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American Vanguard Corp. (AVD)

Business Update Call

CORPORATE PARTICIPANTS

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Analyst, ROTH Capital Partners LLC

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MANAGEMENT DISCUSSION SECTION

Operator: Hello and welcome to the American Vanguard Business Update Conference Call and Webcast. [Operator Instructions] A question-and-answer session will follow the formal presentation. As a reminder, this conference is being recorded.

It's now my pleasure to turn the call over to your host, Chairman and CEO, Eric Wintemute. Please go ahead, sir.

Eric Glenn Wintemute

Chairman & Chief Executive Officer, American Vanguard Corp.

Thank you, Kevin. Good morning, everyone, and thank you for joining this call. Let me start by putting a point on what we had outlined in the press release that we issued on Friday. We expect our full year 2022 financial performance will exceed that of 2021 in all material respects. Furthermore, we expect to achieve significant growth and profitability in 2023 over 2022, and we will be giving you specific performance targets for the 2023 year in about six weeks on our March earnings call.

In the fourth quarter, we were forced to delay roughly $15 million of high margin sales due to a supply chain disruption. Now that we have fixed the supply disruption, we expect to largely recoup the sales that we lost in Q4, such that they will shift forward and benefit 2023 performance. With a strong balance sheet and favorable market conditions, we believe we are poised to enjoy strong growth in all metrics for this coming year.

I'm showing you here the Safe Harbor. Okay. So, on slide 3, the global supply chain has been in unsettled state for the past three years due to the pandemic and shifting buying practices. At one time or another, we have witnessed shortages in containers, ships, warehouses, and trucks used to transport many goods across multiple sectors. Within our industry, these factors have interrupted production of raw materials and intermediates, particularly those sourced in Asia. In spite of these conditions, our supply chain team had succeeded in sourcing virtually all raws, intermediates and packaging without interruption over the past three years of the pandemic.

I am proud of the work that we have done as this has required near constant attention and pre-planning. However, in the fall of 2022, our domestic supplier of a key intermediate that is used to produce Aztec, our leading corn soil insecticide, was unable to start production due to capacity constraints. This persisted for several months. Accordingly, we positioned one of our China-based suppliers to commence production of that input. Synthesizing this intermediate involves a very complex, multi-step process.

While technically capable of filling our requirements, the Chinese supplier was caught in continual lockdowns from China's zero-COVID policy, which, once lifted resulted in nearly everyone in the facility contracting COVID. This culminated with a mandatory closure of the entire industrial park during the New Year. At the return of its full workforce, our Chinese supplier has resumed manufacturing the key intermediate. Also our domestic supplier is back online.

Further, we have started synthesis of Aztec at our own facility in Alabama. As we continue to receive this key intermediate, we will be producing Aztec over the next 75 days or so. In short, we have prepared the supply chain and are looking forward to returning to business as usual.

In parallel, let me focus on how we are managing this disruption with our customers. We are a leading manufacturer of corn soil insecticides. As you can see on slide 4, the many brands that we market in the US and abroad. As it became clear that our inventory of Aztec was going to be impacted by supply disruption, we began working with our customers to meet the growing needs through increased supply of these other CSIs, especially Counter, Force and SmartChoice.

While unable to make up for the sales of Aztec that we anticipated in Q4, consolidated net sales for the period were equal to those of Q4 2021. Further, we have now orders in hand at Aztec in the amount that is three to four times higher than what we typically have during the first quarter. In short, subject to achieving full production, we expect the net sales and gross profits that we anticipated from Aztec in Q4 to shift forward into Q1 and Q2 of 2023 as we supply growers in time for the upcoming planting season.

Before looking forward, let's take a quick step back to recap last year. As per our press release, we have revised our 2022 performance targets on slide 5. The overarching point here is that despite the temporary unavailability of our leading high margin corn soil insecticide during the fourth period, we generated sound financial results on a full year basis. Bear in mind that the figures I'm about to discuss are based upon preliminary unaudited financial data.

Going from top of the P&L to the bottom, our revenue is forecast to grow at about 10%, which is within our targeted range. Similarly, gross profit margin at 40% and OpEx as a percent of sales at 33% are also in range. Interest expense will be about 5% above the target for 2021, which, given all of the rate hikes that occurred over the course of this last year is excellent. The debt-to-EBITDA target is within range and well below our 2.5 times max rate. Net income is not yet known as it will depend upon tax and final accounting. And our adjusted EBITDA at 15% to 18% growth rate will fall below the range previously given. Please be mindful that we're reporting on 2022 estimates versus our own targets. When we look at how 2022 stacks up against 2021, we expect that our financial performance will exceed the prior year in all material respects.

Before turning to the 2023 outlook, let me note that over the past several quarters, we have placed emphasis – an emphasis on maintaining a strong balance sheet. As you can see on slide 6, we ended 2022 cash with cash available in the amount of $198 million. Further, our debt net of cash was $31 million as compared to $36 million at the end of 2021. In addition, our net average, which is debt net of cash divided by EBITDA, was 0.42. In other words, we started the year virtually debt free with ample cash and cash equivalents to meet working capital needs while funding R&D, further commercializing technologies like SIMPAS and ULTIMUS, and completing accretive acquisitions.

In addition, we achieved this very low debt position after having spent $34 million on repurchasing of 1,668,892 of our shares through two share repurchase programs; a $20 million accelerated share repurchase, which we have completed; and a $20 million 10b5-1 plan, which still has $6 million of capital available for future purchases. Further, we increased our cash dividend to shareholders by 25%, thereby returning a portion of our profits to our shareholders.

There are two key takeaways on this slide 7 that I want to emphasize. First, our Q4 miss was due to a supply chain issue that is now resolved. This effect should boost our corn soil insecticide sales in the first half of 2023. As mentioned, our current Aztec orders are three to four times higher than they would be normally at this time of year. And second, we expect to achieve significant growth in revenue and earnings in 2023.

Finally, we are well positioned to address the market and expand our business. As you'll note in slide 8, the outlook for 2023 presents ideal conditions for the company's strong financial performance. As mentioned, we anticipate higher sales of our corn soil insecticides during the first half. Second, we expect to benefit from lower cost of goods and an improved supply chain for raws and intermediates. This should enable us to build inventory to meet demand.

Third, freight cost, which peaked in 2022, has settled down and are returning to more reasonable levels. Fourth, the level of AMVAC products in the distribution channel is comparatively low. In addition, our new formulations, expanded portfolio of green product solutions, and improved market access, for example, in Australia and Brazil, should enable us to participate more fully in a strong global ag economy.

In summary, we expect to achieve significant growth and profitability in 2023, and we'll be giving you more specific performance targets in our March earnings call. Finally, thank you for your continued support of American Vanguard. And with that, I will ask our operator to poll for any questions you may have. Kevin?

QUESTION AND ANSWER SECTION

Operator: Thank you, sir. At this time, we'll be conducting a question-and-answer session. [Operator Instructions] Our first question today is coming from Gerry Sweeney from Roth Capital. Your line is now live.

Gerard Sweeney
Analyst, ROTH Capital Partners LLC

Q

Good morning, Eric, Bob. Thanks for taking my call this morning.

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

A

Yeah. Hi, Gerry. Thanks for [indiscernible] (00:11:53).

Gerard Sweeney
Analyst, ROTH Capital Partners LLC

Q

Just a couple of questions. It sounded like the shortfall is – on the Aztec product [indiscernible] (00:12:02). It's going to entirely – I'm not sure if that's your words, but those are my words. It's going to push into the first half of 2023. I'm also just curious if there's any impact on margin on that business just because you had to find alternatives or pay up for pricing or anything like that, or is this just – we should just look at the push into the first half of 2023 and similar...

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

A

Yeah. As far as increased cost – and the only increased cost we have are [ph] airfreighting this (00:12:38) and we're going to be airfreighting all of the material that's being made in China. And the material, obviously, domestic is – it's up in Wisconsin, so that won't be airfreighted, but we'll have some additional costs, but it'll be relatively immaterial in the overall margin.

Gerard Sweeney
Analyst, ROTH Capital Partners LLC

Q

Got it. And then you did touch upon this, I think, in your comments, but it sounds maybe just a little bit more commentary on supply chain overall. It feels like things are loosening up across the board. I know you've been fighting a lot of headwinds on that side and you've done pretty well. You can't always [indiscernible] (00:13:13). But, is it a fair assumption to say things are loosening up across the board? Any commentary on maybe tightness in any markets or inputs for 2023?

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

A

Well, one of the key areas since we do a lot of phosphate businesses, the phosphorus supply chain was really bad in 2021. And not only increases, but [ph] Kazakhstan (00:13:44) shut down and China was not supplying for [ph] P4 (00:13:50) anymore. So, a number of our phosphorus suppliers had filed a force – or client force majeure. But yes, that's probably – for us specifically, that was maybe our biggest challenge which phosphorus has come back down. Everybody's back on loan. And so, availability of our raws is much easier than what we had dealt with last year.

So – and we're seeing again with some being – some raws having a strong tie like our – to methanol. Those prices were high. But again, those have come – are coming back down as well. Natural gas is coming back down. So, overall, yeah, we're – going into this year, we're feeling a lot more comfortable with our raw material chain.

Gerard Sweeney
Analyst, ROTH Capital Partners LLC

Q

That brings me to my last question. Obviously, raw material price, it sounds – looking at slide 8, raw material pricing down, low inventory in the channel, transportation costs coming down, all big tailwinds. And obviously, also had the Aztec pushing into this year which we have benefit, but sort of onetime. But any headwinds? You're – in spite of the Aztec myth, you're sort of painting a pretty good picture for 2023, even though you haven't put official guidance out there. But I'm just curious of anything that concerns you for 2023.

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

A

Yeah. Right. Right. There's always the possibility of having shortages of different pieces. We're – or with our SIMPAS equipment, we're installing equipment now. We're getting things built of different parts or when we have something that has a lot of different components, there's always concern that you don't get everything on time. But, overall, yeah, optimism looks fine. Obviously, there are factors that could happen such as escalations of conflicts that would be out of our control. But with – I think the farm economy is really strong. There's – the [ph] food banks (00:16:26) are low. The reserves are not there. And talking with experts in the field, they think that this should continue into 2026. So, I'm not identifying anything right now that is of major concern.

Gerard Sweeney
Analyst, ROTH Capital Partners LLC

Q

Got it. So you're looking at some good tailwinds for 2023. I appreciate that. That's it for me.

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

A

Okay. Thanks, Gerry.

Operator: Thank you. Next question today is coming from Chris Kapsch from Loop Capital Markets. Your line is now live.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Yeah. Good morning. Just to follow up on that last question, headwinds, tailwinds. The – given that raw material costs are easing supply chain generally, notwithstanding this Aztec issue easing, lower transportation. Just curious how agchem pricing from your vantage is holding up [ph] juxtaposed (00:17:25) against kind of what could be viewed as lower cost environment?

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

A

Yeah. So, I think the biggest shift is fertilizer. That took the biggest increase. As availability has come in, I think the prices are coming down there. We're seeing some downward pricing on some of the commodities, such as glyphosate, glufosinate, some of the more generic insecticides, fungicides.

With regard to our products, we're not seeing a position where we're going to need to readjust our pricing downward. So, I think that's – right now we're – in most of our products, certainly, we're in a better position because we're kind of the only supplier of that particular chemistry. And some of our distribution business, let's say, in Central America, and maybe in Australia, there may be pressure on some of the products that they sell that are commodity. But again, we're seeing lower costs coming through. So, some of that lower costs may need to be passed through to be competitive.

But overall, yeah, I think growers are – a shift that has occurred for the 2023 season versus the 2022 season. As growers are going into the 2022 season, we're just concerned about getting supply at any cost. And so, the push was get everything in Q4, make sure it's in the barn. For this year, I think people seeing that prices softening, are looking at – we're looking at Q4 as, okay, we don't have to have it right now. We can do more just in time and hope that prices come down before we actually purchase and plant. So, I think that's kind of what we're seeing. So, as far as our margins, I think we feel pretty good about where we are.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Got it. That's helpful. And twice you mentioned that [indiscernible] (00:19:49) at this juncture in the first quarter, three to four times "normal seasonal levels." So I'm just looking for some more context around that. Is that simply because some of the orders that were not fulfilled in the fourth quarter? Is there double ordering for – from certain customers to try to get safety stock? Or how much of this is a function of simply higher corn acreage [indiscernible] (00:20:15)? And a follow up on that, maybe looking at the USDA forecast for higher corn, how much of that is in kind of the – your – the addressable market for these [ph] soil powder (00:20:29) insecticides, which is really just the heart of the Corn Belt. [ph] Some additional (00:20:34) context might be helpful?

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

A

Yeah. Going into the year, we did see growers stepping up for what they anticipated, [ph] one, be (00:20:46) a strong commodity price, [ph] two (00:20:49), corn rootworm pressure seems to be increasing year-over-year. But the bulk of what I'm addressing is, these are orders that didn't get filled in fourth quarter. And we – our team went out to everybody as we had this Aztec issue and said, okay, here's the amount of Aztec we feel comfortable, we may get to everything that you need for Aztec, but for now, let's, place a kind of supply chain. And this is what each one kind of allocated out would get for Aztec and then some additional orders for Counter, Force and SmartChoice that would make sure that they're going to be able to meet customer demand.

So, as we go through the next month and a half, we'll get a much better picture of what percent of the original Aztec will be met with Aztec. And if we do all of it, great. But we produce more of the other corn soil insecticides to make sure that every grower out there gets corn soil insecticide in order to treat his field.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Eric, what are the chances or the risk that, because of this issue, you will have lost some opportunity or acres with to an – alternative to soil [ph] powder (00:22:34) insecticides? And...

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

A

The alternatives are really us, right? Syngenta has force in bag. But going through the SmartBox system and SIMPAS, obviously, that is our business. And so I don't think – I think growers will use the product they intended to use of. And so, I don't think they're [ph] going not use (00:23:06) product. I think that's just more a function of one of our corn soil insecticides they will use.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Got it. And last one, the – since, you're – you won't manufacturer synthesizing or compounding this product, I guess, in the fourth quarter. Just curious if you – what – if you can quantify the impact to absorption variances in gross margins and does that carry through into 2023 at all, or is it isolated in 20 – in fourth quarter of 2022? Thank you.

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

A

Yeah. So fourth quarter, there was the other half of the Aztec molecule that we were not able to make. But there's another section that does get made. And we can continue to make that at the Axis Facility in Q4. So, though the second half of the molecule that then gets combined with the first piece, we didn't make, which is true, so absorption wasn't as high. But again we'll doing that in Q1 and into the beginning of Q2. So, overall, we're not seeing any major impact.

Chris Kapsch
Analyst, Loop Capital Markets LLC

Q

Thank you.

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

A

Thank you, Chris.

Operator: Thank you. We reached the end of our question-and-answer session. I'd like to turn the floor back over for any further or closing comments.

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

Okay. Well, thank you, everybody, for getting on the call this morning. We're looking forward to this 2023 year and we'll be giving kind of the normal guidance that we do for the year at the next call, which I think we're currently scheduled for March 13. So, I look forward to updating you at that point. And have a great day.

Operator: Thank you. That does conclude today's teleconference and webcast. You may disconnect your line at this time and have a wonderful day. We thank you for your participation today.