing with in terms of helping farmers achieve that goal if that's something that kind of gains momentum. Thank you.

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

A

Yeah.

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

A

Yes.

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

A

Bob, go ahead.

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

A

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Hi, Chris. I think you're going to see what you're saying. There's some of the seed companies breeding for better nitrogen uptake. Yes, it depends on how successful you are, but I think it's going to be a combination of both breeding and input, primarily either in furrow, like through a SIMPAS application. I think some companies are also posting full-year application, but it's yet to see how effective that is. But I calculated a 20% reduction, depending on what you think as the price of nitrogen in a given period of time is around a $5 billion market, that could essentially become available. So everybody is racing to that. You see companies, some of our strategic competitors, are launching products. We feel SIMPAS is the optimal device to not only deliver the nitrogen fixation solution, but also to measure the effect of the nitrogen fixation solution and that you're correlated with yield. We have a model which basically calculates that out for the farmer and it's quite unique and I think we're going to see some good things there for our company. On top of that, just to give you a little color, we've submitted two grants to the USDA. We'll be submitting further grants. There are also state grants. And our strategy here is to have them either subsidize the adoption rate of SIMPAS as a tool, but also perhaps give money to the grant universities to utilize SIMPAS for more of a biological product development.

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

A

Yeah. And I think also our team shared with us what I hadn't quite understood. One was measuring the inputs going in for nitrogen uptake products, but also using ULTIMUS to measure the amount of nitrogen that goes through the field or a fertilizer. So putting that on so you can actually go from railcar or bulk storage tank going through and actually measuring how much fertilizer of what fertilizers are going through the farm. So one is, hey, we're doing this and that's reducing our nitrogen, but then you can also confirm it with the amount of nitrogen or phosphorus or any of the other synthetics going into the field. So kind of a double-edged verification. So it's really exciting.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Great color. Thank you.

Operator: Thank you. [Operator Instructions] Thank you. Our next question comes from the line of [ph] Andrew Lester with Harla Capital (00:57:37). Please proceed with your question.

Q

Hi. Thank you for taking the question. I'm relatively [indiscernible] (00:57:44) but some questions like what percentage of the business is represented by Ukraine?

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

A

Oh, very small. I think we've got – we were about $1.4 million, looking to get to $2.5 million this year and last heard I think it was right about $1.8 million is what we thought we were going to do this year. So not a big piece, but we do have people there. We think it's a good market for SIMPAS. And as mentioned, we did have a system that got up and used for planting and planting time this year. So not a huge exposure. But I think we got [indiscernible] (00:58:33)

Q

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It's also I mean – with sort of due respect, the stock sort of got crushed today 10%, 25%. And I didn't see any – I went through the Q and obviously the slides and everything. I didn't see anything glaring. My guess is that in light of the global dislocations, some investors might have thought this was the time to, let's say, crush it in terms of earnings beat, a sales beat or whatever, and to have a more moderate to beat into sort of undercapitalized the opportunity. So if the world becomes somewhat more normal, how would you deliver sort of an exciting upside going forward? And I know you have about 600,000 or 700,000 shares left from the buyback that you can now take advantage of. Is there any thought to increasing that in light of what the level of the stock right now?

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

A

Yeah. So we had – as you mentioned, you're correct, we had about 670,000 shares available into that buyback. We purchased about 48,000 shares today. So we've got about 620,000 shares left. And that will continue as long as we're at or below $20 a share. I think, yeah, given the situation. I mean, we're not – I mean, I'm not – I don't think we clearly understand what the reaction was in today's market. Again, we met or exceeded expectations. We've now discussed where EBITDA people asking before, when can you get back to 2012 levels. So, we're hitting that this year. We've put a target out there of $155 million three years from now in 2025. So I think we're very excited by the way the company is performing. So the only thing that we saw that was unusual, again, that we can point to is that we released our Q and our earnings before we did our conference call. So we'll see what happens tomorrow. But as you rightly pointed out, there's nothing in there that would cause alarm from our standpoint.

Q

Right, I just thank you. As an all-time investor, I think it catches certainly people off sites. They were looking at your emails. They understood that you were going to have the call after the close. And although you – as you explained, you had the best of intentions, letting people read things, process it and sort of be more prepared, I think it sort of behooves you to conform the convention like others and sort of get it all out there at the same time. And maybe that could avoid some confusion and help things next time.

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

A

Yeah. No, as I mentioned, it won't be a move we'll make again.

Q

Thank you for your time.

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

A

Sure.

Operator: Thank you. Ladies and gentlemen, we have reached the end of the question-and-answer session. I will now turn the call back over to Eric Wintemute for closing remarks.

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Eric Glenn Wintemute

Chairman & Chief Executive Officer, American Vanguard Corp.

Okay. Well, again apologize for the activity in the market today. I've been at this a while and it never ceases to amaze me how things happen. I don't think this is an overall market reaction of the industry or anything along those lines, because we're clearly standing out here versus our peers. So again, my best guess is people were taken by surprise by having the Q out in advance and it triggered some concern. So, hopefully those concerns are now answered and alleviated. We'll be following up with investors after this call and talking through any concerns that are there. So very appreciative of – and we had a large crowd today which would be expected. But I appreciate you all taking the time and we look forward to giving you further updates. Bye.

Operator: This concludes today's conference and you may disconnect your lines at this time. Thank you for your participation and have a wonderful day.

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