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Darling Ingredients, Inc. (DAR)

Q4 2019 Earnings Call



CORPORATE PARTICIPANTS

James E. Stark

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Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Brad Phillips

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John Bullock

Executive Vice President-North American Specialty Businesses & Chief Strategy Officer, Darling Ingredients, Inc.

OTHER PARTICIPANTS

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Heather Jones

Analyst, Heather Jones Research, LLC

Benjamin Joseph Kallo

Analyst, Robert W. Baird & Co., Inc.

Adam Samuelson

Analyst, Goldman Sachs & Co. LLC

Thomas Palmer

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning and welcome to the Darling Ingredients, Inc. Conference Call to discuss the Company's Fourth Quarter and 2019 Fiscal Year Results. After the speakers' prepared remarks, there will be a question-and-answer period, and instructions to ask a question will be given at that time. Today's call is being recorded.

I would now like to turn the call over to Mr. Jim Stark. Mr. Stark, please go ahead.

James E. Stark

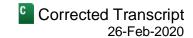
Vice President-Investor Relations, Darling Ingredients, Inc.

Thanks, Anita. Welcome to the Darling Ingredients earnings call. Participants on the call this morning are Randall C. Stuewe, Chairman and Chief Executive Officer; Brad Phillips, the Chief Financial Officer; and John Bullock, our Chief Strategy Officer. There is a slide presentation available and you can find that presentation on the Investor page on our corporate website.

During this call, we will be making forward-looking statements, which are predictions, projections or other statements about future events. These statements are based on current expectations and assumptions that are subject to risks and uncertainties. Actual results could materially differ because of factors discussed in yesterday's press release and the comments made during this conference call, and in the Risk Factors section of our Form 10-K, 10-Q, and other reported filings with the Securities and Exchange Commission. We do not undertake any duty to update any forward-looking statement.

Now, I would like to turn the call over to Randy.

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Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Thanks, Jim. Good morning, everyone. It's a pleasure having you on our call today. We finished 2019 with record earnings and are starting 2020 off in a very strong position with great momentum. As we discussed during our last call, we felt our Fuel segment anchored by DGD would deliver solid results. We achieved \$1.25 per gallon EBITDA margin that we predicted all year. Pre-blender's tax credit, or BTC, and once the BTC was made retro and prospected for the next three years, we are solidly positioned to deliver consistent and predictable earnings for the foreseeable future.

As you know, Darling is uniquely positioned with its vertically integrated supply chain fats to capitalize on the growing demand for low carbon fuels. Our supply chain is tethered to our Feed segment that processes and repurposes waste streams from the global food production industry into fats and proteins.

2019 was a record year for input tonnage as we grew by nearly 2% versus 2018. Fat prices showed late-year improvement and are poised to meet the rising demand for low carbon fuels in 2020 and beyond. Specialty proteins enjoyed a solid quarter and year as pet food demand shows no signs of slowing. The only weakness we see is the mixed BC proteins as they fight for feed ration share that has been disrupted by global trade and disease issues.

Our Food segment, its adjusted EBITDA was 7.6% higher in Q4 of 2019 versus the same period last year. And for all of 2019, adjusted EBITDA for this segment was approximately 31% higher than 2018. The primary component of this segment is our collagen business. We continue to be optimistic on future growth in our Peptan business and we'll be commissioning three new factories during the second half of 2020.

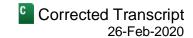
The Fuel segment had a strong performance in the fourth quarter, not only because of the reinstatement of the BTC, but the performance of Diamond Green Diesel earning \$1.57 per gallon before adding \$1 per gallon BTC. DGD produced record volumes accompanied by better pricing for the finished product. DGD sold approximately 277 million gallons in 2019, while earning \$2.25 EBITDA per gallon.

For 2019, Darling reported record pro forma operating income of \$389 million after adjusting for the 2018 retroactive BTC of \$86.6 million. Combined adjusted EBITDA for 2019 was \$739.7 million, again, taking out the 2018 BTC. We are certainly pleased with the reinstatement of the BTC for 2018 and 2019. In fact, the BTC has been in place for all the time that DGD has been producing renewable diesel and will be in effect for 2020, 2021, and 2022, which we believe brings certainty to the renewable fuels, part of our business, and we appreciate this administration's continued support and encouragement for more renewable green fuels in the transportation sector of this country.

We are also encouraged to see the Phase I trade deal signed with China, which should bring more demand for protein products and hopefully lifts protein prices over the course of the year. African Swine Fever does still present a headwind for our business in China, and that story has been overrun by COVID-19 or coronavirus that is having a global impact on a lot of companies that have operations in China and around the world. I'd like to address this a little later in the call.

With all the challenges we face globally, we were able to produce significant earnings as our employees worldwide continue to execute our strategy of being the best sustainable company on the planet. Our DGD II expansion is proceeding on schedule, and when completed in Q4 of 2021, DGD will have the capacity to produce 675 million gallons of renewable diesel plus 60 million gallons of renewable naphtha.

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Darling Ingredients and Valero are equal partners in the DGD joint venture. We work together on everything that touches this renewable diesel business, and we both continue to actively discuss the potential for DGD III to be co-located with Valero's refinery in Port Arthur, Texas. This project would increase DGD's production capacity to more than 1.1 billion gallons of renewable diesel annually and give us nearly 100 million gallons of renewable naphtha. We are currently underway in Phase II engineering and are still targeting a final decision on this investment later this year or early next, with commissioning to take place in 2024.

Now, with that, I'd like to turn the call over to Brad for little financial highlights. Brad?

Brad Phillips

Executive Vice President & Chief Financial Officer, Darling Ingredients, Inc.

Okay. Thanks, Randy. Net income for the fourth quarter of 2019 totaled \$242.6 million or \$1.44 per diluted share compared to a net income of \$40.6 million or \$0.24 cents per diluted share for the 2018 fourth quarter. Excluding the 2018 retroactive portion of the blender's tax credit from the 2019 fourth quarter, net income was \$156 million or \$0.92 per diluted share. Net income for the fiscal year 2019 totaled \$312.6 million, or \$1.86 per diluted share, compared to \$101.5 million, or \$0.60 per diluted share, for the fiscal year 2018. Again, excluding the 2018 retroactive portion of the BTC from net income for the fiscal year 2019, net income was \$226 million or \$1.34 per diluted share.

The 2019 fourth quarter and fiscal year results included \$86.6 million retroactive BTC for 2018 and \$147.8 million of BTC for 2019. Slide 7 in the investor presentation depicts the last three years of DGD EBITDA applying the BTC when earned rather than recorded. DGD's production gallons increased significantly in 2019, running at its stated capacity of 275 million gallons. Interest expense for 2019 was down nearly \$8 million as we had lower interest rates on our two outstanding Notes.

Now looking at taxes. As previously mentioned, the biofuel tax incentive was reenacted retroactively for calendar years 2018 and 2019, and extended for calendar years 2020 through 2022. Accordingly, the company's 2019 effective tax rate of 15.6% is lower than the federal statutory rate of 21%. Tax expense and cash tax payments for 2019 were \$59.5 million and \$29.8 million, respectively.

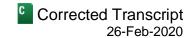
For 2020, we are projecting the effective tax rate to be 20% and cash taxes of approximately \$40 million. Capital expenditures of \$359.5 million were made during the fiscal year of 2019. CapEx was higher as we completed several expansion projects in 2019 and we anticipate Darling's CapEx for 2020 to be in the range of \$300 million to \$310 million as we complete construction of the three collagen units in our Food segment in the middle part of 2020. The CapEx range includes approximately \$230 million of normal maintenance and compliance CapEx.

Our liquidity remains strong with unrestricted cash of \$73 million and \$911 million available under our revolving credit facility. We did pay off the remaining balance of our Term Loan A in the fourth quarter of 2019.

Also in the fourth quarter, we repurchased another 407,076 common shares of the company as part of our share repurchase program, bringing the total shares repurchased in fiscal 2019 to 1,43,710 shares at a total spend of approximately \$19.2 million. With the BTC reenacted, we currently estimate the distribution from Diamond Green Diesel exceeding \$200 million by early July 2020 under our distribution policy, and we should receive approximately \$20 million in tax credits for Darling's biodiesel sold in 2018 and 2019. We currently intend to reduce our debt with these significant cash inflows. We project that our bank leverage ratio will decline below 3:1 following this debt reduction.

With that, I'll turn it back over to you, Randy.

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Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Hey, thanks, Brad. COVID-19, or coronavirus as the media calls it, continues to dominate headlines across the world. For Darling, we have nine facilities in China and several have been impacted. We are starting to reopen our plants that were impacted, but the ramp up of production may be hampered by our ability to get the necessary chemicals and raw materials delivered, as transportation restrictions related to the disease continues to be a bottleneck in China.

As of today, we remain confident that our China operations will not have a material impact on our 2020 earnings. Our Fuel segment was certainly the star performer in 2019, and we expect that it will continue to be a strong earner going forward. We believe that DGD can earn \$2.50 EBITDA per gallon in 2020, with the 275 million gallon production capacity. Darling's share of that EBITDA would be approximately \$345 million.

We have confidence in this projected performance, as DGD has a first-mover advantage over others who have announced making investments in renewable diesel, and DGD is going on nearly seven years of supply chain production and distribution management experience compared to other possible new entrants in the renewable diesel space.

We feel strongly that we have worked out the kinks of this business. We do understand that the margin environment may attract newcomers, but our ability at DGD to use a multitude of low carbon intensity or low CI scoring feedstocks gives us advantage over producers who choose to use pure vegetable oil feedstocks.

We are also confident that our announcement yesterday regarding DGD's terminal agreement with IMTT gives DGD a significant advantage in the logistics of supplying feedstocks to our location and enhances DGD's ability to ship renewable diesel through multiple modes to customers anywhere in the world. The demand for low carbon fuels is growing and will continue to expand, and we are positioned well to capture a greater share of this expanded growing market.

I'd like to remind everyone that Darling is the largest and has the significant experience in the collection, processing and delivery of feedstocks around the world. We're currently projecting our core EBITDA should show growth over 2019 and be in the range of \$450 million to \$475 million in 2020. This growth is expected to come from both the Feed segment and the [ph] Food (00:12:41) segment, as capital investments we have made in these over the last couple of years will start to bear fruit.

The math is straightforward, as DGD is debt-free and we continue to de-lever Darling with a meaningful distribution from DGD in July and this should result in a combined pro forma EBITDA of approximately \$800 million, with debt being reduced to around the \$1.4 billion range.

Our focus to drive improved results through operational execution is key delivering long-term shareholder value. We believe that we have momentum into the coming year and we'll continue to refine how we can achieve even better results.

We continue our commitment to sustainability as we feel strongly about repurposing waste streams into usable products around the globe. You will hear more from us about our efforts around ESG as 2020 progresses.

With that, that wraps up our comments here. Let's go ahead and open it up to Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] The first question comes from Craig Irwin with ROTH Capital Partners. Please go ahead.

Craig Irwin

Analyst, ROTH Capital Partners LLC

Hey, good morning, and thanks for taking my questions. So, Randy, 77.9 million gallons produced in the fourth quarter is a really hefty utilization number, well over 100%, even north of 110%. And then, \$1.57 a gallon was quite a lot stronger than the \$1.40 that we've been talking about just a number of weeks back, several weeks back but close to beginning of the quarter. Can you talk to us about what's really going right at Diamond Green operationally that's allowing you to exceed your targets? Are these things one-time in nature or can they potentially recur? Is there maybe a little bit of seasonality with the benefit of a cooler environment allowing you to maybe outperform, get more out of the plant that we should look at as maybe more of a seasonal factor emerging for Diamond Green over the next couple of years?

John Bullock

Executive Vice President-North American Specialty Businesses & Chief Strategy Officer, Darling Ingredients, Inc.

Hey, Craig. This is John Bullock. Actually, no, Diamond is performing exactly as we anticipate Diamond to perform. Operations were excellent in the fourth quarter. We actually run a little bit better when we get to summertime specs on renewable diesel than we do. So, we're in a period of time where running conditions maybe weren't quite as favorable as they might be coming up over the next several months once we get to the summertime specifications.

So, no, there's nothing onetime about operational performance at Diamond Green Diesel. We just have excellent, excellent operators at that facility and they're doing a phenomenal job, and we would anticipate that facility would continue to run at that type right now. From time to time, we do have to take a turnaround at those facilities. However, other than that, we are able to operate at 100% uptime almost all the time, in part because we have excellent operators and in part because we have a very sophisticated supply chain for the feedstock going to Diamond Green Diesel and the ability to move the product out to the various markets we moved to.

So, we don't have to slow our facility down because we have an efficient supply chain. And I think when you see all that come together, what you see is really, really good operational performance. That's what we expect now from Diamond Green Diesel, which is kind of fun to have a facility that runs out well, that you have the expectation that it's going to run that well.

As far as margins go, the margin environment is excellent and we continue to see it be excellent as we move forward for the next several months. It's a good time for Diamond Green Diesel all the way around right now.

Craig Irwin

Analyst, ROTH Capital Partners LLC

Great. And since you did mention turnarounds, are there any turnarounds on schedule maybe in the first half of the year that we should know about?

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John Bullock

Executive Vice President-North American Specialty Businesses & Chief Strategy Officer, Darling Ingredients, Inc.

There is no – there – we never really know exactly when we're going to have a turnaround now at Diamond Green Diesel. It's just whenever the catalyst starts to fade on this a little bit, so. I think we have a turnaround in the plan. We should be able to make 275 million gallons and have a turnaround this year. Exactly when that turnaround will be? I don't know that we've announced that for sure, because we're never quite sure when that's going to occur.

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

But I think it's safe to say it will not be in the first half of the year here.

John Bullock

Executive Vice President-North American Specialty Businesses & Chief Strategy Officer, Darling Ingredients, Inc.

Certainly.

Craig Irwin

Analyst, ROTH Capital Partners LLC

Good. So, my second question is about SG&A. There's been quite a lot of conversation about this back and forth last night and this morning with clients. So, the absolute increase year-over-year, \$33 million, I know you broke it out for each of your segments. You have been very clear that when BTC is reinstated, there will be a catch-up on some of the incentive compensation for the company given that you really have been focusing on sort of squeezing the last drop out of the sponge over the last few years. But I kind of suspect that accounting for incentive comp is quite significantly impacted by the market finally ascribing a more appropriate value for Diamond Green and the very strong stock performance you've had over the last few months. Can you maybe break out for us what the increases are in SG&A, how much of this accrual was one-time in nature? And the impact of the stock price on incentive comp, was that a material part of the increase that we saw? And, I guess, we all like that. So, that's obviously something maybe you can talk about if it's sustained.

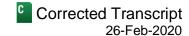
Brad Phillips

Executive Vice President & Chief Financial Officer, Darling Ingredients, Inc.

Yeah. Craig, this is Brad. So, ballpark of the \$49 million increase, approximately half of that – a good half of that, let's call it incentive comp and stock award expense, and a portion of that stock award expense is driven certainly by the stock price. And a portion of that incentive stock comp expense was for 2018. So, there, that will not be recurring in 2020. However, stock comp in 2020, I'll get sort of kind of a range here in a second for next year, will be up some. But this \$49 million, a good half of that was the stock and the incentive comp combined.

We also, as you always have, an SG&A, just a laundry list of other things and they're never equal year-over-year. There was – in 2018, we had some business interruptions that were credits against SG&A and that's where those land. So, there was a decent-sized piece of the difference, as well as a couple of legal settlements. So, those – you get those behind you, those that hit SG&A, as well as let's call it the make-whole over in the Benelux countries for our Rendac waste disposal businesses with the government. So, those make-wholes will come through SG&A. And there was more of that in 2018 than 2019, so that was unfavorable, that moves up and down based on timing of those contracts. So, for 2020, we're kind of in a range, looking at a range in SG&A of [ph] 82 to 85 (00:20:35) [indiscernible] (00:20:36).

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Craig Irwin Analyst, ROTH Capital Partners LLC	Q
That's lower than what I have modeled, so I like that. Thank you. Thanks for taking my questions.	
Brad Phillips Executive Vice President & Chief Financial Officer, Darling Ingredients, Inc.	A
Sure.	
Operator: The next question comes from Heather Jones with Heather Jo	nes Research. Please go ahead.
Heather Jones Analyst, Heather Jones Research, LLC	Q
Good morning. Thanks for the questions.	
Randall C. Stuewe Chairman & Chief Executive Officer, Darling Ingredients, Inc.	A
Good morning.	
Heather Jones Analyst, Heather Jones Research, LLC	Q
So, a quick question on the Feed business. So, recently, we've seen meat to move fairly rapidly and I was wondering if you could give us a sense of v	
Randall C. Stuewe	Λ

Yeah. I think – Heather, this is Randy. Let me comment about the kind of the global commodity world and it kind of varies from continent to continent right now. I'll start in Europe. We saw in Q4 and then already in Q1 here fat prices moving up rapidly. And so, we're out of the blocks strong from fat pricing in Europe today and we would call protein prices stable in Europe today.

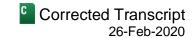
You go up to Canada, where still fat prices and protein prices have hit a bottom up there and seem to be slightly moving up now, fat prices a little more than protein. And then you come back into North America here or into the US, and while we've seen fat prices move up off the lows in Q4 and keep in mind that that December dipped kind of hard here and then came back here and then in Q1, and fat prices have moved up nicely here in the US.

Protein prices by [indiscernible] (00:22:23) kind of moving around. And so, we've seen that the chicken complex proteins seem to work through the excess inventories and move up a little bit. The pure beef products, pet food demand, as we said, is very strong, and then the mixed BC meat and bone meal, we finally work through the excess inventories that we had out there by getting them sold and exported. And so, we've seen that move back up. But you're still back in range now of where we were a \$100 a ton underneath soybean meal, we're now \$50 under, which is still historically kind of the low side of where that is.

So, we would say, for 2020, we think fat prices will continue to move up. One of the fallouts of coronavirus or COVID-19 is China was a supplier of used cooking oil to the European and whether it's biodiesel or renewable diesel and into that type of market and those exports have completely slowed. So, we've seen UCO markets in Europe and in the US start to move up rather rapidly because of the tightening of supply there.

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

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Protein, it's still the production and feeding animals, animal production around the world remains very, very strong. It's really fascinating that in our November call with everybody all we could talk about was ASF, a little bit of demand destruction. But we couldn't figure out how China was going to feed themselves now who're dominating the world with a virus here that we're not sure how that is going to cause additional demand destruction. But, overall, we continue to see very, very strong slaughter. Our factories are full around the world and the customers are taking both the fat and the protein, the fats being driven by strong biofuel markets around the world and the protein by animal production in pet food.

Heather Jones

Analyst, Heather Jones Research, LLC

But on the medium-term, you'll size specifically, so I know it's still weak relative to history, but am I right in remembering that you have a decent size piece of your business in North America that is exposed – pretty exposed on the pricing side? So, any positive move in that pricing should be good for you?

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Yeah. And there's a there's a yes and a no there. What I was trying to refer to is as you continue to see, as you follow the poultry industry, you're seeing more and more halal diets which are requiring species-specific, non-mixed, ruminant-type products. And so, that's the weak market, the [ph] falling stock market or the deadstock (00:25:02) business in the Midwest, we've made significant adjustments in how we margin that business and manage it. It had really good fourth quarter for us. But, yeah, I mean the answer is, yes, we've seen meat and bone meal move up, and yes, if all proteins move up, it will rise with the rest of the boats here.

Heather Jones

Analyst, Heather Jones Research, LLC

Okay. And then moving on to fats, just like you pointed out for China, I read something like they might get one load out of there for all of February just given where the restaurant eating out, their UCO supply is so tight. So, UCO prices had been hitting highs there. When we think about the US and all, what are you thinking as far as the price ceiling that we'll see on yellow grease and UCO or poultry fat or whatever? I mean there's strong demand from you guys and all, but is there a price ceiling relative to the feed or relative to a more conventional biodiesel that we should be thinking about for fats in North America?

John Bullock

Executive Vice President-North American Specialty Businesses & Chief Strategy Officer, Darling Ingredients, Inc.

Yeah. Heather, this is John Bullock. We would anticipate that we will see strong UCO pricing throughout the balance of this year certainly for the next couple of quarters. I don't know that we're necessarily in a position to give you a number while we think UCO is going to be going to. But UCO is clearly desired by the biofuel community. It's a great feedstock for renewable diesel and biodiesel. And as the supply tightens up here, that's going to have an impact on pricing you would anticipate.

Heather Jones

Analyst, Heather Jones Research, LLC

Okay. Perfect. Thank you so much.

Operator: The next question comes from Ben Kallo with Baird. Please go ahead.

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Benjamin Joseph Kallo

Analyst, Robert W. Baird & Co., Inc.

Hey, good morning, all. I just wanted to ask about the kind of the go or no-go decision with the Port Arthur facility, and if it's a market based from the demand side or is it – you look at the supply side and whether the logistics are there to feed that new facility? Thank you.

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Yeah. Ben, this is Randy. I think we're – the engineering process we're following is the same as we've done on DGD I and DGD II. It's a gated process. We're in the Phase II where we kind of lay out the facility, make sure it fits in there, \$20 million-plus of engineering to get an early estimate. And then we – once we see it fits and logistics do work, then we'll go to Phase III engineering and then a decision is made. If you were – as I always joke with people, the spreadsheet says make the investment now and start it up tomorrow. But we have a very rigid process that we go through in order to do this.

So, you'll see us continue. I think if you had to handicap it, we're very confident of the global demand for the product. As we've talked about, DGD I and II are very well committed into 2022 now, and we continue to see a global market developing from really just transportation fuels today. But we're also part of the engineering in DGD III and then the consideration of a sister plant, DGD IV, we'll look at aviation and then cold weather fuels as we see it continue growing market around the world for these. And you'll hear more about that in the spring as we start to open our kimono a little bit more on where we see the global demand. But right now, we can't make enough of this stuff.

I think it also allows us then to comment a little bit. While there might be lots of pre-announcements out there of people studying the business and my comments were very much that clearly the margin environment encourages you to make an investment. Unless you've got the supply chain locked up and know how to originate, it's a very, very complicated business to get in. I mean, the cracking of the molecule is one thing, the origination of the fad is another thing. And so, the advantage we have is very, very significant and we feel very good about it for the next three-plus years going forward, and I feel pretty confident that Valero and ourselves will come to the final decision on DGD III in a positive way driven by global demand, and once we get our engineering estimate firmed up, we'll come with DGD IV with the announcement of board approvals.

Benjamin Joseph Kallo

Analyst, Robert W. Baird & Co., Inc.

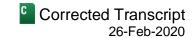
Great. Thanks for that color. And then just on capital allocation, maybe if you could just kind of outline as you start splitting out the cash flow from the JV. Is it debt paid down first or how should we think about that?

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Yeah. I mean, we've got published out there a dividend policy that says we retain \$50 million-plus whatever capital is needed for the coming quarter for the expansion. It's debt free down there. There is – it's generating significant cash. As Brad alluded, we have, I don't know, \$451 million or \$457 million of blender's tax credit coming in. It's been filed. It will probably be received sometime in April, I would guess. But given our dividend policy, we do it at the end of the quarter and that would be at the end of the quarter, then it would be the 1st of July. And then, Brad, net of whatever we have down there that's needed, I think our capital expenditures left on DGD II down there are \$800 million, \$850 million, plus or minus a little bit. And so, \$420 million this year; \$430 million next year, and you can kind of run the math. And that's the reason we were kind of giving you the \$2.50 a

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gallon, 275 million gallons. Brad pulls \$200 million, \$220 million dividend here in July. And then, we're not saying that we won't pull another dividend this year. It's just going to depend on the cash outflows and the timing of the construction and as we go forward here and that's – a lot of that always becomes weather-driven. By July, we'll have steel up, concrete's poured right now, footings are done, and concrete will start to go up and that's when the cash starts going out the door pretty quick.

Benjamin Joseph Kallo

Analyst, Robert W. Baird & Co., Inc.

Great. Thanks, guys.

Operator: The next question comes from Adam Samuelson with Goldman Sachs. Please go ahead.

Adam Samuelson

Analyst, Goldman Sachs & Co. LLC

Yes. Thanks. Good morning. So, Randy, John, I was hoping to maybe dig in a little bit on the \$2.50 a gallon kind of margin outlook at Diamond Green. Maybe first, just thinking about the LCFS kind of value embedded in there, are we – have we reached kind of the peak in terms of LCFS value capture relative to the opportunity, or is there still incremental opportunity whether it's year-on-year 2020 versus 2019 or just on a go-forward basis to capture more of that value that's created by the renewable diesel?

John Bullock

Executive Vice President-North American Specialty Businesses & Chief Strategy Officer, Darling Ingredients, Inc.

Yeah. This is John. So, we've been reticent to comment about what percentage of the LCFS we retain. We consider that to be information which is confidential with us and our customers. Obviously, as you can tell from our results, it's been a greater and greater percentage of the LCFS. And I think we've seen a lot of that and I don't know that we're totally at the point where we won't see some more of it.

So, the answer is, we probably will see a little bit more because the demand is just excellent, excellent for Diamond Green Diesel's product at this point in time. It's not going to be on the rapid increase that we've seen over the past year or year-and-a-half, but I don't know that we've reached the peak of the mountain in terms of the pricing on the LCFS markets.

Adam Samuelson

Analyst, Goldman Sachs & Co. LLC

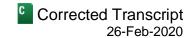
Okay. That's helpful. And then as you think about the more durable margin advantage of the facility, I mean \$2.50 a gallon expectation this year, \$1 that's the blender's tax credit, and you think about your logistics advantages versus others, your feedstock advantages particularly versus those who could be using vegetable oil process efficiencies in the plant, anyway to help think about and dimensionalize kind of what you see as the durable margin advantage of Diamond Green versus other facilities, which also helps us kind of frame the challenges others would face on investment in new capacity?

John Bullock

 $\textit{Executive Vice President-North American Specialty Businesses \& \textit{Chief Strategy Officer, Darling Ingredients, Inc.} \\$

Yeah. This is John again. I don't know that I necessarily want to put a number on that. I think that would be hard to do. However, it is amazing to me when you think about the sheer complexity of the size and scale of these renewable diesel plants and the sheer volume, the thousands of railcars, the thousands of trucks, the hundreds of

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ships that have to be involved in moving this product around both inbound and outbound, and the complexity of managing all that especially trying to be competitive on several different rail lines to receive your product, being – having various remotes to move the product out of various rail lines to move it out to the various LCFS markets, the supply chain complexity of renewable diesel facility in many ways is the most complex aspect of a renewable diesel facility and we always find it relatively humorous here.

We see lots of announcements and nobody seems to realize that the most important part of this business is a piece of the business that at least publicly nobody talks about. And so, we would not be doing this, we would certainly have not built Diamond Green Diesel too if we did not think that we have the opportunity coming along with IMTT, the announcement we just made yesterday.

We spend literally thousands of hours on every renewable diesel investment, on supply chain analysis, both inbound and outbound, because we think this is a defining competitive advantage, and it's important for everyone to realize we're not building Diamond Green Diesel just to run when margins are really high. We're running, building Diamond Green Diesel to be the most competitive renewable diesel facility in the world or facilities in the world in any margin environment. And that competitive advantage from a supply chain is absolutely critical. If you're not designing that in upfront, you're not designing a facility to compete in the long run.

Adam Samuelson

Analyst, Goldman Sachs & Co. LLC

That's some super helpful color. And then, if I could squeeze just one more in just on the base business. Randy, I think, in the prepared remarks, you talked to \$450 million to \$475 million EBITDA expectation for the base business. That growth versus 2019, any way to bucket that between Feed, Food, Fuel?

Randall C. Stuewe

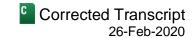
Chairman & Chief Executive Officer, Darling Ingredients, Inc.

I knew you were going to do that. No. But the answer is we think Feed will – obviously, that's the largest segment. We should see a pretty nice improvement. The \$57 million, \$58 million fourth quarter should not be repeated, as we said, with all the one-timers that flew through it that Brad mentioned in his comments. Clearly, a full year of our Amparo, Peptan plant running is going to help us. We had a pretty nice performance in China last year in our Food segment. I think we'll be okay there this year. A little hesitation in my voice, comments are that it's very challenging over there. But at the end of the day, all three of our gelatin plants are running today in China and that's a domestic business.

And then, I commented we have bringing up an order, we have our Angoulême, Gent, and Epitacio, Peptan plants all coming online starting up in April, May, and June concurrently with production to the market in May, June, July. So, the Food segment, as we said, will show some very nice growth, but it will be back-half loaded as we go forward. Much as John talks about renewable diesel demand, we continue to see very nice and significant growth in the hydrolyzed collagen business around the world in sports, health, and nutrition market.

So, clearly, it's going to – as we said, the Fuel segment is always kind of an annuity out there. The difference this year versus last year will be the prospective tax credit. But as you were asking and I'm just throwing a few more color comments in here for you, while John was talking about renewable diesel and the demand and the margin structure, the margin structure post-BTC for the classic biodiesel business is not good. And I want to say that the earnings in the classic biodiesel business that we operate today in fairly competitive plants are somewhere between \$0.00 and \$0.10 a gallon black right now, even with \$1 a gallon.

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The [ph] ren (00:38:33) market did not react, the feedstocks as we talked about moved up, the HOBO spread kind of went crazy. So, that's really not a very good business. That will weigh a little bit on our Canadian operation, but overall, we should be able to make it up. So, long story short, we think the low side is \$450 million. We think if we get any type of pricing authority, \$475 million-plus is doable and making sure that those Peptan plants come up online, I think we're positioned even to go higher in 2021.

Adam Samuelson

Analyst, Goldman Sachs & Co. LLC

Good all that color. I'll pass it on. Thanks.

Operator: The next question comes from Tom Palmer with JPMorgan. Please go ahead.

Thomas Palmer

Analyst, JPMorgan Securities LLC

Good morning and thank you for the question. I wanted to touch on the economics today at Diamond Green Diesel. You just touched on, excuse me, some of the weakness in traditional biodiesel operations, we have seen diesel roll over a bit [ph] before ren has (00:39:34) come under pressure kind of in wake of the blender's tax credit approval. But you came out with a pretty strong number historically, right, at \$2.50 per gallon for the Diamond Green Diesel business. As we think about the start of the year, so really the first quarter, is that a reasonable number, or just given what we've seen with some of the initial dislocation following that blender's tax credit approval, should we be looking more for a ramp in subsequent quarters? So, just any color on kind of today's unit economics versus how you see it progressing.

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

All right. Thanks, Tom. This is Randy. A good question. Hope you pay attention here. I think the margins will actually be better than \$2.50 a gallon in Q1. And at the end of the day, we've continued to lay out there quarter-after-quarter the margin structure in the business. As John alluded to, we continue to capture more and more of the LCFS premiums around the world, both domestically and export, and the business is running strong.

So, \$2.50 is where we're comfortable seeing for the year. So, feedstocks, we think will be higher in the back half of the year. So, at the end of the day, we probably have stronger earnings there in Q1, Q2, and if we're right on the Q3, Q4 with fat prices going up, our core business then picks up a little more on the back half of the year.

Thomas Palmer

Analyst, JPMorgan Securities LLC

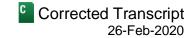
Great. Thanks for the color there. And then just wanted to ask quickly on the logistics agreement that you announced yesterday, is this a necessity to make sure you can move product or is this incremental in terms of lowering the overall cost structure at DGD when we think about distribution costs?

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Yeah, I'll give a comment, then I'll let John also comment. I mean, number one, when you're going to have a facility on-site with DGD I and DGD II, 675 million gallons, let's round up to 700 million gallons, I'm confident we can probably make that many gallons eventually, 8.5 pounds a gallon. You're talking 6 billion pounds of fat, you're talking 40% of the US North American supply and trying to bring it all into one location in railcars and trucks, as

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John alluded, could be done and we're going to do the best we can, but we have the opportunity to put some tanks across the river about 5 miles away and I think we're taken on per our announcement 790,000 barrels of tankage over there that will allow us to ship both fat by water, meaning barge, by rail, by truck, by ship in the IMTT and offload, and then at the same time, we'll be able to move renewable diesel over there to both improve our outbound logistics both at the site, our current site, and be able to double load as we need to.

John, do you want to comment a little more?

John Bullock

Executive Vice President-North American Specialty Businesses & Chief Strategy Officer, Darling Ingredients, Inc.

Yeah, it was interesting, because when we had originally designed Diamond Green Diesel II, we did not have the IMTT terminal logistics specifically designed in. We had an alternative where we were going to be able to do things on-site at our facility. But the IMTT guys came along and we had good long discussions, it really evolved into something that in my mind is absolutely spectacular. We're going to have pipeline capability both on the raw material, raw fat coming across from IMTT to our facility, but also on renewable diesel going over to IMTT to be able to load out.

When you start talking about the logistics of 675 million gallons, 700 million gallons of renewable diesel plus another 60 million gallons of naphtha, we now have two different locations off of the Valero docks as as well as IMTT that we can load finished product. We can bring raw materials in by barge, by vessel. If the international market starts to supply us with some fats into the marketplace, we have already today KCS capability in the Diamond Green Diesel I, and they've been spectacular partners with us in supplying Diamond Green Diesel I.

We have CN capability today that we load renewable diesel out of. We will incorporate now CN loading/unloading capability at both the Valero site and also at IMTT and be able to load out CN renewable diesel out of IMTT.

From a logistics and supply standpoint, with the additional 790,000 barrels of capacity that we're bringing on board, it now means that we have a massively, effectively functioning terminal that supports our ability to be able to make sure that we are always buying the fat when its cheap and available and to be able to ship the product out to whatever the market is that the best market for us to be able to go to. It also means for anybody that's doing business with us that if you ship us a railcar, it's going to get unloaded fast. We're turning it fast. If you bring a boat into us, we're going to be able to get it in and deal with it quickly.

So, in terms of supply chain efficiency, we're making it extremely easy for our supply chain partners to work with us. And when you're the type of demand and supply that we intend to be in North America, that's a very important element, because all of your customers, whether they be suppliers of raw material or finished product guys, they all demand the respect that you've got a facility that it can efficiently deal with the product that they're sending to you or taking from you, and that's what IMTT gives us, just phenomenal capability and flexibility.

Thomas Palmer Analyst, JPMorgan Securities LLC	Q	
Thank you.		
Operator: The next question comes from Ken Zaslow with Bank of Montreal. Please go ahead.		
Kenneth B. Zaslow Analyst. BMO Capital Markets (United States)	Q	

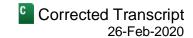
Darling Ingredients, Inc. (DAR) Corrected Transcript Q4 2019 Earnings Call 26-Feb-2020 Hey. Good morning, everyone. Randall C. Stuewe Chairman & Chief Executive Officer, Darling Ingredients, Inc. Good morning, Ken. **Brad Phillips** Executive Vice President & Chief Financial Officer, Darling Ingredients, Inc. Good morning. Kenneth B. Zaslow Analyst, BMO Capital Markets (United States) So, just a couple of quick follow-ups. A lot has been covered here. One is how much of the Food EBIT growth – EBITDA growth is from the CapEx projects that is associated with that? That's my first question. Randall C. Stuewe Chairman & Chief Executive Officer, Darling Ingredients, Inc. The Food EBITDA growth for in 2018 or 2019 or 2020? Ken, I would – let me – I'll just answer it, because I mean the 100% of the growth in the Food segment is the collagen growth business of the new plant in Amparo that came online year-over-year. Kenneth B. Zaslow Analyst, BMO Capital Markets (United States) So, you're not expecting any underlying improvement in the business that - it's all CapEx projects? Is that fair or majority? Randall C. Stuewe Chairman & Chief Executive Officer, Darling Ingredients, Inc. Yeah. I mean – yeah, the Food segment is made up of our casings business which is really small, our edible fats business which we had a little bit of erosion there, because China started buying raw fat, frozen fat out of Europe, and so – but we've seen the price of raw fat or edible fat in Europe move up nicely, so that offset the margin erosion by the volume decline has been offset. And then really the growth that we see over the next two years is 100% related to the rebalancing of our gelatin, collagen business model there around the world. Kenneth B. Zaslow Analyst, BMO Capital Markets (United States) Okay. And how much of the Feed improvement is because of just a lower compensation? Right – is that right, and not the replication of the fourth quarter numbers, is that a significant portion of that as well? Randall C. Stuewe Chairman & Chief Executive Officer, Darling Ingredients, Inc. Not sure I understand your question again.

Right. The Feed in the quarter fell short of at least our expectations, right, because of the SG&A increase.

Analyst, BMO Capital Markets (United States)

Kenneth B. Zaslow

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Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Yeah.

Kenneth B. Zaslow
Analyst, BMO Capital Markets (United States)

So, when you're looking year-over-year, and the improvement for 2020, I'm assuming probably about half of that is just recovering that part of it plus then the other half is probably the improvement in pricing. Is that a way to think about it?

think about it?

Randall C. Stuewe

Kenneth B. Zaslow

Analyst, BMO Capital Markets (United States)

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

I would look at it three ways. One, yeah, you won't have a significant flow-through of – the true-up of the incentive comp programs and legal settlements that went through that segment. Number two, you've got a stronger fat market in Europe year-over-year right now that's going to flow through in Q1. And then, also we will have our LA, Grapeland, and Wahoo assets on full year now. So, we should have some – always, when you have plants under construction, you have a little additional extra expenses that seem to flow through those businesses. So, we should be running very strong here in the US. And then, we have some expansion projects happening in Canada today that should help contribute to the growth this year.

Analyst, BMO Capital Markets (United States)

Okay. And then, in terms of the EBITDA improvement on the core business – and it is a minor issue, but when

Okay. And then, in terms of the EBITDA improvement on the core business – and it is a minor issue, but when you're thinking about the Fuel Ingredients, does that include or exclude the BTC?

Randall C. Stuewe
Chairman & Chief Executive Officer, Darling Ingredients, Inc.

So, that excludes DGD. We would just say that that Fuel segment has always been, what, \$50 million to \$60 million, Brad, something like that. I don't have the numbers in front of me. That's because that's anchored by our

Ecoson and Rendac businesses that are tariff businesses and very, very straightforward.

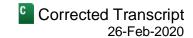
Kenneth B. Zaslow

And my last just strategic question is the cash that you had received from Diamond Green Diesel will go to the debt repayment. Previously, you said that you would think about acquisitions, but has that been tabled just because of the strength of DGD and you're looking just to deleverage and give back to the shareholders? Is that how to think about it?

Randall C. Stuewe
Chairman & Chief Executive Officer, Darling Ingredients, Inc.

That's how we're looking at it today, Ken. I mean, we're – Brad and I are obviously looking at the capital structure both near-term and long-term on where we're going to put the business. I mean, for the first time in my 17 years, I've been involved in discussions with the word investment-grade now attached to him. So, we're going to go ahead and just basically – our Senior Term A is gone now. It'll go against the Term B. That's the last [ph] prepayable (00:49:37) debt we have and then we'll figure out where we're going from there.

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Kenneth B. Zaslow

Analyst, BMO Capital Markets (United States)

Great. I appreciate it, guys. Thank you.

Operator: The next question is a follow up from Heather Jones with Heather Jones Research. Please go ahead.

Heather Jones

Analyst, Heather Jones Research, LLC

Thanks for taking the follow-up. So, I wanted to go back to the LCFS credit. You all are getting a bigger and bigger piece of that, but I was thinking about the mandates in Europe, the mandates on the West Coast and then talks of a low carbon program in the Northeast. And just some capacity is being added, but you all have highlighted really well the difficulties of the supply chain. So, I was wondering, do you envision a scenario where given the steepening mandates and the difficulty of bringing supply online that it could get to a point where you actually could receive more than 100% of the LCFS, is that crazy talk?

John Bullock

Executive Vice President-North American Specialty Businesses & Chief Strategy Officer, Darling Ingredients, Inc.

Heather, this is John. I mean, we'll see how these markets develop. I would say you highlighted one of the things that we're extremely interested in, which is all of the developing LCFS programs, whether it be Washington State, the Canadian Federal Program, New York State, the Northeast, there's even some talk in Midwest, there's some talk in California or Colorado about various programs. It seems like the low carbon concept is just really taking hold out there. And all markets are – all pricing is based on markets, right? And so, to the extent that the demand remains strong, if the market is in such a situation where we are able to command premiums, don't worry, we'll ask for those premiums.

Heather Jones

Analyst, Heather Jones Research, LLC

Okay. And my final follow-up is, have you seen any shifts going into 2020 in DGD portfolio as far as what you're pricing on spot versus term contracts?

John Bullock

 $\textit{Executive Vice President-North American Specialty Businesses \& \textit{Chief Strategy Officer, Darling Ingredients, Inc.} \\$

Yeah. Heather, this is John. Most of our product is sold on a – on term basis with the formulas. We do very little spot sales.

Heather Jones

Analyst, Heather Jones Research, LLC

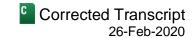
Okay. Thank you so much.

Operator: This concludes our question-and-answer session. I would now like to turn the conference back over to Randy Stuewe for any closing remarks.

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

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Thank you. We appreciate everyone's time today and look forward to seeing you as we get out on the road to get to tell our exciting story to the investment community, and we'll see everybody then. Thanks again.

Operator: This conference has now concluded. Thank you for attending today's presentation. You may now disconnect.

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