Sensient Technologies Corporation

Moderator: Lori Hauser
April 25, 2018
10:00 a.m. CT

OPERATOR: This is Conference #1249634

Operator: Good morning, everyone. Welcome to the Sensient Technologies Corporation First Quarter 2018 Conference Call. Today's call is being recorded. At this time for opening remarks, I would like to turn the call over to Mr. Steve Rolfs. Please go ahead, sir.

Stephen Rolfs: Good morning. I'm Steve Rolfs, Senior Vice President and Chief Financial Officer of Sensient Technologies Corporation.

I would like to welcome all of you to Sensient's conference call to discuss 2018 first quarter financial results. I'm joined this morning by Paul Manning, Sensient's Chairman, President and Chief Executive Officer.

This morning, we released our 2018 first quarter financial results. A copy of the release is now available on our website at sensient.com.

During our call today, we will reference certain non-GAAP financial measures, which we believe provide investors with additional information to evaluate the company's performance and improve the comparability of results between reporting periods.

These non-GAAP financial measures remove the impact of restructuring costs, currency movements, the impact of the 2017 U.S. tax legislation and other costs as noted in the company's filings. Non-GAAP financial results should not be considered in isolation from or as a substitute for financial information calculated in accordance with GAAP.

A reconciliation of non-GAAP financial measures to the most directly comparable GAAP financial measures is available on the Investor Information section of our website at sensient.com and in our press release. We encourage investors to review these reconciliations in connection with the comments we make this morning.

I would also like to remind everyone that comments made this morning, including responses to your questions, may include forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995.

Our statements may be affected by certain factors, including risks and uncertainties, which are discussed in detail in the company's filings with the Securities and Exchange Commission.

We urge you to read Sensient's filings for a description of these factors. Please bear these factors in mind when you analyze our comments today. Now we'll hear from Paul Manning.

Paul Manning: Thanks, Steve. Good morning. Sensient reported adjusted earnings per share of $0.89 in the quarter compared to $0.82 in last year's first quarter.

Color had a very good quarter, reporting solid revenue and profit growth driven largely by the cosmetics and the foods businesses. The results in cosmetics continue to be very strong with robust global demand in end markets.

We have strong sales and technical resources around the world to help our customers deliver unique formulations for their product, and we are making further investments to increase cosmetics production capacity.

We also continue to emphasize the commercialization of new products, making it easier for our customers to manufacture their products. For example, our cosmetics team recently received the 2018 Beauty Industry

Award for the best color cosmetic ingredient at the recent In-Cosmetics Global Trade Show.

The food color business has also performed very well in the quarter with strong natural color growth in North America and Asia Pacific and I expect these strong results to continue as the year progresses.

During the quarter, we had a number of significant natural color wins, including several natural conversion opportunities with high-profile brands. We also completed the acquisition of GlobeNatural's natural color business.

This acquisition gives Sensient significant new natural color production capacity and solidifies our supply chain for several key raw materials.

Sensient will maintain its technical and market leadership position in natural colors as customers continue to demand natural colors that perform at parity with synthetic colors.

Overall, Color performed very well in the first quarter, driven by new wins and I expect the group to meet my targets of mid-single digit revenue growth and high single-digit profit growth for the year.

Asia Pacific's revenue did not meet my expectations, principally as a result of customer order timing. The group's gross profit was up over the last year, but was offset by investments in SG&A.

We're seeing a lot of positive developments in Asia and we're off to a strong start in the second quarter. The group is on track to meet my growth expectations of mid- to high-single digit revenue and profit growth for the year.

Flavors & Fragrances operating income was off in the quarter for a number of reasons. First, within our Natural Ingredients business, we are experiencing higher onion costs at the same time that we are seeing pricing pressure due to an increased onion supply in the market. I originally estimated the impact of these issues to be $0.03 in the first quarter and $0.01 in the second quarter.

The actual impact was about $0.05 per share in the first quarter. Due to continuing price pressure and lower crop yields, along with higher plant costs due to poor quality crop, and I now expect the impact to be a $0.05 headwind in the second quarter and a $0.05 headwind in the third quarter.

Second, our Fragrance business experienced higher raw material costs, stemming from a well-known supply chain disruption that has impacted the industry.

We had a short lag in implementing pricing in response to this issue and that had a $0.01 impact on our first quarter results. Barring any additional setbacks from the supplier, we do not expect any further impacts from this issue.

Finally, the group was impacted by higher costs and lower volumes following the conclusion of restructuring at one of our North American plants. The affected plant has been running well and we're making progress on reducing costs.

However, we are experiencing lower volumes, in part due to our restructuring activities, but more notably due to ongoing market declines in several key dairy categories. These lower volumes have created a larger financial impact than we projected in February.

I'm pleased with our progress elsewhere in Flavors & Fragrances. Our BioNutrients business, each of our European Flavor businesses and our Fragrance business each delivered double-digit profit growth in the quarter.

Overall, the strategic initiatives we have undertaken and the restructuring program had created a solid foundation for growth in businesses that had previously been uncompetitive and undifferentiated.

We are also seeing positive signs with respect to revenue. Flavors & Fragrances revenue growth in the first quarter was approximately 3.5 percent, removing the impact of our divested businesses.

The group has had some significant wins already this year, including becoming a core supplier to a large consumer products company, new wins in our Sweet business outside of the traditional yogurt and ice cream segments that we had served and new wins in BioNutrients.

I believe we can build on these successes and now that we have lapped our culling efforts, I expect similar or better top line growth for the rest of the year.

Many of the businesses in Flavors & Fragrances are performing well and I expect to see continued revenue growth from the group throughout the year. However, I have to revise our 2018 profit outlook for the Flavors & Fragrances group as a result of the higher onion costs and continuing pricing pressure in the onion market.

I now expect profit within this segment to be down in the second and third quarters, with growth resuming in the fourth quarter of 2018. I'm disappointed by this development, but I remain confident in the long-term potential for Flavors & Fragrances.

In light of the revised outlook, I'm adjusting our EPS guidance and I now expect EPS to be between $3.70 and $3.80 for 2018. This represents growth of 8 percent to 11 percent over adjusted 2017 EPS. Steve will now provide you with additional details on the first quarter results.

Stephen Rolfs: Thank you, Paul. Sensient's operating income was a $55.7 million in the quarter compared to $24 million in last year's first quarter.

The 2017 operating income results include restructuring and other costs of $31.3 million and excluding the restructuring and other costs, adjusted operating income was $55.3 million in last year's first quarter.

Foreign currency translation increased both revenue and operating income by approximately 5 percent in the quarter. Diluted earnings per share were $0.89 in the quarter compared to $0.30 in the comparable period last year.

Restructuring and other costs reduced last year's first quarter earnings per share by $0.53. Adjusted earnings per share were $0.82 in the first quarter of 2017. Foreign currency translation increased EPS by $0.05 in the quarter.

Cash flow from operations was $18.3 million in the quarter compared to $31.2 million in the first quarter of 2017.

Our cash flow presentation reflects new accounting guidance, which now classifies certain cash receipts from securitized accounts receivable as cash flows from investing activities. The amount of cash receipts reported as cash flow from investing activities was $9.1 million in the quarter and $6.4 million in last year's first quarter.

In order to compare this presentation to the old method of presentation, these cash flows need to be added to our cash flow from operations. Capital expenditures were approximately $11.1 million in the quarter, and we expect capital expenditures to be between $50 million and $60 million for the full year.

Sensient repurchased 1 million shares of common stock in the quarter, adjusted debt to adjusted EBITDA is 2.9, and barring any opportunistic acquisition opportunities, I would expect that our leverage will trend toward our long-term target of 2.5x debt to EBITDA. We will continue to take a balanced, prudent and long-term approach to deploying our capital.

We continue to evaluate the impact of the U.S. tax legislation that was passed in December. Our tax from the first quarter came in slightly better than our 25 percent guidance. I now anticipate that our 2018 rate may be a few points lower than my 25 percent estimate as a result of certain planning opportunities.

Later this year, there may also be new guidance that may adjust some of the estimated charges we took at the end of 2017 when the new legislation was passed. Thank you very much for your time this morning. We will now open the call for your questions.

Stephen Rolfs: Operator, we're ready for your questions.

Paul Manning: Yes, operator, it looks like the first question is coming from Mike Sison from KeyBanc.

Operator: OK, sir. We have a question from the line of Mike Sison from KeyBanc.

Michael Sison: Steve, you did drop of, for what it's worth, in some of your comments. But in terms of your outlook for Flavors, Paul, I just wanted to better understand. I think you had hoped to see organic sales growth and constant currency sales growth starting 2Q and building momentum in 3Q and 4Q. Is that still your outlook for the year?

Paul Manning: Yes. I think we -- between a combination of new wins, organic growth that a lot of customers that we've been really focused on, I think those factors are certainly looking very good for the remainder of the year.

We see a lot of good progress that's been made in Fragrances, BioNutrients, our European businesses in particular, but I also see some growth in other U.S. markets and Latin America. Really, the headwinds to that growth, obviously, with the onion pricing issue, that's a bit of a headwind.

And then of course, the dairy market with which we had in my prepared comments, that that continues to be a bit of a headwind. But I think net of those headwinds, we still are endeavoring and expecting to be in that top line range you just mentioned.

Michael Sison: Great. And then, I was intrigued by your comment that you were able to win or win a spot on a core supplier position at one of the largest consumer products company. What enabled you to do that?

You've tended to focus on regional and local players. Is there certain technology that they found intriguing or certain product lines that you have that are now more competitive on a bigger scale?

Paul Manning: Yes. I would say this. One of the things that makes this company very special is the fact that we can take a lot of different technologies and apply them to many different markets. And so I think what we see from customers is an interest in suppliers that can bring more and more technologies to the finished product.

So whether, for example, you may be bringing color or flavor to a drink where formerly you only brought color or flavor, there is a certain value that we can bring multiple technologies and product lines to many customers who are trying to speed up development or, perhaps, have outsourced a lot of their development and, therefore, rely upon suppliers that can bring a whole host of capabilities.

And so I think this multidimensional approach we're taking in the market is very, very effective. And what's interesting is, I think, as well another customer comment, is that customers are looking to us beyond just, for example, a food product.

Hey, can you do flavor and color here? Yes. And by the way, it's natural color, so it's very complicated and that may in part different effects on the flavors that a synthetic color might not have.

That capability we have is very, very important. But they're also looking at that whole product. So maybe that's being produced in a product that's using solid based inks instead of water-based inks.

And so therefore, we can bring concepts to them on that front as well. So I think in general, what enabled -- what is enabling a lot of our wins right now is this sort of multidimensional technical capability.

Something that we've been working on for some time and I think what's really helping there is the nature of customers, as we see them, are changing, right? So the B and C guys, for example, maybe they don't have as large of the staff and they are more and more dependent on a supplier.

But the speed with which B and C and even some of the A customers now want to launch products. That multidimensional technical approach is very, very helpful in terms of enabling the customers to do that, to launch those products more quickly.

Michael Sison: OK, great. And then, your balance sheet is still in pretty good shape. You made 1 nice acquisition. Any updates on kind of the acquisition environment? Are there opportunities to do anything bigger? And the cosmetic actives business seems to be an area that continues to do well for you guys. Is that potentially an area of focus?

Paul Manning: Yes. So yes, we're happy with the Globe acquisition. That's very consistent with our strategy and it's really giving us a lot of opportunities to broaden our portfolio and really to balance a lot of our high-tech solutions as well. In terms of what we look at, again, I think if I could say this, if I could find umbrella technologies, those are very, very interesting acquisitions.

In other words, it's a technology not just for food colors, but it's a technology that could be adopted to a lot of things. For example, maybe it's helping you on natural colors, but it could also help you with extracts and it could help you with cosmetic actives.

And so it's those umbrella technologies that, I think, generate the best return because it's oftentimes difficult for them to market themselves to a company that's singularly focused on, say, one or two sets of ingredients. So that would probably be more of our focus than anything else.

You certainly heard me say before, there are definitely companies to buy, but in my opinion, many of them are very, very expensive and the expectations are not consistent with us being able to generate a good ROI for our investors.

And so we will continue to shy away from those. But yes, I think umbrella technologies that can really enable progress in each of our businesses would be my principal focus.

Operator: Your next question comes from the line of Brett Hundley from The Vertical Group.

Brett Hundley: I'm just kind of adding up some of the incremental headwinds, whether be onion or the fragrance raw is kind of relative to what you came out with before on your last call.

And at least I'm getting to over $0.10 of an incremental headwind, but of course, you're the top end of your guidance only comes down by $0.10. I'm just wondering if you can point out some of the offsets there.

Is it related to your Colors business and some of the natural color wins? Is there anything anticipated in that number for prospective share repurchase, that kind of thing? We just wanted you to address that, please.

Paul Manning: Yes. So if you just did the math, you'd say we're at 3.70 that went down to 3.80 I referenced some additional headwinds in onion. So if you do the math, sure. But you're right, there's probably a little bit more than just onion that's a headwind.

So you've answered part of that question in your statement. Yes, we see a lot of great things happening in the company, whether it's natural color wins, cosmetic wins, fragrance wins, BioNutrients wins.

And so sometimes it's hard to understand what the full magnitude of those wins may be, but I am excited about what I'm seeing and I'm excited about being past culling and restructuring and FX and all other noise. So we get a nice, clean and pure view of revenue.

And so yes, to answer very, very explicitly, I see offsets, positive offsets in the businesses that I mentioned. I wouldn't say, as I think about positive offsets I have been my necessarily, at this point, additional buybacks. So this should really be driven by organic growth and new wins in the business units.

Brett Hundley: OK. I guess I'll follow on to that since we're talking about buybacks and then I just had some more of some conversational-type questions on your onion and garlic business. So just as it relates to your balance sheet and capital allocation and following on with your discussion with Mike. So I guess two parts here.

A larger peer of yours recently came into the M&A market and paid our really hefty price for a naturals-based company and I know it's your desire to rotate towards acquisitions now that you're past culling and physical restructuring of your business and I know you're talking about umbrella technologies here and

I imagine some of these naturals-based companies can give you some of those umbrella technologies.

But when you see a deal like that, does it affect your ability to conduct M&A in any way, in your opinion? And I guess related in the second part of my question is, your share repurchases for Q1 almost matched that of what you did for all of 2017.

So x the M&A story, should we expect this management team and the board to really prioritize share repo over the interim at levels that could materially exceed years past? I think you guys have 2 million shares left on your authorization, so I just wanted to get a comment from you on that.

Paul Manning: Yes. So let me start with the second part and I'm sure Stephen want to add some things in here, too. On the share repurchase, yes, you're right. It's about the same magnitude as last year and it's maybe in the distinction is a matter of timing than magnitude.

We did it upfront because, ultimately, I see a lot of positive developments in the company. I see a lot of negative things in the rearview mirror right now.

And so that 1 million share repurchase is a -- should be a very strong indication that we see a lot of positive developments and potential within the business. Now with respect to M&A, sure, we certainly look at companies that are purchased and we're quite aware of those types of activities.

Does that change how I look at things? Does that -- in other words, was I competing for a company that somebody else is trying to compete with? Oftentimes, that's not the case. We're -- again, we're looking for technologies.

You find these things not necessarily in an auction or a brand you've heard of, so much as you do a lot of research, you understand where there's definitely differentiated umbrella technologies that is oftentimes protected with patents. That's a really solid long-term strategic acquisition.

If on the other end of that bookshelf would be an acquisition directed principally at market share, I guess again, you'd hear me -- you're not going to necessarily see Sensient competing with those types of M&A activities.

So yes, I don't really -- to me, there's nothing that changes my philosophy. Nothing that's happened in the last, say, 6 to 12 months the market that would change my philosophy on the types of companies that we're looking for.

I'm looking to maximize, to get to our 15 percent ROIC and I am not going to do that with going out and paying a hefty multiple for market share, is the way I'm looking at that at this moment in time.

I think we're going to get that ROIC faster where we can get a good technology at a reasonable price and deploy that technology in each of our businesses around the world. That's what's going to get me closer and faster to my 15 percent ROIC.

Brett Hundley: Yes. OK. And then if I could have...

Paul Manning: You want to say something?

Stephen Rolfs: Let me just comment on that. So echoing on what Paul said about the share repurchase, we basically just front-loaded that in the year and our cash flow, we think, will be strong and the rest of the year and it will bring that leverage down more to our long-term target.

And Mike mentioned that, I may have cut out in my comments. I just want to say a couple of things about cash flow just to make sure that, that wasn't where I cut out.

So if you look at our headline cash flow from operation number, it looks strange because there's an accounting change that moves some of the cash flows down into financing.

If you put that back up, you'd see our cash flow was down about $10 million in the quarter and almost all of that is attributable to receivables and it's tied to the timing and it's title growth we had in some of our businesses that grew well like cosmetics and fragrances and natural colors. And so I think cash flow will be strong over the rest of the year.

And I wanted to point out, I've gotten a number of questions about inventory and I've talked to a number of investors over the year about inventory. So our inventory levels are -- they were elevated at the end of 2017, and we talked about two reasons for that.

One was because, within our Flavor and Fragrance business, we made a conscious decision to build inventory to support certain businesses that in the past have experienced supply chain and production disruptions.

So you can think of that as an alternative to maybe investing more capital for more capacity. So there's no margin impact, there's no cost impact to that.

We just made a decision to elevate inventories there. The only thing I've talked about within our Natural Ingredients business is that garlic had been low and our garlic inventory should come back to a normal level. Again, there's no cost increase impact from that.

That's just a normalization of our inventory. The only area was the Natural Ingredients where there was the cost impact with the onion and Paul quantified that. So in the quarter, inventories actually were a source of cash. I just wanted to point that out. Sorry, Brett, go ahead.

Brett Hundley: No problem. And so long as there's not a big queue behind me, I just wanted to have a quick back and forth on your onion and garlic business. So onion, the data is certainly there to suggest what you're talking about, high import volumes, low price.

When I try and back into margin impact, I'm admittedly using a lot of assumptions here, but am I in the right ballpark with a view that the onion issue is dragging your total F&F segment margins down by about 100 bps in the quarter? Am I in the right ballpark there?

Paul Manning: Yes, I'd say you're in the right ballpark. In fact, maybe even a little bit more, but you're headed down the right street there.

Brett Hundley: OK. OK. And Paul, I guess, why do you feel better about the end of Q3 now? You've obviously had to revise your timing and sorry if I missed this in your prepared remarks, but why might you feel better that things can normalize towards the end of Q3 now?

Paul Manning: So couple of reasons. With onion, well let's just say that the Natural Ingredients business being perhaps the single biggest headwind here. It's really a function of a new crop comes online towards the end of Q3.

So that presents a whole different dynamic with respect to market supply. As you noted, there was a glut of global onion precipitated by some actions that took place overseas and put a lot of onion in the market. Very unusual event.

And so we see that, I think, we're fairly confident that, that has already been corrected with respect to what is now being grown overseas. So yes, the supply, we expect to come down significantly and that would start in the Q3 time frame.

And so to the extent we expect to sell through our higher costs inventory as well as market pricing normalizing due to a more regular supply, we see those things principally happening in mid- to late Q3, so then we would expect to see -- feel those benefits in Q4. That's a real big issue that we'll get past.

Brett Hundley: And to be clear, you don't necessarily see your own production cost normalizing? I think there's a lead time there. You're more making our call on the price -- the product pricing environment getting better.

Paul Manning: No. I think it's a little bit of both. Yes, the pricing, if I'm right and I'm pretty sure I am, that, that will help. But some of our costs have been driven by the yield that we actually achieved this year on onion.

So with lower yields, obviously, there's less flow into your plant, so you will have more of that absorption headwind. We also made a deliberate decision to kind of brings down our inventories.

Our inventories were too high on some of our product lines over there. And so therefore, that was an intended reduction in product flow through the plants.

So not an explicit cost, but okay, you have fewer products to spread your overhead over. We think this year's crop between what we planted and what our expected yields are, we would anticipate there will be less of that accounting absorption overhead problem.

But the other factor that we're feeling right now from this crop was that it was of a lower quality crop. And when you have a lower quality crop, you don't necessarily get precisely the product you wanted in the first place.

So there tends to be more reprocessing, which comes at a cost, for example. And again, with a normal and healthy crop come that Q3 time frame, we would anticipate not having a lot of those costs go into Q4 and beyond.

Brett Hundley: OK. And then just very quickly, I'll yield the floor. On garlic, how would you describe -- how intact is your margin profile there?

I mean, when you look at dehydrated prices, it looks like they're actually -- like they remain pretty solid. Whole garlic prices appear relatively favorable, at least on the spot basis. How would you characterize your margin profile in garlic right now?

Paul Manning: I think our garlic margin is fairly consistent. Most of the garlic that we're getting, in fact, probably 90 percent to 95 percent of it is U.S. based.

I know there's this thought out there somewhere that we're getting this vast supply of garlic from China and that's just simply inaccurate. It's like about 5 percent. So whereas there's been a lot of price movement in the Chinese garlic side of the world, that the U.S. side is a lot more consistent.

Operator: We have our next question from the line of Mr. Francesco Pellegrino of Sidoti & Company.

Francesco Pellegrino: I know it's been a long time coming to get that non-GAAP reconciliation as clean as it was in this morning's press release, so congrats on that.

Paul Manning: Yes, thank you. It's a -- I've been waiting for a long time, Francesco, longer than you can imagine.

Francesco Pellegrino: Longer than I've been covering the name. So with that being said, I wanted to just touch on some recent disclosures the company had made. Just about some changes in management.

Mr. Grover's departure this was some of that, Paul, you've really like raved about it and really looked like he was stepping in, like when he stepped in towards the end of 2015, you really raved about some of the things that he was bringing to the table, whether it was his focus on M&A or implementing certain strategies for the business or his ability to navigate the supply chain.

And it looks as if you sort of like implemented these strategies in which you guys are going to be keeping higher levels of inventory to sort of help you navigate some of your customer orders and it just seems as if this -- he leaves and all of a sudden, you're faced in all of these headwinds and Flavors & Fragrances, which should be more of a turnaround story now and experiencing these headwinds going forward.

I just seems like an odd time to leave when there's only more upside as compared to all of the headwinds that I've been experiencing -- that you guys have been experiencing in this segment.

Paul Manning: So, yes. I mean, I guess, as I said in the 8-K, he left to pursue other opportunities and I guess that pretty much summarizes it.

Francesco Pellegrino: OK. So then, where we are today with the Flavors & Fragrances, what are you looking for in regards to the next president of the Flavors & Fragrances Group given that they're going to be taking -- they're going to be leading this segment post-restructuring from day one essentially and trying to drive a 20 percent operating income margin going forward, when we're having all these highly commoditized headwinds that are sort of impacting, I guess, the most recent quarter and the rest of your outlook for 2018.

Paul Manning: Yes. So we obviously want an individual who's quite knowledgeable about the industry. We want an individual who's quite clever and proficient on the commercial, sales, and marketing side of the business.

I certainly don't need a restructuring expert. We've got that one covered off real well. So there's a lot of very good talent and so I think we've -- we'll be in very good shape when we select the individual.

But fundamentally, this is -- you always need a good problem solver, right? People who can overcome obstacles and are intelligent enough to prioritize correctly and exercise good judgment with employees and their people who carry a lot of respect.

So I think that what we're looking for here is not unlike what we've been looking for in the past, and we made a lot of management upgrades over the years, and we've got a lot more A players than we've had ever in the company at all levels. And so I'm pretty optimistic that we've got a very strong team and the individual that we bring in will only enhance that further.

But yes, to shorten my answer here, an experienced individual from the industry who has a very strong sales and marketing background, who could help us to continue to capitalize on the new wins that we have, continue to help us calibrate and refine our value proposition. In other words, what makes us different or better than the competition. And those are the important things. So that's what we're focused on in the next candidate.

Francesco Pellegrino: So one of -- first question I get asked all the time whenever I speak to investors on the name is just about catalysts for Sensient and it always comes down for Flavors & Fragrances group and obviously that long-term 20 percent operating margin.

You're going to be finding this external individual that didn't roll up their sleeves over the past couple of years to really bridge you from the 15.7 percent operating margin that you had in 2017 to where you want this segment to be over the long term, as compared to maybe just what your response was last quarter.

Is there any more insight into how we get to a 20 percent operating margin? Obviously, we'll get some margin expansion once we're past this onion derivative issue. But outside of that, is it through M&A? Is it through more automation?

Is it through tampering synergies within M&A? I'm a little bit lost in regards to just really how to bridge current operations or even if you just want to talk about the base year of 2017 to adjust the long-term operating performance of the segment.

Paul Manning: Yes, it starts with a very sophisticated concept to just sell more stuff that's consistent with strategy, right? So the strategy for us is about -- I'm not going out there necessarily to go gain a whole keep of market share on undifferentiated more commoditized products that you win some, you lose some, here today, gone tomorrow.

We really want the sustainable, technically driven types of products that create a lot of value for the customer. And so again, this is where the notion of more integrated sales, a stronger and continued emphasis on flavors, the idea that we can sell the integrated front more flavors and colors together.

But the other piece of this too is when you look at Flavors and the history of this industry, it went from synthetic flavors to natural flavors, I believe, and maybe one of the competitors did too is that really the future here is all about extracts.

And extracts have a great label declaration, they're viewed very positively by consumers. And so I think there's a lot of technical sophistication that goes into extracts that perhaps you don't see in other parts of the flavors industry.

So I think we're going to continue to focus in that part of the product portfolio as well. And then you consider the culling. Well, culling is -- you can look at that as a financial exercise, but you could also look at that as a strategic exercise. An indication of what we think is important and what we think is important to invest in.

And I think with the investments that we've made, it's very lopsided in favor, obviously, things like flavors and BioNutrients and fragrance compounds and natural colors, and it's less in terms of supporting things like more the mundane or things that are more commonly available in these markets. So I think that is still the case.

We're going to get past this onion headwind and I think we're -- with the top line growth, we still expect to show the continuing growth we're seeing in Colors and then the acceleration in Asia, I see the margin coming together pretty nicely for us.

Francesco Pellegrino: So it's drive more volume to create more manufacturing and operating leverage in the business model as well as growing certain product lines like extracts that are higher margin. Did I get it?

Paul Manning: Yes, the first part of what you're saying is certainly inferred from the second part of what you said.

Francesco Pellegrino: OK. And then, just a last question for me before I jump back into the queue. I understand the math and how we sort of reconciled down to the adjusted EPS guidance going forward.

Is there a way to have the conversation more about a pretax number, just so we can sort of back out the noise from share repurchases and the lower effective tax rate?

Because I wasn't expecting your share repurchase number to be as robust as it was and I think we can sort of strip out that noise if we start talking like pretax or if you want to talk adjusted EBITDA. Whatever it is, I'm just sort of looking to get down to the core business.

Stephen Rolfs: Sure. So Francesco, Paul mentioned the headwind in Q2 and Q3. So we do -- although we expect flavor and fragrance operating profit to be down in those two quarters, for the year, we still expect to see mid-single-digit improvement in our EBIT.

So even with those headwinds, we expect to grow operating profit or EBIT by single digits. And I mentioned in my prepared comments, we see a little bit upside in the tax line, that might be some of the noise you're talking about.

There may be some things that are coming out more favorable than maybe some planning opportunities that would lower our tax rate 2 to 3 points below the 25 percent, which was my previous guidance.

So some of that improvement would be in our guidance range, there may be other things that happen later in the year that may be additional upside tied to guidance that comes up from the IRS, that would not be in the guidance range.

Francesco Pellegrino: Steve, thanks for the explanation on the cash flow impact and your free cash flow impact. It was something that was a little bit of a head scratcher. So I appreciate you outlining that during the call.

Stephen Rolfs: OK, good.

Paul Manning: If anything on the call is that you're right, that is a little bit of a head scratcher. So certainly, we can have follow-up calls with folks on that one to clarify that one further.

Operator: We have our next question comes from the line of Finton Ryan from Berenberg.

Finton Ryan: My question was on the cash generation. Just to confirm. The -- do you have an explicit target for free cash conversion that you're aiming for?

And I know you mentioned the timing impact of the inventories receivables impact in Q1. So is this do you expect that to reverse for the rest of the year? Just to be clear. Or is this going to be the full year run rate level?

Stephen Rolfs: Sure. So on the first quarter cash flow, again, inventories were favorable and I think it's fair to say we've reached a peak on inventories.

So the things that I talked about in our Natural Ingredients product line, you'll now see that trend down over the rest of the year. And I believe we have inventories where we would like them in most of the Flavor business units.

So again, I think you consider the sort of a peak and it would normalize for the rest of the year. If I look at last year's cash flow, our headline cash flow from operations number was $180 million. That did have $20 million of the accounts receivable securitization in it.

So we had -- last year, we had about $160 million of cash flow from operations. And after capital expenditures of $56 million, we were at about $105 million of free cash flow.

That had in it a significant inventory build. It also had in it some restructuring outflow. So I would expect that we would be able to beat that number this year. And again, that would come about over the remaining three quarters.

Operator: The last question comes from the line of Garo Norian of Palisade Capital.

Garo Norian: I was curious just some of the announcements on management. Has a new head of Asia Pacific been identified?

Paul Manning: Yes. Well, we've -- the first announcement, just to get give a bit of a back story here, the first announcement we made was that we anticipate Rob Wilkins, the incumbent, to be retiring at some point this year. Once we lock that down, we then issued an 8-K, I believe just a few days ago, suggesting that Rob will retire officially on June 1.

And then yes, we have an internal candidate who is obviously in transition with Rob as we speak who comes from the cosmetics side of the business and significantly successful on the commercial side of that business.

He's operated in three different continents, very, very effective in Asia Pacific. So we are quite excited to have our new head of Asia Pacific to be in place officially on June 1. So yes, we've got that one covered.

Garo Norian: That's great. And then just secondly, going back a little bit to some of the M&A discussion. When you look at some of the multiples that are being paid out there in what is what's called broadly the space that you play in and then you look at where your multiple is, how do you think about the difference, I guess, in those 2 numbers?

Paul Manning: I think our stock needs to be higher, I guess, would be my first comment. That would help close that gap soonest. But I think, hey, we've got a lot of, as I said, noise in the figures over the last couple of years between restructuring and culling and FX.

So I think that's -- it's been very difficult for some folks to get a real clearer picture of things. I think now that we are past that stuff, that will help tremendously in terms of, again, I think giving people a real sense of where we are and where we're headed.

But I think we're just going to continue to focus on the revenue side and new wins and continue to grow the EBIT margin. And I think that will be fully recognized. But we're going to see better results in Flavors.

I think we're going to continue to see the very good results in the other part of the business. So yes, in short, I think, the noise is going to probably be the biggest help and I think continuing to improve the results is going to be also quite a good help.

Operator: We have reached the end of the conference call. At this time, I will turn the call back to the company for closing remarks.

Stephen Rolfs: That will conclude our call. Thank you very much for your attention this morning. If anybody has any follow-ups, you can certainly feel free to call the company. Thank you again and that will conclude the call.

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