11-May-2022

ICL Group Ltd. (ICL.IL)

Q1 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by and welcome to the ICL Analyst Conference Call. Our presentation today will be followed by a question-and-answer session [Operator Instructions] . I must advise you that this call is being recorded today. [Operator Instructions]

I would like to hand the call over to the first speaker today, Peggy Reilly Tharp, Vice President of Global Investor Relations. Please go ahead, ma'am.

Peggy Reilly Tharp
Vice President-Global Investor Relations, ICL Group Ltd.

Thank you. Hello, everyone. I'm Peggy Reilly Tharp, Vice President of Global Investor Relations. I'd like to welcome you and thank you for joining us today for our quarterly earnings call. The event is being webcast live on our website at icl-group.com.

Earlier today, we filed our reports with the securities authorities and the stock exchanges in the US and in Israel. Those reports as well as the press release are available on our website. There will be a replay of the webcast available after the meeting, and a transcript will be available shortly thereafter. The presentation, which will be reviewed today, was also filed with the securities authorities and is available on our website. Please be sure to review the disclaimer on slide 2.

Our comments today will contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements are based on management's current expectations and are not guarantees of future performance. The company undertakes no obligation to update any financial information discussed on this call at any time.

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We will begin with the presentation by our CEO, Mr. Raviv Zoller; followed by Mr. Aviram Lahav, our CFO. Following the presentation, we will open the line for the Q&A session. Raviv, please.

Raviv Zoller

President & Chief Executive Officer, ICL Group Ltd.

Thank you, Peggy, and welcome, everyone. Clearly, a great deal has changed in the world since we last reported. And I want to try to give you the clearest picture possible of the impact we have seen and expect to see in our business and across our end markets.

To begin with slide 3, while we have benefited from commodity market upside, this has not distracted us from continuing to focus on our long-term specialties operations and on expanding this portion of our business. Commodity cycles come and go, but the upside is subject to external factors beyond our control. And this is why we remain dedicated to our specialty strategy, which will benefit our shareholders in both the near term and into the future.

In the first quarter, ICL delivered record results with all-time record sales of more than $2.5 billion, an increase of more than $1 billion and ahead of our expectations. Adjusted EBITDA crossed $1 billion and was also an all-time record, as we leveraged our agility and diversity despite global uncertainty. Our specialties business, Industrial Products, phosphate specialties and Innovative Ag Solutions all delivered record results, and all four of our divisions contributed to the significant growth in sales and EBITDA. Overall, strong quarterly performance was supported by increased demand and higher prices in most markets, as the disruption caused by the pandemic, sanctions and the conflict in Ukraine radically shifted market dynamics.

During the quarter, we maintained our focus on long-term cash generation by innovating with our specialty businesses product portfolio and by driving cost efficiencies to deliver free cash flow of $218 million, up more than 260%. While it can be easy during an upcycle to lose focus on costs, our initiatives in this area remain on track.

We continue to enrich and expand our existing customer relationships and build new ones by serving as a consistent and reliable supplier in the face of continuing supply chain challenges. We plan to continue to optimize both our customer and supplier relationships with emphasis on long-term sustainability considerations, as we manage through these issues and significantly higher raw material costs and freight rates.

Finally, our policy to distribute a payout ratio up to 50% of annual adjusted net income resulted in a dividend of $23.83 per share, up more than 350% versus $5.25 in the first quarter of last year. In total, ICL will pay out $306.5 million in dividends for the quarter.

Now, please turn to slide 4 for a look at the [ph] metrics (00:04:37) I just discussed. Sales were up nearly 70%, while adjusted EBITDA was up more than 230%. EBITDA margin for the first quarter increased to nearly 40% from 20% in the first quarter of last year and was also up significantly when compared to the fourth quarter 2021 rate of 29%. We also added nearly $120 million of operating cash flow in the first quarter.

On slide 5, we have a snapshot of our first quarter results. And once again, you can see we demonstrated improvement in each key financial parameter with very significant improvement in most of them, including gross margin of nearly 50% and EBITDA margin which doubled year-over-year to nearly 40%.

I would like to now begin our segment review with Industrial Products on slide 6. Record quarterly sales were $494 million and up 24%, while record EBITDA was $203 million and up 66% year-over-year. This business

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continued to benefit from our strategic shift to long-term contracts. And today, more than 70% of bromine compound sales are under long-term contracts. This segment also saw higher pricing year-over-year, which helped offset increased raw material and shipping costs.

While bromine prices in China increased year-over-year, they declined from record highs in the fourth quarter of 2021, still remaining significantly ahead of the pre-COVID rates seen in 2019. Phosphorus supply from China rebounded in the first quarter, following the elimination of environmental restrictions in the fourth quarter of 2021. However, this supply is expected to be impacted by the resumption of COVID shutdowns in China in the second quarter.

Most of our flame-retardant products were sold out in the first quarter, which contributed to the record sales. Phosphorous-based flame retardant sales increased 22% to record levels, as the construction industry remained strong. Other end markets continued to moderate, including automotive and consumer electronics. Automakers face continued production issues on a global basis, while the consumer electronics market has softened following exceptionally strong 2021. The oil and gas industry maintained its momentum in the first quarter. However, some clear brine fluid orders shifted to the second quarter.

Turning to slide 7 and our Potash business, where sales of $795 million were up more than 120% year-over-year and EBITDA of $450 million was up 626%. For the quarter, our average realized price per ton of $601 was up $344 year-over-year and up $114 over the fourth quarter. In late February, ICL signed framework agreements with customers in India and China to supply potash in 2022 at $590 per ton.

During the quarter, potash prices continued to increase due to global disruptions in availability related to sanctions on Belarus products. This situation has been further exasperated by uncertainty evoked by the conflict in Ukraine, as Russia is also a significant player in the global potash market.

Price in the quarter for corn, rice, soybean and wheat were all up double digits, once again, due to strong demand and tight supply. Concerns about global food security were amplified due to the recent unrest in Ukraine, as both Ukraine and Russia are leading exporters of wheat, corn and other food staples. At our Dead Sea site, we concluded our annual maintenance shutdown in March versus April last year, and more than 70 projects were successfully completed.

Our P-9 pumping station also achieved its first quarter of full operations following commissioning late last year. At ICL Iberia, production improvements continued to advance as we enter our first full year of production following the completion of the ramp project at the Cabanasses mine in 2021. For the first quarter, production increased by 38% to a 182,000 tons and we are in the process of completing additional projects in Spain, which will help us reach our 1 million ton annual run rate target.

Our metal magnesium sales increased in the first quarter due to higher prices and competitor challenges during the recovery of global end market demand. As you recall, during our fourth quarter call, we announced our Boulby operations would be moving from our Potash segment to Innovative Ag Solutions and we will provide an update on this realignment during our IAS division review. This change helped us to consolidate our specialty agriculture business in one segment and to sharpen our focus on targeting long-term growth of our organic fertilizer solutions.

Turning to slide 8 and our Phosphate Solutions division, where record first quarter sales of $798 million were up nearly 60% year-over-year, while EBITDA of $247 million was up more than 160%. This business saw record results for both commodities and specialties and maintained its strategic, long-term focus on driving specialty

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profitability despite the surge in commodity prices. In the quarter, our phosphate specialties business benefited from increases in both prices and quantities.

Food specialty results were supported by higher volumes and prices globally, while industrial specialty results benefited from higher demand across most industries and regions with particular strength in the US and Europe. Pricing was up across all regions and offset higher input costs in the first quarter. Our YPH joint venture, once again, delivered record results with strength in both commodities and specialties along with improved pricing for key products and better product mix versus last year.

Demand continued to grow for our specialty mono ammonium phosphate destined for electric vehicles and other energy storage offerings. Record phosphate fertilizer sales were driven by surging prices amidst reduced supply, and the market for sulfur and other raw materials also remained tight. Raw material prices, especially sulfur, are expected to have a more significant impact going forward this year.

Turning to slide 9 and Innovative Ag Solutions where ongoing momentum combined with continued strategy execution to help deliver record results. In total, first quarter Innovative Ag sales hit an all-time record high of $566 million, up nearly 70%. EBITDA of $110 million was also an all-time record and up more than 230%. Existing fertilizer momentum was supplemented by increases in commodity prices related to Russia's invasion of Ukraine, two substantial participants in the commodity and food supply chains, as raw material prices escalated and supply chain issues continued.

Regarding Brazil, our integration remains on track and the overall market remains durable. First quarter results were ahead of expectations and benefited primarily from higher prices, but also increases in volume. Our turf and ornamental business had a good first quarter as well and started the season with solid distributor demand.

Record specialty fertilizer sales in the quarter were driven by higher prices, with polysulphate-based products branded as FertilizerpluS, contributing both in terms of price and volume. FertilizerpluS had record results due to improved market share and higher prices. Polysulphate production, which is now housed under IAS, was up 30% to 238,000 tons, while sales volume increased 11%, helping ICL Boulby to achieve quarterly profit contribution for the very first time.

If you will turn to slide 10, I would like to wrap up my portion of today's call by reviewing a few recent sustainable investments and innovations in our target areas of industrial, food and agriculture solutions. For industrial efforts, we have brought together a global and multidisciplinary team to address opportunities in sustainable energy storage. This dedicated unit will expand on our company's existing capabilities and refine our product offerings, including phosphate, bromine and phosphorus-based specialty solutions for the rapidly growing energy storage market.

Additionally, during the first quarter, we monetized intellectual property developed by ICL when we sold our 50% share of the Novetide joint venture for a capital gain of $22 million. For our food-focused business, we saw success with an innovative milk protein product created by our Prolactal team, which naturally delivers superior taste and texture for products like yogurt and cheese.

In Turkey, our team developed an advanced cattle feed solution called BufferMAX to help farmers increase the quantity and quality of their milk production, while reducing expenses. While our alternative protein is still behind our initial expectations, the team is expanding its customer pipeline, and new brands are using our solution as part of their planned product offerings.

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As part of our efforts to offer sustainable agricultural solutions, we're consolidating and expanding our biostimulant product offerings. This area is growing rapidly as the marketplace looks for more sustainable solutions when it comes to crop inputs, especially in light of rising commodity prices.

Our acquisitions in Brazil have expanded our opportunities in this area and we are working together to maximize our existing potential and next steps in this exciting market. This aligns with other sustainability efforts, including work completed our Haarlem site in the Netherlands. ICL recently became the first fertilizer producer in the world to obtain Fertilizing Products Regulation certification from the European Union. This certificate, which is based on the new EU fertilizer regulations, addresses the biodegradability of polymer coatings for controlled-release fertilizers or when combining mineral fertilizers with biostimulants. Once again, ICL is at the forefront of sustainability and innovation in its efforts to help create impactful solutions.

Finally, on slide 11, I'd like to summarize where we are and where we are going as a company. First and foremost, we're keeping our eye on the ball. While potash and phosphate prices are going to be even stronger in the second quarter, the commodities upside is external and unpredictable, just like it is in every cycle. Therefore, while we are enjoying the commodity upside while it persists, we remain focused on our specialty offerings and our agility as we look to target consistent growth in sales and EBITDA.

We need to use this time to continue to drive our cost efficiency initiatives, while increasing capacity to enable continued growth in our specialties businesses. We also need to invest in research and development to innovate and expand our specialty product portfolio. We must accelerate innovation and sustainability efforts to establish our business leadership for the future.

All the while, we need to maintain our focus on our long-term customer relationships as these drive our business. By providing innovative and quality specialty solutions for our customers in a consistent and reliable manner, we are able to maintain our premium position, which in turn helps us to continue to deliver the goal of long-term cash flow generation. Combined, these efforts will help us to not only keep our eye on the ball, but also to continue to create and return value to our shareholders.

As always, I want to thank the entire ICL family of employees spread out across the globe for all of their hard work and contributions during this quarter. Your confidence and creativity in the face of global uncertainty helped ICL to, once again, deliver record results.

And with that, I will turn the call over to Aviram.

Aviram Lahav

Chief Financial Officer, ICL Group Ltd.

Thank you, Raviv, and to all of you joining us today. While you've already seen slide 13, I would like to call out a few additional highlights. First quarter adjusted operating income of $880 million was up more than 370% and adjusted operating margin of 34.9% was up dramatically from 12.3% in the first quarter of last year. Adjusted net income attributable of $613 million was up more than 350% year-over-year, and adjusted diluted earnings per share of $0.48 were up $0.37 or more than 350%.

As Raviv mentioned, quite a lot has transpired since we reported our fourth quarter earnings. As you can see on slide 14, while global growth remains strong, inflation in most countries has soared to multiyear highs. The US dollar has surged to its highest levels in nearly two decades, which is causing swings for other currencies around the globe.

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The combination of these dynamics and the situation in Ukraine has had a ripple effect around the world and resulted in even greater uncertainty. As a result, the supply chain disruptions we experienced throughout COVID and into 2022 have not only continued, but conditions have become worse. In addition to issues related to Ukraine, there have also been delays due to resumed COVID restrictions and shutdowns in China.

Commodity prices have continued on their upward trajectory and we expect additional impact going forward due to the invasion of Ukraine. For potash, in particular, existing sanctions on Belarus have been compounded by international sanctions on Russia, resulting in further tightening of supply since these two countries accounted for approximately 40% of potash supply in 2021.

On slide 15, you can see prices for potash, phosphoric acid and sulfur have continued to trend higher, with prices reaching new 10-year record highs. For the first quarter, while we were able to offset the increases of raw materials, which go into our specialty solutions, this is expected to become more difficult as the year progresses. Also, while marine transportation costs declined in the fourth quarter, rates trended up again in the first quarter.

Our supply chain, procurement and logistics teams have worked tirelessly to overcome higher overall costs and global supply chain challenges. We will continue to optimize our customer and supplier relationships to manage through these challenges and to work to ensure consistent and reliable product supply for our customers. We will also continue to leverage our advantageous production locations and global supply chain capabilities.

On the left side of slide 16, you can see the impact of higher prices on our year-over-year sales growth. For quantities, I would like to call out several items. For Potash, as Raviv mentioned, our annual maintenance shutdown shifted from April last year to March of this year. For Industrial Products, we experienced production limitations in China, which impacted quantities of brominated flame retardants in the quarter. For IAS, we have been rebuilding our Ludwigshafen facility in Germany following the fire last fall and operations resumed just this month. We also made a conscious decision at IAS to focus on polysulphate at Boulby versus less profitable salt production.

Additionally, we saw positive contribution from our recent Brazilian acquisitions. Even during the off-season, these businesses comprised 22% of Innovative Ag Solutions sales in the first quarter. For Phosphate Solutions, even as prices for phosphate commodities soared, we maintained our long-term strategic focus on specialty sales, which represented 55% of sales in the first quarter.

On the right side of the slide, you can see improvement in sales from all four of our segments with the impact of higher prices continuing to flow through to our results. I would also like to point out that in connection with Israeli taxation, which is a key component of our effective tax rate, as prices of our products continue to trend upwards, our effective tax rate is expected to increase due to the surplus profit levy on our natural resources among others.

Turning to slide 17, you can see the significant contribution that higher prices made to adjusted EBITDA. But once again, on a segment basis, all four of our businesses contributed to the year-over-year improvement. For Phosphate Solutions, we continue to prioritize our phosphate specialties focus, which made up 47% of EBITDA for this segment.

Before we turn the call over to the operator for Q&A, I would like to review a few highlights on slide 18. For the first quarter, our net debt-to-EBITDA ratio improved to 1 times from 2.4 times in the first quarter of last year. We have continued to drive growth in cash flow generation through cost controls and efficiencies and continue to invest in our long-term specialties businesses.

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We also achieved our sustainability linked loan goals for 2021. As a reminder, our goals over the five-year term of the loan include an annual reduction in direct and indirect Scope 1 and Scope 2 CO2 emissions resulting from our global operations. And this progress is being monitored and verified by an independent third-party organization in accordance with the GHG Protocol and relevant ISO standards.

We also committed to expanding our participation in Together for Sustainability by adding qualified vendors meet criteria in the areas of management, environment, health and safety, labor and human rights, ethics and governance. And finally, we continue to expand the representation of women among our senior management, executive and board of director roles.

Turning to slide 19, I would like to call your attention to our updated guidance, which reflects our very strong results in the first quarter and significant changes in market dynamics. As a result, we now expect to deliver an adjusted EBITDA range of between $3.500 billion and $3.750 billion in 2022 with our specialty businesses contributing approximately $1.300 billion to $1.400 billion of this amount.

And with that, I would like to turn the call back over to the operator for Q&A.

QUESTION AND ANSWER SECTION

Operator: Ladies and gentlemen, this starts the Q&A session. [Operator Instructions] Our first question comes from the line of Alex Jones from Bank of America. Please go ahead, sir.

Alexander Jones
Analyst, Bank of America

Q

Thanks very much for taking my questions. Two, if I may. I'll go one by one. The first question on the margin in Industrial Products, clearly above 40%, very, very strong, how should we think about that in the balance of the year? Will sort of continued price increases sustain it to that level or will that pressure push it down or start pushing it down a little bit at least? I'll start with that and then will come back with more. Thank you.

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

Okay. Thanks, Alex, for the question. The margin came out higher than we expected in the beginning of the year, and the reason is that our long-term contacts have an annual price update and that happens in the beginning of the year. And the pricing came in higher on almost all of our contracts. We expect the margin going forward not to vary too much from first quarter.

Alexander Jones
Analyst, Bank of America

Q

Thank you. That's clear. And just a second question on the volumes...

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

Just to make sure I'm accurate. Typically, fourth quarter is a weaker quarter, so could be a little weaker at the end of the year, but don't expect anything different in the next quarter.

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Alexander Jones
Analyst, Bank of America

Q

Thank you. That's clear. And just a second question on the volumes of that division. You called out in your comments a number of different drivers, auto, consumer electronics wide, there was an 11% decline year-on-year this quarter. How should we think about that into the second quarter, given sort of China COVID lockdowns ongoing, but then into the balance of the year, how do you think about that? Thank you.

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

Okay. So, thanks for that question. I want to point out, if you look at the numbers, it seems like quantities in IP division went down quarter-over-quarter. And what I want to point out is that we shut down two of our plants in China last year. Those two plants created quantity, but negligible profitability. Also, in our third site in China, we had a shutdown for over a month. So, that means that the realistic quantities went up, but because of those factors in China, mainly the shutdown of a – or rather the sale of one of our sites and the shutdown of the other quantities went down.

In terms of quantities going forward, we expect quantities in the second quarter to be similar to the first quarter. Maybe just a bit less in electronics related, but at the same time, more on clear brine fluids because some orders were postponed to the second quarter. The visibility in the second half is not as high as in the first half yet and that's very natural.

We could see if the situation in China persists and unexpected logistic issues happen as a result of the lockdown, that could have an effect. Right now we're not seeing that in terms of our bookings. And again, most of our business is contracted over 70% and it's even higher in China, is contracted annually. So, we don't see anything dramatic. But we did want to point out that there could be some effect due to the relative weakness coming about in electronics and automotive. And again, these are a result of the lockdown in China.

Alexander Jones
Analyst, Bank of America

Q

Great. Thank you very much.

Aviram Lahav
Chief Financial Officer, ICL Group Ltd.

A

My mic is on. So, [ph] one for that (00:28:37)...

Operator: Moving on to the...

Aviram Lahav
Chief Financial Officer, ICL Group Ltd.

A

...and potentially in China because it's a significant part of the division is that shipments might come in later. So, on a quarterly basis, there can be some delays because China – the ports in China, there's a massive lockdown going on these days, depends how it will go about. If it makes sense to you, I think it's a general issue that prevails there. I think that over time this must be resolved. But at least in Q2, by the way, it can be that things will be [ph] playing (00:29:08) between the quarters. That's just an effect of the shipping itself.

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Operator: We have another question coming from the line of Geoff Haire from UBS. Please go ahead with your question.

Geoff Haire
Analyst, UBS AG (London Branch)

Q

Actually, my question has been answered previously, so I don't need to ask it. Thank you.

Operator: Thank you. We have another question and it comes from the line of Joel Jackson from EMO Capital (sic) [BMO Capital] (00:29:40). Please go ahead with your question.

Joel Jackson
Analyst, BMO Capital Markets Corp. (Canada)

Q

Hi. Good afternoon. You don't get off that easy with me. I want to talk about potash, obviously. Maybe I could start off with a high-level question, gentlemen. If I look at your EBITDA, expected EBITDA range – midpoint, sorry, for 2022, it's a $2 billion increase for 2022. Can you bridge that? How much of the $2 billion of EBITDA increase in 2022 would come from potash price? How much would come from other businesses, other – can you break down that bridge as granular as possible for your business, please?

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

You mean just the delta?

Joel Jackson
Analyst, BMO Capital Markets Corp. (Canada)

Q

Yeah. The delta, the $2 billion delta from 2021 to 2022. How much of that is potash price? How much of that is other things and other businesses? As much as granular as possible would be very helpful.

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

All right. So, you can see we have a number for the specialties business, right? So, the specialties accounts for about [ph] 300 and some (00:30:49) at the midpoint, and the rest is about 75% potash and 25% phosphate. To give a better sense, to give a little more, I mean, Q2 obviously potash prices are going to be higher than Q1.

First half sales are already behind us. So, we already know the numbers for the first half. And for the second half of the year, we have higher prices for potash in the third quarter, but the third quarter is not sold out yet. So, we took conservative numbers for the third and fourth quarter on potash. The average selling price in the second quarter for potash is expected to be around $800.

Joel Jackson
Analyst, BMO Capital Markets Corp. (Canada)

Q

Okay. So, that's very helpful, so...

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

Yeah. Sorry, $800 is the number before transport costs. So, the realized price will be around $760-ish.

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Joel Jackson
Analyst, BMO Capital Markets Corp. (Canada)

Q

Thank you. So, if I do that math, it sounds like 60% to 65% of the 2022 EBITDA delta is potash price.

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

That's pretty accurate, yes.

Aviram Lahav
Chief Financial Officer, ICL Group Ltd.

A

A bit less, I think.

Joel Jackson
Analyst, BMO Capital Markets Corp. (Canada)

Q

Okay. So, then my next question would be, so at these potash prices, obviously, we're seeing a lot of peers talk about demand destruction and prices not going higher or lower. What is your view right now on price here, of demand here? Has the price hit the right level now to balance demand versus missing Belarusian ton? Do you think we're going to see some softness? What are your views on where the market goes next in potash?

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

Okay. So, there's short term and there's a long term. In the short term, the basic facts are that there's a lack of supply in the market. There's over 2 million tons of potash missing for Brazil. Brazil has to have the potash because the type of land that is there in Brazil demands potash, so they can't skip a season or something.

There will be some demand destruction in Europe. Some in Europe will skip the season. That means that potash deliveries for this year will be lower. It will be lower – it may be lower in the States as well. In the short term, that doesn't do too much because, again, the market is undersupplied. For the short run, it's actually a better news for stability for prices, because anybody that skips a season this season will need more potash next year. So, that means that once market comes back and maybe if sanctions are lifted and product comes back, there'll be more demand for potash next year.

So, in terms of potash dynamics, there will be demand destruction. There's quite a lot of uncertainty yet in terms of decisions to be made by distributors and farmers. There was a lot of destocking, so stock levels are low. In China and India and even in Brazil, they're getting lower by the day now. And in the US because of the wet season, there wasn't as much application of potash at this season. So, there was some softness in the US, but I expect that to change towards the fall season.

So, I think demand will be healthy enough to sustain these existing prices. It's difficult to speak about higher prices because these are some – these are uncharted waters. We've never been here before. We can say that there is demand that's not going to get the product because some countries that don't have the means and don't have the access to Belarus or even Russian product are not going to be able to get product, that's going to cause quite a lot of hunger problems in various places, and that in itself can create additional dynamics.

We do see that in some countries, governments are becoming aware of potential demand destruction that will cause hunger issues. And as a result, India has raised subsidies very significantly for potash and for phosphate. Countries like the UK have supported fertilizer companies directly. I read a couple days back that France is now

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giving grants to farmers at the private farmer level to make sure that applications happen, because at the end of the day, if there's not enough application of fertilizers and fertilizers are responsible for about 50% of global production of agriculture, there won't be enough food. The implications are very, very significant.

And of course, the same with crop prices, especially wheat, because of the Ukraine-Russian situation, I don't see wheat going lower. Maybe the contrary, so if wheat goes up and other crop prices go up, there could be room for price increase, but again I'm not expecting, we're not modeling price increase. Quite the opposite, we're trying to be as conservative as possible.

Phosphates depend more on decisions made by Morocco and China. China, in terms of export policy and Moroccans in terms of how much DAP they will produce. They don't have the quantities of ammonia necessary for DAP. So, that means that there will be – there could be shortage. And of course, there already is shortage of acid, white phosphoric acid. So, there are all kinds of supply dynamics that need to work themselves out.

And all in all, we don't see – we definitely don't see a softness in potash because Belarusian product is not coming out of the mines and not entering into the market and that's just product that's not going to come into the market. If they get back to the production, it'll be in the future. In the future, there will be higher demand because of some demand destruction at these times. And so, that's pretty much what I have to give you as color on the market.

India, China working very hard to make sure that there's enough food for their populations. US, a little bit of softness because of weather issues. Europe, quite a lot of demand destruction, so less fertilizers this year and more next year. Brazil, not clear still how they're going to get the additional fertilizer that they need. Potash already mentioned, over 2 million are missing and other fertilizers where they depended on Russia. They depend on Russia. It depends how much product from Russia is going to come to Brazil. Currently, we see that a lot of product came in in the past month-and-a-half, but that product went out of Russia long time ago. Not clear if significant deliveries are going to be able to arrive in Brazil in June and July.

Aviram Lahav
Chief Financial Officer, ICL Group Ltd.
A

Maybe just to note, Raviv, that India and China together, they comprise below 30% of the total potash sales for ICL in a year. So, in the latter part of the year, the spot prices can be quite beneficial to ICL, if they continue to sustain, obviously.

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.
A

Joel, that's the best we can do for now.

Operator: Okay. Joel, you might be on mute. Can you unmute yourself? We are moving to the follow-up question, and the question comes from the line of Laurence Alexander from Jefferies. Please go ahead with your question.

Laurence Alexander
Analyst, Jefferies LLC
Q

Hi. Yeah, good morning or good afternoon. Just wanted to get your thoughts on the M&A landscape, given how well your cash generation is doing and how poorly tech valuations are doing. So, are you seeing different kinds of opportunities, or are you changing the types of companies in your M&A pipeline?

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Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

That's a fantastic question. We've been a little frustrated in the past year, year-and-a-half, because we're looking at M&A opportunities and we're excited to grow our business. And at the same time, valuations have been a little crazy. Hopefully, if there's – I mean, I'm not hoping that the markets go down, don't get me wrong, but if valuations rationalize, then definitely that creates more opportunity for us.

We want to have and we do have the liquidity and we're generating plenty of cash and we're going to be generating even more cash. So, we want to be opportunistic. We have our eyes on a few interesting targets, and we hope to be able to do more in terms of M&A in the next couple of years than we did in the past couple of years.

Laurence Alexander
Analyst, Jefferies LLC

Q

And for Innovative Ag Solutions, what do you see as the normalized run rate, because kind of the underlying improvement in that segment is a little bit harder to track with the [ph] fly ups (00:41:40) you're seeing?

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

Yeah. For this year, we're going to see a very nice growth. The growth that you saw in first quarter is going to continue for the rest of the year. The growth in Brazil is phenomenal, so much stronger than it was last year. I do also want to point out, like I pointed out in the IP division, that if you look at the IAS results, it would seem that quantities actually went down.

When you put Brazil on the side and look at the rest of the business, it looks like quantities actually went down a bit. And that, again, doesn't tell the right story because of two issues. One, in Aviram's remarks, he mentioned the fire we had in our facility in Germany towards the end of last year, and that facility was not working in the whole first quarter.

So, the quantities that typically come in Europe from that site were not there in the first quarter. And of course, that's going to change for the next three quarters. The other thing is that in Boulby, in order to reach our targets for polysulphate production, we took down salt production, which is low value and does not do anything for our P&L, but we took down production by 65,000 tons. And those two issues, the facility in Germany and the salt took the quantities of the division down. But those, of course, are one-time events that will not stay with us.

So, all in all, the growth in the legacy business of IAS has been around 20% and the growth in Brazil, even more than that. And it's also a growth with growing margins. So, we see a margin expansion as we grow, which is also very nice. Will we continue to see margin expansion? Again, that depends on what happens to overall fertilizer prices. So, I'd rather be conservative and not project that. But we see very nice margins. We had low-single digits in this business just two years ago, and now we're getting to high-double digits and it's nice to see that. Thanks for the question.

Laurence Alexander
Analyst, Jefferies LLC

Q

Sorry, just one clarification, if I may is, how do you think about mid-cycle EBITDA for your specialty businesses? If the current conditions sort of normalize in two, four, five, however many years, I mean, just what do you see as the mid-cycle kind of benchmark?

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Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

So, mid-cycle for IP business would be above 30%. We saw significantly above 30%. But mid-cycle, I would say, at the minimum more than 30%. We had that in the past. The reason is we're a market leader, we're a price leader. So, that business is very solid and safe. Yeah.

In IAS business, as we presented in our long-term plan, we're targeting 15% plus. And in our phosphate business mid-cycle, we're also targeting above 10%. But again, phosphate plus 10% is when our commodities business is making close to zero. So, on our specialty phosphate business, we're targeting plus 17%. That's the number that we had in our long-term plan.

Laurence Alexander
Analyst, Jefferies LLC

Q

Okay, great. Thank you very much.

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

Thank you.

Operator: Our next question comes from the line of Vincent Andrews from Morgan Stanley. Please go ahead with your question.

Will Tang
Analyst, Morgan Stanley

Q

Hi, guys. This is Will Tang on for Vincent. Thanks for taking my question. Now that I feel Boulby has turned to profit kind of given the higher prices in production, can you talk about what your expectations for the business are for the rest of the year? And I guess whether we can expect it to continue turning to profit long term from here on out.

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

Yeah. So, we got to 238,000 tons of production in the first quarter, which is a run rate of about 1 million tons. So, we expect that to be relatively stable for the rest of the year and end up the year at about 1 million tons. In terms of pricing, pricing went up from about $115 in the first quarter of last year to $210. The first quarter of this year, it has to do with commodities, but much more than that, it has to do with the positioning of the product.

We call the product – we branded the line of products as polysulphate FertilizerpluS. The product is an organic product that has some potash, a lot of sulfur and micronutrients such as magnesium and calcium. And the positioning is that it's a high-quality organic fertilizer with no chemical process involved and the reliability of the product is high. The results are very good.

And looking forward, we expect that the premium that some markets will pay will be higher due to the organic certification that we have now both from the EU and from the US. And the growing appreciation to the results of the product that we're selling, it took us between three to four years to penetrate markets. And now that we have, we expect to maintain our profitability, maybe even grow it at second half of the year as long as no dramatic changes happen.

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And we feel that over time we will build additional premium because of two reasons. One, because of the positioning of the product is high-value organic product. And second, because we're developing a whole line of product that involves combinations of polysulphate with other nutrients, granulated products that create better use efficiency for plants.

And those additional products that we're developing under the brand are being accepted very well. And each one that comes out and proves its successful value gets us more premium. So, the product portfolio success together with acceptability of the branding is going to give us additional premium and higher prices in the future that will enable us to grow our margin. Hope that answers.

Will Tang
Analyst, Morgan Stanley

Q

Got it. Yeah. Thank you. And then I guess just as a follow-up. Between last quarter and now, you've kind of almost doubled your earnings expectations for 2022. I know you briefly touched on M&A a little bit, but could you give us a run-through again about how you're thinking about, I guess, allocating that excess capital that maybe you weren't expecting few months ago?

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

So, again, remember, you said we doubled and we already said that almost two-thirds of that is coming from potash prices. Remember that when we modeled in the beginning of the year, we explained our conservative guidance. We were at the time selling potash at $249 in China, and $440 or so in India. And just that China prices went to $590, which is well over 100%. And of course, Brazil prices went from around $650, $700 at the time that we put together our original model to currently about $1,200 per ton. So, it's pretty straightforward why that's changed.

Again, we're sold out for the second quarter, so I gave the number of about $760 realized price for the second quarter. In terms of second half visibility, it's still too early, because although, like Aviram mentioned, one-third of our product is already sold at $590 to China. And India, we don't expect that to change. The rest of the sales really depend on developments in the market in terms of prices and who knows what's going to happen in terms of the situation in Ukraine and, potentially, the food inflation causing the world hunger. There's too much volatility out there to give an accurate projection at this point.

Aviram Lahav
Chief Financial Officer, ICL Group Ltd.

A

Just to add that potash, of course, is the dominant factor. But phosphate is also up very considerably between the time that we estimated and what we see now. It's also about $400 million [ph] up in (00:52:04) operating income terms. So, that's another significant factor. You put those two together with the IP side and some on the IAS side and you get the difference. I think that bridge is for you logically what happened in the first estimate and what we see now.

Will Tang
Analyst, Morgan Stanley

Q

And then I guess as a follow-up to that, could you kind of talk about how you're thinking about allocating excess cash that you guys are expecting to generate?

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Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

Well, we're paying out $306 million as a dividend, which is pretty much the net cash generation and the free cash flow generation this quarter. Looking forward to the rest of the year, we're going to generate a significant amount of additional cash. And we're considering M&A opportunities as well as having enough reserves to be able to protect our position or better our position in terms of the interests we have with government concession and other issues that where we could be opportunistic to take care – to take advantage of these very good times that we're going through in order to better our long-term situation.

Aviram Lahav
Chief Financial Officer, ICL Group Ltd.

A

Maybe just one comment, if I may, on capital allocation. The working capital side, as we grow our business in Brazil, it demands more capital than most probably most of the rest of the world. Receivable terms are longer. Especially around receivables, trading terms are longer. The margins are very nice, but we have to allocate some working capital to Brazil as well. Anybody that works there, it's a well-known fact.

Will Tang
Analyst, Morgan Stanley

Q

Got it. Thank you.

Operator: And we have a follow-up question coming from the line of Joel Jackson from BMO Capital. Please go ahead.

Joel Jackson
Analyst, BMO Capital Markets Corp. (Canada)

Q

Hi. I got cut off at the end there. I appreciate your color on polysulphate. So, I have two questions on that. If you think the $215 a ton selling price, can you somehow in your mind come up with how you divide the value that a customer's paying at, say, $215 between potassium, sulfur, calcium, non-chloride, organic, like is there – how does your marketing team think of the value the customer gets at $215 among all those different buckets? Does that make sense when asking?

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

It's a good question. I would say, look, the potash component is 14%. So, I think it'll take a long time until we get more than the potash value for those 14%. The rest is coming from the combination of the nutrients and their effect that the results that they yield. So, as the results become clearer and as we go from one season to the next, our position improves because if you get higher yields, then you're not going to pay 100% of the higher yields because you're not confident yet that the result is going to repeat itself.

So, I think we'll need to have repetitive, good results with our customers to build the premium. And again, the combination of nutrients is not just the nutrients embedded in the polysulphate, but we're also creating now additional products that combine polysulphate with other nutrients in order to increase the combined value. And again, some of those products are being accepted very well, including PKs and NPKs with polysulphate.

Joel Jackson
Analyst, BMO Capital Markets Corp. (Canada)

Q

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Okay. So, now I'm going to ask this question at bit different. It's going to sound like Debbie Downer, so I apologize, but I'm being honest. So, you got the 1 million ton production run rate and you're at the highest commodity prices ever, potash prices cannot go higher. Sulfur prices cannot go higher, [ph] let's just say (00:56:36), or as high as they've been, and you're just barely turning a profit on this product now over a decade into it. Is that not a sign? Because commodity prices are going to be cycle, [ph] they'll go in (00:56:47) cycles, they're going to go down. Is that not a sign that this business is never going to be anything other than really just around breakeven? And that might encourage why nobody should build any more capacity of this product, you or anybody else.

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

Okay. So, first of all, it's a very fair question. We're not 10 years into this product. We're 4 years into this product. The mine used to be potash mine and we're building our polysulphate business in the last four years or so. The reality is that it may not be a high-margin business on its own, but given the results that we have so far, we know that in combination with other nutrients, we get some tremendous results. And again, this is for very specific types of land and markets. So, does the fact that we think that we can make it a profitable business and we can command just as good pricing in commodity down cycles because, yes, the embedded value of the potash will go down, but the premium and the acceptance will go up.

Does that mean that it's a multimillion ton market? The answer is no. We think that the world needs 1 million or 2 million tons. It doesn't need more than that. In order for somebody to sell more than that, they'll have to make a call, what their assessment of the market is. Our assessment of the market is that we are nicely sized for a niche market, if you will. That's why we're treating it as a specialties market – as a specialties product, is going to be sold as a specialties market. It has service around it. It has logistics around it.

We don't think that it can be profitable selling as a commodity business and competing with SOP or other type products. So, the short answer is yes. It's not easy to get to where we want to get. We're very happy that we're making money instead of losing money. At this capacity and given our proven success with the product, we don't think that it'll be a bleeding business that will take us back anymore. But at the same time, we still have a long way to go to get to the premiums that we want and get to the long-term stability that we feel safe about making a nice margin in this business.

Joel Jackson
Analyst, BMO Capital Markets Corp. (Canada)

Q

Thank you for all that color.

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

A

You're welcome. Thanks for the question.

Operator: Thank you. We have no further question at this point, so I hand the conference back to you.

Raviv Zoller
President & Chief Executive Officer, ICL Group Ltd.

Okay. So, before I hand it over to Peggy, I just wanted to thank Dudi, who's been with us for a few years, and he's moving to his next assignment. And we wish to thank him for years of great work on IR in ICL. Congratulations on

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your new job and lots of success. And we hope you continue to be proud of us on what we're doing. And I'll turn it over to Peggy.

Peggy Reilly Tharp

Vice President-Global Investor Relations, ICL Group Ltd.

Thank you, Ravi, and we will speak with you again next quarter.

Operator: Ladies and gentlemen, this concludes today's conference call. You may now disconnect your line. Once again, thank you for your participation today.

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