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Call Participants

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Presentation

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the ICL analyst conference call. [Operator Instructions] I must advise you that this call is being recorded today.

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

Peggy Reilly Tharp
Vice President of Global Investor Relations

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 U.S. 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.

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 & CEO

Thanks, Peggy, and welcome, everyone. I'd like to begin by recognizing all the expressions of concern we've received since October 7. In addition to hearing from you, our investors, we've also heard from our customers, suppliers, competitors and so many others. These heartfelt messages are greatly appreciated as we navigate the current situation in Israel. While I will provide more detail later in this call, I would like to assure you that while there are some challenges, our operations in Israel continue without significant disruption.

For the third quarter, you can see a quick overview of results on Slide 3. Sales of $1.86 billion were flat sequentially as we saw the beginning signs of stabilization in many of our end markets. Adjusted EBITDA of $346 million was down versus the prior record year, as expected.

During the quarter, we completed significant destocking efforts, which in part helped contribute to our strong cash generation. For the third quarter, we generated more than $400 million of operating cash flow and $217 million of free cash flow.

We delivered $0.11 of earnings per share and distributed nearly $70 million in dividends to our shareholders as part of our long-standing policy to pay out 50% of adjusted net income each quarter.

While I will discuss each of our businesses in more detail, I would like to call out our strong potash deliveries in the third quarter, and we are now sold out for the year.

For our phosphate specialties, we had another solid quarter and are in the process of Board approvals for the first offtake agreement for our new battery materials facility, which is now under construction in St. Louis.

I would ask you to now turn to Slide 4 and a 3-year look at our key financial metrics. While sales were down year-over-year, as expected, they were up versus 2021 on both a quarter and year-to-date basis. Adjusted EBITDA was down for the quarter due to lower pricing across all of our businesses. However, we saw some increases in volumes. During the quarter, we benefited from better raw material prices and transportation rates and saving efficiencies overall. However, this was obviously not enough to offset the decline in prices from 2022.

On Slide 5, you can see our specialties sales. While 2022 was an exceptional year, you can see that our year-to-date 2023 specialties sales remain ahead of our more normalized 2021 results. Overall, specialties sales were higher versus the first 9 months of 2021. Similarly, while down year-over-year, our adjusted EPS for the first 9 months of the year exceeded the same time frame in 2021. In the center of this slide, you can see our third quarter operating cash flow, which was up versus the second quarter of this year and our free cash flow, which was roughly flat for the same time frame. When compared to 2021, you can see we experienced significant growth in both operating and free cash flow on both the quarterly and year-to-year basis.

I would now like to begin our segment review with Industrial Products on Slide 6. Third quarter sales were $267 million, while EBITDA was $42 million. As we indicated in June, the recovery in demand for flame retardants has been much slower than predicted. During the third quarter, bromine prices hit bottom, and we also completed some additional destocking efforts. Demand is now slowly picking up in the fourth quarter, and our unique cost position and focus on long-term customer partnerships is allowing us to gain market share.

Demand for clear brine fluids has remained strong as oil drilling activity has increased. Our specialty minerals business unit, targeting food, pharma and other end markets, performed in accordance with our expectations in the third quarter. Overall, our Industrial Products division started gaining market share toward the end of the quarter. As the leading global producer of bromine, we have been able to leverage our efficient cost position and remain profitable despite unique challenges which may have significant impact on smaller manufacturers.

As I said last quarter, our Industrial Products business remains on track for the long term, and we do not expect recent developments, which are predominantly external to have a material impact on the execution of our 5-year plan. We are beginning to see demand recovery becoming visible in some end markets and expect to gain benefits from cost savings initiatives launched in recent months.

Turning to Slide 7 and our Phosphate Solutions division where we reported strong results relative to current global market conditions. Third quarter sales of $620 million were up sequentially, while EBITDA came in at $117 million and was substantially impacted by lower prices in the market, mainly on the commodity side of the business.

For the quarter, our phosphate specialties business demonstrated resilience and represented approximately 60% of Phosphate Solutions sales and nearly 50% of EBITDA. Specialties EBITDA margin of 15% is in line with the third quarter of 2021. Free cash flow was very favorable in the third quarter as we improved our working capital position for Phosphate Solutions. We also benefited from lower raw material and transportation costs during the quarter as we leverage our supply chain capabilities.

Sales and volumes vary by end market and region and our industrial specialties showed strength in Asia Pacific due to resurging demand for battery materials. For our specialty food phosphates, we experienced strong pricing in North America, and overall, food prices continue to be elevated on a global basis.

Europe remains challenging in general as it has for the past 4 quarters with increased competitions from Chinese suppliers, and we continue to defend our market share where necessary in this region. Chinese producers are also becoming more apparent in South America as China continues to export its excess supply. In both Europe and South America, we implemented targeted efficiency efforts to optimize our logistics, raw material costs and energy costs.

For our battery materials expansion in St. Louis, we are on track for this facility to be operational in late 2025. While there has been a lot of noise in the news about electric vehicles lately, we remain excited about the long-term potential of the overall energy storage and electric vehicle industries. We have always expected this to be a gradual ramp-up and are pleased to be the first mover for essential battery materials produced and sourced in the United States.

As I mentioned earlier, we soon expect to announce our first long-term strategic partnership, which will help in creating the next generation of battery and energy storage solutions in North America. We are also seeing growing traction and engagement from additional potential offtake partners.

On Slide 8, you will see our potash results and note our supply is sold out for the remainder of 2023. For the third quarter, sales were $526 million as quantities increased to approximately 1.28 million metric tons with higher volumes to Europe, Brazil and China. EBITDA came in at $164 million and prices began to stabilize.

Our Potash CIF price of $342 was down versus the same quarter in '22 but up slightly versus the third quarter of 2021. In Spain, our production continued to face geological constraints in the third quarter as we continue to transition away from a lower-grade mineral geography, which will carry on over the next few months. This shift is in concert with other efficiency efforts there as we strive to increase outputs and decreased costs in Spain. We also continue to pursue cost savings across our entire potash portfolio and are on track with our plans.

Turning to Slide 9 and our Growing Solutions business, which delivered sequential improvement in both sales and EBITDA in the third quarter. Sales were $550 million, while EBITDA was $37 million. During the quarter, significant destocking was almost fully completed, driving higher quantities across the division and contributed in part to all-time record quarterly cash flow and some gains in market share. In total, Growing Solutions has reduced its inventory by approximately $140 million since the beginning of the year, which is in line with our plans.

Savings and efficiencies efforts for 2023 also remain on track with improvement in the third quarter. Our destocking efforts also helped our Brazilian business where we saw record sales with strong volumes. We gained market share during the quarter and also broken all-time sales record in our foliar business as we remain focused on higher-profit products. For other key geographies, we see demand returning in Europe, especially for our FertilizerPlus products and the pickup in demand is also becoming visible in China as well.

I would now like to draw your attention to Slide 10 and a review of the key areas where we remain focused. Efficiencies have been a theme throughout 2023, and each of the divisions enhanced their efforts in the third quarter. Our Industrial Products team has leveraged its efficient cost position during a challenging industry recovery; while Phosphate Solutions is focused on optimizing its logistics and raw material efficiencies, along with its energy usage on a global basis. In potash, we have benefited from ongoing efficiency efforts at the Dead Sea and are looking for advances in Spain to materialize, while Growing Solutions' efforts to efficiently destock high-priced inventory helped drive their third quarter cash flow and also leaves the business well positioned for additional growth as demand shows signs are beginning to improve.

In total, all of these efforts helped drive our strong total operating cash flow of $1.18 billion year-to-date, and Aviram will discuss our efficiency efforts in more detail.

Growing our specialties product portfolio remains a key long-term priority. Our investment in battery materials for energy storage and electric vehicles will help position the phosphate specialties business for the future and further diversify end market exposure. Our Industrial Products business remains the leader in the global bromine market, which will continue to see long-term growth as electronics become even more firmly embedded in our AI-driven future. For Growing Solutions, we're excited about expanding our reach in growing markets such as Brazil and India and as we continue to develop new, more sustainable products for the future of agriculture.

Our innovation focus on sustainability has been rewarded by a robust, high-value, new product portfolio and improved ties with third-parties as well as improved ratings, including our recent upgrade by MSCI to BBB. We expect to continue to improve our various rankings.

In terms of M&A, new opportunities have recently surfaced, and we have also recruited [Uri Perelman] to join our management team. [Uri] joins ICL as an Executive Vice President and as our Chief Business Development Officer. He will help accelerate our business development, M&A and strategic partnership efforts. [Uri] has an impressive track record in business development, successfully meeting growth processes in several companies, and we are very excited to have him join the team.

Finally, I would like to provide an update on the situation in Israel. I'm deeply saddened to share that we lost several members of our ICL family due to the tragic events that took place on October 7 and in the aftermath. Our main focus has been on providing our employees impacted by the hostilities with their most immediate needs. At the same time, we've been working to keep our employees safe, both at work and home, and continue to adopt all the necessary measures, both at the sites and during transport, to minimize any potential risks. From a business standpoint, we have faced various operational challenges caused by the war but have succeeded in minimizing disruption and maintaining good production levels, thus meeting all of our customer commitments.

As of last week, approximately 600 of our more than 4,500 Israeli employees have been called to reserve duty, a situation that has required some adjustments, which have been working effectively. As many of you have inquired, transportation of goods has become a unique challenge, but our teams have been managing quite well. We are doing our best to get back to our normal business routine and, as you can imagine, we are monitoring the situation on a constant basis. We will continue to make all the necessary decisions and take the required actions to guarantee our business continuity while keeping our employees and communities safe.

ICL has been actively reaching out to the impacted communities and offering them support both material and emotional. And I cannot even put into words how proud I am of our employees who have been volunteering, night and day, to support the people and communities affected by the tragedy Israelis face. While I always thank the entire ICL family of employees all around the world for their hard work and contributions each quarter, this is an especially heartfelt sentiment today. The tenacity of the team in Israel has been inspiring, and the unwavering support of our global colleagues has been heartwarming. We are resilient, and we will prevail as before.

Again, we thoroughly appreciate all of your kind words and prayers and hope the situation will be improved by the time we report our fourth quarter results.

And with that, I would now like to turn the call over to Aviram.

Aviram Lahav
Chief Financial Officer

Thank you, Raviv, and to all of you for joining us today.

Let us get started on Slide 12, where you will see some very familiar external macro pressures. While many of these remain unchanged from the beginning of this year, as Raviv just discussed, the war in Israel, which began in the fourth quarter, brings additional geopolitical issues. Both inflation rates and interest rates have moderated, but remain mixed on a global basis. Overall, global growth remains subdued and the economic recovery in China has been weaker than expected. From an agriculture perspective, grain prices are leveling off and fertilizer prices have stabilized.

On Slide 13, you can see some of the trends I just discussed. While inflation rates are generally trending down, they remain persistently elevated on a historical basis, as do interest rates.

And on Slide 14, you can see the trends in grains and fertilizer prices.

On Slide 15, you can see the expected trend for electric vehicles over roughly the next decade. As Raviv mentioned, there has been a great deal of noise about EVs lately. But as you can see, the rate of growth has always been expected to be gradual. Electrical vehicles sales are on track to hit 9% of all cars sold in the U.S. by the end of this year. That's a 50% year-over-year increase. And it is the second year in a row that EV sales have surged by that amount. The LFP battery materials we will be producing at our facility in St. Louis will be used not only in electrical vehicles, but also by the energy storage industry. It is important to remember that renewable energy needs to be captured and stored for use by EVs and in other applications, and the investments we are making today will help advance such efforts.

If we now turn to Slide 16. On the left side, you can see the sales bridge from the third quarter of last year to sales of $1.86 billion this year, with each of our segments showing a year-over-year decline. Importantly, on the right side of the slide, you can see that while quantities were up, prices had an overwhelming impact as commodities were at all-time highs last year.

Similarly, on Slide 17, you can see the impact prices had on our third quarter adjusted EBITDA of $346 million. Once again, quantities contributed positively in the quarter, while lower prices, especially potash prices, made a significant impact. We did benefit from lower raw material and transportation costs and also from the savings and efficiency programs we've put in place in each business and on a corporate-wide basis earlier this year. We expect benefits from our cost reduction and efficiency efforts to be even greater going forward.

As we showed you last quarter, on Slide 18, you can see that not only is ICL a leader in terms of cost efficiency, we are also a leader in terms of pricing. While we are not as big as some of the potash producers out there, this is actually a benefit to ICL as it gives us the flexibility to quickly shift in and out of markets based on profitability.

I would now like to review a few highlights on Slide 19. As a result of our savings and efficiency activities, we're able to decrease SG&A by approximately 11% year-over-year in the third quarter. Each of our businesses also worked to reduce working capital and high cost inventory. And as Raviv mentioned, our aggressive destocking efforts are now centrally completed. These efforts were part of an orchestrated plan. And while we did see some margin impact, we were able to gain market share as we reduce inventory.

Our destocking also helped, in part to drive our strong cash conversion. At quarter end, our available cash resources totaled $1.8 billion. For the third quarter, our net debt to adjusted EBITDA rate was a healthy 0.9. We also declared a dividend of $0.05 per share for the third quarter, resulting in a trailing 12-month yield of 5.5%. Taxes were $43 million, reflecting an effective tax rate of 23% for the third quarter of this year. This relatively low rate was mainly due to the devaluation of the shekel against the U.S. dollar and deferred taxes for carryforward losses related to the taxation of profits from natural resources.

Finally, you can see we reaffirmed our 2023 guidance calling for adjusted EBITDA of between $1.6 billion to $1.8 billion. And as we stated in today's press release, we expect to be in the middle of that range.
And with that, we can begin the Q&A.

Question and Answer

Operator

[Operator Instructions] Our first question today comes from the line of Alexander Jones of Bank of America.

Alexander Jones
BofA Securities, Research Division

Two, if I may, just to follow up on a couple of comments you made, Raviv. The first one on battery materials. You talked about this first customer contract or partnership that's nearing completion. Could you give us a little bit of an idea the sort of criteria you're looking for when signing contracts with customers in terms of volume commitments or returns or margin levels or technology commitments? That would be really helpful

And then the second one just on Industrial Products. You made a comment that demand is slowly picking up in Q4 so far. Could you expand a little bit on that in terms of different end markets you might be seeing that in or the magnitude of that so far?

Raviv Zoller
President & CEO

Okay, sure. Thanks, Alex. First of all, for battery materials, as you know, our plant is for 30,000 tons. And we'll be ready to start supplying towards the second half of 2025. We're looking for customers that are either automakers, battery makers or somewhere in between. And we're negotiating with quite a few potential customers. Some of the negotiations are closer than others. Some will take quite some more time until we can qualify and meet expectations.

We're talking about potential customers for a few thousand tons each. And the reason we mentioned is that because we have the first agreement come to fruition, and subject to Board approval of both sides during the coming days, we should be able to announce in a few days. So that's where we are on battery materials, again, 30,000 tons in total. We expect the facility can serve no more than 2 or 3 customers. And in the next few months, we expect to be able to discuss more than one customer. So that's on that.

On Industrial Products, we're talking about demand for electronics. Construction is still away from us. And I think the reason that we're seeing in electronics is that there is a level of demand that is slower than usual. But all the inventory in the supply chain is gone now, so we can actually feel the demand that exists. And that means that volumes are going up now, and it will continue to go up in the coming months. And as you know, we have long-term contracts. So that means that when we want to increase the volume, we can, and that's what we're doing these days.

In terms of how fast the recovery will be, we think it will take quite some time because there is yet to be seen robust demand for electronics. Even electric vehicles, demand is a little slower than was expected at this point. And also artificial intelligence, which is the next wave, is not something that we can feel at this minute and I'm talking about increased demand for servers. And of course, construction-related flame retardants is much farther away. So some of the demand recovery that we're seeing is because of the supply chain that is now not full of inventory and additional demand will come from the market once interest rates start going down, hopefully. I hope that answered it.

Operator

Our next question today comes from the line of Ben Theurer of Barclays.

Benjamin M. Theurer
Barclays Bank PLC, Research Division

So also just two quick follow-ups. One, to begin with, on the Growing Solutions piece, and you've talked about the destocking being significantly completed, clearly, it seems there was still an impact in the third quarter. So help us understand like how should we think about the fourth quarter and then maybe looking into the first quarter of 2024 just as it relates to the match of demand or like actual demand versus what the supply is going to be. How do you think about the cadence here? And what's like kind of a normalized level of profitability you expect in that segment, particularly given the volatility we tend to get out of Brazil? That would be my first question.

Raviv Zoller
President & CEO

All right. Thanks, Ben. In terms of what we're seeing in Growing Solutions, the destocking is materially over. And what that means is that we're going to see a normalized margin, which is more like 2021 margin. Going into 2023, we're already growing volume. We grew volume in Q3 even versus last year. So we expect growth of volume and better margin given higher prices and no need for destocking.

In Q3, we came in actually a little lower on EBITDA than we expected, and I think we'll see the same in Q4. Some of that has to do with internal planning. As some of the potash that we were going to supply internally to help promote some of our blends we're going to need for external customers, which means that some of the profitability that we expected in Q3 and Q4, we're not going to lose, but we're going to see it in the potash sector. But coming first quarter of 2024, we're going to see normalized profitability as we did in 2021. Of course, 2022 doesn't measure up to anything that we know. I hope that answered it.

Aviram Lahav
Chief Financial Officer

Ben, this is Aviram. Just one thing, take into account that this is agriculture and the seasonality part of it. So actually, as you know, Brazil will be still a very strong quarter seasonally, but less so than Q3. And the Northern Hemisphere has not yet started the season. So when you asked about Q4, take this also into account when you look at Growing Solutions, basically agriculture.

Benjamin M. Theurer
Barclays Bank PLC, Research Division

Okay. Perfect. And then actually one follow-up for you, Aviram, just on like capital allocation. How should we think about it? You talked about the dividend and, obviously, what the CapEx is. Cash flow is actually pretty strong still at roughly $1.2 billion on a year-to-date basis. So how should we think about the priorities, M&A versus CapEx, dividends/buybacks? What's like the kind of order? And where would you like to do more?

Aviram Lahav
Chief Financial Officer

Okay. That's a very broad question, and probably Raviv would want to chip in, especially on the M&A side, but I will say the following. We are generating very significant operating cash flow and it translates into a very healthy free cash flow as well. Part of it is destocking and part of it the working capital has gone down. And another element is that we are really, really operating the company very closely. And we've got a savings plan. And it's all coming together into, I believe, is a very healthy cash flow. You couple it with our capabilities, which we also note in the market, basically, cash is not a barrier to doing an M&A transaction.

So before M&A, I'll address it in a minute, we are really continuing to do everything we can internally in order to translate the performance on the P&L with the best cash flow we can get. 2023 is not an easy one. 2024, we have quite a lot of challenges as the whole industry has, but hopefully, we will be able to translate it into a healthy financial, let's say, cash flow results.

With regards to M&A, look, in the end, M&A, there's a capability to do it. And also we need to have relevant strategic targets that we want. And we said this oftentimes, we are not buying top line, we're not buying EBITDA. What we're buying is, if we go, we are trying to expand the horizon of the company, follow the strategy, to go specifically in the specialties side of our businesses and opportunities as they come. I think Raviv said this in his opening remarks that we are making the M&A team even more robust with a topnotch manager that heads it. And we're looking for opportunities. When it becomes relevant, we will not have financial burden to do this M&A transaction.

Raviv, do you want to add something to that?

Raviv Zoller
President & CEO

Just to remind everybody that we have a dividend policy that's been working well for us, which is a distribution of 50% of our adjusted earnings every quarter, and our investors are seeing a nice dividend return. And that still gives us ample cash to go through a transaction, to any transaction more or less, that we need. We were actually close to an M&A pretty lately that didn't go through because of valuation. Once again, we showed discipline given that, at the end of the day, we want to make sure that we do the right transaction.

We don't think that the share buyback is the right use for cash in a company that's targeting growth. We've also seen our competitors acquire shares at very, very high valuations. So we may be closer than we were in the past, but we're not close yet to actually approving such a program, unless we see that it takes us a lot more time to go through the M&A that we've planned. M&A has first priority before other things.

Also, I believe that Aviram didn't mention that, in terms of CapEx, we expect CapEx to be more or less in line with 2023. There'll be somewhat of an addition because of our LFP plant, which is an important venture for the company's future, for our growth. So that's going to require another $100 million or so next year. So we expect next year's CapEx to be circa $100 million more than the CapEx this year and, again, targeting LFP.

Operator

[Operator Instructions] Our next question today comes from the line of Joel Jackson of BMO.

Joseph Vaccaro
BMO Capital Markets Equity Research

This is Joseph on for Joel. So first of all, we just wanted to say we are shocked by all the events over the last month and hope that everyone at ICL is doing okay. So with that, for my first question, could you guys just please rank the outlook for the different major potash markets and how those views compare to your thoughts maybe 3 years ago? And also, what are your initial thoughts on global demand for 2024 relative to 2023?

Raviv Zoller
President & CEO

Okay. So first of all, thanks for your kind words. We appreciate it. Your support means a lot. In terms of potash market, currently, we're expecting demand next year to be around 68 million to 69 million tons, following about 60 million to 61 million tons last year and about 64 million to 65 million tons this year. In general, inventories are low in most regions, and there's a need for replenishment of inventory. Chinese inventory is relatively I wouldn't say high but it's not low. But at the same time, there's a lot of demand coming out of China, so there's a healthy environment for next year as well.

As you know, prices have stabilized and demand is strong. We're sold out for the year, of course, like I think everybody else. And we see strong demand in Brazil, strong demand and even rising prices in the U.S. India, very low inventory. We're not currently selling to India in the past couple of months, but I'm sure demand will be there. There is some subsidy issues, I guess, both in potash and in phosphate, and we'll see how that turns out.

In terms of global supply, we still see Belarusian product being 3 million or 4 million tons lower than capacity. Given the current demand, we think it's a healthy environment for next year. Longer term, we don't see any major disruption until potentially BHP comes to the market. They say in '26, it seems a little optimistic to us. But again, we don't have detailed information to say anything intelligent about it at this point.

So that's the demand. There's a need for replenishment. The affordability is higher than average. The overall atmosphere in most regions is positive. European potash is still selling at around $400 and even more. We expect fourth quarter average potash price to be almost at the level of third quarter. In terms of selling prices, nothing really has changed. Just at the beginning of the third quarter, we were still selling at higher prices in some regions. So that's pretty much what we're seeing at this point. In terms of our production, we will be next year expecting 4.7 million to 4.8 million tons. It's what our initial expectation is. I hope that answered it.

Operator

We have no further questions. Please proceed.

Raviv Zoller
President & CEO

All right. So thanks very much for joining us. We appreciate it. And hope for the safety of all, and looking forward to coming back and reporting to you at the end of the next quarter, reporting for the year. And by then, we'll be able to come out with and give you our forecast for next year. Thank you very much.

Aviram Lahav
Chief Financial Officer
Thank you. Thank you very much.