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Darling Ingredients, Inc. (DAR)

Q3 2023 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning and welcome to the Darling Ingredients Inc. Conference Call to discuss the Company's Third Quarter 2023 Results. After the speakers' prepared remarks, there will be a question-and-answer period and instructions to ask a question will be given at that time. Today's call is being recorded.

I would now like to turn the call over to Ms. Suann Guthrie. Please go ahead.

Suann Guthrie

Senior Vice President-Investor Relations, Sustainability & Global Communications, Darling Ingredients, Inc.

Good morning. Thank you for joining the Darling Ingredients third quarter 2023 earnings call. Here with me today are Mr. Randall C. Stuewe, Chairman and Chief Executive Officer; Mr. Brad Phillips, Chief Financial Officer; Mr. Bob Day, Chief Strategy Officer; and Mr. Matt Jansen, Chief Operating Officer of North America. Our third quarter 2023 earnings news release and slide presentation are available on the Investor Relations page under Events & Presentations tab on our corporate website and will be joined by a transcript of this call once it is available.

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

Now, I will hand the call over to Randy.

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Thanks, Suann, and good morning, everyone, and thanks for joining us for our third quarter earnings call. Darling's global ingredients platform delivered as predicted and DGD faced some headwinds and operational challenges during the quarter. Overall, we feel good about the momentum we are carrying into fourth quarter and 2024.

Turning to the Feed Ingredients segment. Raw material volumes were flat compared to third quarter 2022. Our gross margins have returned to pre-acquisition levels, demonstrating our ability to successfully integrate Valley and FASA. Our work is not done and we expect further improvement. Fat prices were lower year-over-year, but sequentially improved late in Q3.

Turning to our Specialty Food Ingredients segment. Raw material volumes increased 18% year-over-year due to Gelnex acquisition. Our global collagen platform delivered solidly and we continue to shift our product mix into higher margin products. Hydrolyzed collagen remains an important part of our long-term growth strategy within the Food Ingredients segment. Earlier in the quarter, we commissioned a new spray dryer in Epitacio, Brazil, adding much needed capacity to continue our growth. I'm also excited to share that our research and development efforts in this segment have resulted in our ability to formulate a product that target specific health concerns, such as glucose moderation. We are currently in scientific trials and expect to bring this ingredient to market during 2024.

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On October 26, we announced that DGD volumes for the third quarter were lower due to a regularly scheduled turnaround at DGD 2 in St. Charles, Louisiana that took the unit offline for 27 days. After that turnaround, DGD 2 had a minor operational disruption. So in total, DGD 2 was offline for 37 days in the quarter. This resulted in lower gallons produced, higher cost, and lower than expected operating profits. Year to date, DGD has sold 910 million gallons of renewable diesel at approximately \$1.02 per gallon EBITDA, and Darling has received \$163.6 million in cash dividends year-to-date.

With that, I'd now like to hand the call off to Brad, and then I'll come back and discuss the rest of my thoughts for 2023 and 2024. Brad?

Brad Phillips

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

Okay. Thanks, Randy. Net income for the third quarter 2023 totaled \$125 million or \$0.77 per diluted share compared to net income of \$191.1 million or \$1.17 per diluted share for the third quarter of 2022. Net sales were \$1.63 billion for the third quarter 2023, as compared to \$1.75 billion for the third quarter 2022 or a 7% decrease in net sales. Although Darling's third quarter 2023 gross margin increased \$10.1 million and was 23.8% as compared to 21.5% for the third quarter of 2022, operating income decreased \$90 million or 33.5% to \$178.4 million for the third quarter of 2023, compared to \$268.3 million for the third quarter of 2022, primarily due to Darling's share of Diamond Green Diesel earnings decreasing \$49 million. Additionally, depreciation and amortization and SG&A increased about \$21 million and \$32.6 million, respectively, as compared to the third quarter of fiscal 2022 primarily due to the Gelnex and FASA acquisitions.

Now, moving to non-operating results. Interest expense increased from \$39.8 million in the third quarter 2022 to about \$70.3 million in the third quarter 2023, primarily as a result of increased indebtedness due to the acquisitions. For the three months ended September 30, 2023, the company reported an income tax benefit of \$15.4 million and an effective tax rate of negative 13.6%, which differs from the federal statutory rate of 21% due primarily to the relative mix of earnings among jurisdictions with different tax rates and biofuel tax incentives. The company's effective tax rate, excluding the biofuel tax incentives and discrete items is 25.9% for the three months ended September 30, 2023. The company paid \$40 million of income taxes in the third quarter.

For the nine months ended September 30, 2023, the company reported income tax expense of \$52.3 million and an effective tax rate of 8.4%. The company's effective tax rate, excluding the biofuel tax incentives and discrete items is 28.4% for the nine months ended September 30, 2023. The company also has paid \$127.7 million of income taxes year to date as of the end of the third quarter. For 2023, we are projecting an effective tax rate of 9% and cash taxes of approximately \$30 million for the remainder of the year.

The company's total debt outstanding at third quarter 2023 was \$4.4 billion as compared to \$3.4 billion at year-end 2022. Our bank leverage – covenant leverage ratio at the end of the third quarter was 3.25 times. We continue to maintain strong liquidity with \$1 billion available on our revolving credit facility as of the quarter end. Capital expenditures totaled \$146.2 million for the third quarter 2023 and \$380.6 million for the first nine months.

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

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.



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Hey. Thanks, Brad. As previously announced a few weeks ago, we revised company guidance to \$1.6 billion to \$1.7 billion of combined adjusted EBITDA for the full fiscal year 2023. For Q4, we carry good momentum in from the third quarter around the world. Raw material volumes have slightly softened, but our diversified geographic footprint makes the impact negligible. Clearly, the global fats and oils have softened as a direct reflection of an ample supply of global fats and oils and delayed start-ups and inconsistent operations of renewable diesel plants.

While we've seen a lot of press and noise about significant gallons of new renewable diesel coming to the market, the numbers appear to tell a very different story. If more capacity outside of Diamond Green Diesel was operating, fat prices undoubtedly would be higher. DGD is performing well and we do not have any planned turnarounds in Q4. Margin structures are adjusting and we're very encouraged with the conversations we're having with a variety of interested parties regarding sustainable aviation fuel and our ability to deliver the margins in line with what we have communicated.

Looking forward to 2024. While the heavy lift of our integration work has been completed, there are still a few opportunities that can add some margin improvement in our Feed segment and our Food segment should continue to reflect our product mix shift. From an earnings perspective, we see 2024 shaping up nicely and expect to deliver and de-lever with an improved performance globally. The table is set with an improved outlook for the LCFS, growing demand for SAF, strong demand for our low CI feedstocks and favorable tax structures.

Given the environment we see for 2024, we – at this time, we anticipate combined adjusted EBITDA to be in the range of \$1.7 billion to \$1.8 billion. In 2024, we plan to lower capital expenditures, focus on improving our working capital usage and we anticipate regular dividends from Diamond Green Diesel. This will all help us accomplish our leverage targets by year-end. Given the anticipated dividends from DGD and the strength of our global ingredients business, we should be well on our way to achieving our target leverage ratio of about 2.5 by year-end 2024.

With that, let's go ahead and open it up to questions and I'll come back with some closing comments.

QUESTION AND ANSWER SECTION

Operator: We will now begin the question-and-answer session. [Operator Instructions] And our first question will come from Manav Gupta of UBS. Please go ahead.

Manay Gupta

Analyst, UBS Securities LLC

Good morning, team. My question first is on the little bit on the macro side. How do you view the recent stock proposal by CARB, which increases compliance by 50% by 2030? Also has the ARR mechanism, which pulls forward the program in case of over-generation of LCFS, do you believe this will be supportive of RD economics once it kicks in in 2025?

Matthew J. Jansen

Chief Operating Officer - North America, Darling Ingredients, Inc.

Hi. Good morning, Manav. This is Matt. So first of all, the answer is yes. We do believe that this is supportive to the RD business. As you know, the LCFS is an important component to the margin build in the RD space. And given that the SARIA that was put out a couple of months ago and the expected legislation that is forthcoming, there are several components that we think are supportive for the RD and even the SAF business. So obviously, volume is an important part. And then there's the component for a potential of an SAF in California of up to – in the neighborhood of 150 million gallons, which will line up very nicely with the – our SAF project.

And there's even the component of timing. There's the possibility of an earlier implementation. Right now, it's set for 2025, but there is the chance – and we all have to stay tuned on this, but there is the chance for even sometime in Q3 or Q4 an implementation coming on this. So again, all-in-all, we are very optimistic and quite satisfied with the LCFS.

Manay Gupta

Analyst, UBS Securities LLC

Okay. I'm assuming you're basically referring to the fact that the ARR will pull forward the program into 2024. So the program could actually start in third quarter 2024?

Matthew J. Jansen

Chief Operating Officer - North America, Darling Ingredients, Inc.

That's a potential. Yes.

Manay Gupta

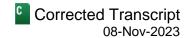
Analyst, UBS Securities LLC

Okay. Thank you. A very quick follow-up is on slide 7. You indicate lower fat sales volume were a \$32 million year-over-year headwind and lower protein sales volume were a \$13 million year-over-year headwind. Given that integration is going well for both Valley and FASA, should we assume this was just a temporary blip and the volumes will come back as we go ahead?

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

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Yeah, Manav. This is Randy. I mean, what we're seeing in my script, I commented on it that that's directly related to lower cattle slaughter numbers predominantly in North America. And clearly, the cattle economics have changed in the US. The herd is low but being replenished and that's just directly related to year-over-year comparisons of if you think of it this way, red meat has the most fat, the most protein, and then pork and then chicken. And so that's direct – that's what that is. The volumes in South America are relatively flat right now. Europe is in good shape but that's all pretty much North America. Canada is in good shape.

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

Adam Samuelson
Analyst, Goldman Sachs & Co. LLC

Yes, thank you. Good morning, everyone.

Suann Guthrie
Senior Vice President-Investor Relations, Sustainability & Global Communications, Darling Ingredients, Inc.

Good morning.

Adam Samuelson
Analyst, Goldman Sachs & Co. LLC

Good morning. So I guess first question, Randy, I mean, if you think about the updated kind of outlook for the balance of this year and you gave kind of a framework for 2024, can you first quantify in the quarter the hedge – the resolution and the pre-announcement to a hedge loss at Diamond Green? Can you quantify that? And as we think about Diamond Green for the fourth quarter, if there's no scheduled turnarounds, should we be thinking about production a lot closer to where you were in the second quarter, which if true, and even at third quarter margin levels would imply, make it pretty tough to get to the low end of the way you're framing the full year? So can you just help reconcile that?

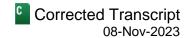
Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

I don't know that I would frame it the way you just finished that sentence. No. You know, clearly, there's always a timing issue how the fat prices in our core business flow through. And also, remember, a significant portion of the North American portfolio ends up at Diamond Green Diesel as the purchaser. So you had a little bit of a double wham here. Number one, the prices started to accelerate in third quarter again, but we had already sold Diamond Green. And so those sales now are coming to be fruition in Q4 for our core ingredient business. On the other side, we saw heating oil spike up. You do get some hedge losses. You can go into the or you can go to straight to the financials in the derivative sections on the Valero release and you can see what that number is, and it was a significant number.

At the same time you had higher fat prices flowing through, then you had heating oil now coming off. And so at the end of the day, that's my comment about margins are adjusting. You know, if you think about the efficiency of the D4 RIN, when that thing came down, one did say, it said far prices had to come down to put, some type of margin back in the business. So clearly, the margins in DGD are coming back very nicely in Q4 here. And you know, they'll finish the year strong and then that's what gives us then the momentum into next year. I mean, like we said, we're trying to – we've always said, we're not going to guarantee, you've no volatility in DGD because there's a lot of moving parts there but at the end of the day, 910 million gallons at \$1.02 or year to date. We said coming into the year we'd be somewhere between \$1, \$1.10. We're using a \$1.10 for next year. We'll finish up

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somewhere, within our guided range for the year. It just depends on how everything flows through, but no, from what we see right now, we're right on target.

Adam Samuelson

Analyst, Goldman Sachs & Co. LLC

Okay. That's helpful. And then just in the Feed segment, can you maybe just – maybe the quarter-on-quarter EBITDA decline help bridge some of that? So EBITDA was down \$26-or-so million versus the second quarter. Can you help bridge how much of that was seasonality? How much of that was the commodity prices? Maybe some of the weakness in pet ingredients? And if you think about the fourth quarter kind of with where commodity prices land? Can you help us think about some of the key items in EBITDA in Feed moving forward?

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Yeah. And I think you kind of answered most of your question there. I mean, typically the seasonality hits in this business, especially in North America and Europe in third quarter in the Feed segment because you're being – the quality of the raw material in the summer times is much harder to process. That's code for it's harder to get the fat out of the product and leave it in the protein. So you kind of have lower quality fat – less fat, and that's how it flows through it. It has for, 142 years.

The pet food business is something that to put your finger on right now. Pricing remains good in that area. Demand was weak, but it's picking back up again. You've got a little bit of a trade down going on, it appears, around the world right now in the pet food side. But overall, when we're looking at 2024 versus 2023, that it looks pretty, pretty stable there. Protein prices, on most products are in pretty good shape. I mean, there's a little bit of trade disruption in the world right now in different areas that are moving or moving proteins around.

Matt, what else you want to add here?

Matthew J. Jansen

Chief Operating Officer - North America, Darling Ingredients, Inc.

Yeah. I mean, I would say, the Q3 as you all know was a typical very hot summer. And our businesses did, as expected, feel that. And so but we are seeing, especially now in Q4, a quick return to the pickup and recovery.

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Yeah. Keep in mind, Adam, that a year ago today, not sequentially, but a year ago, here was we still had Ward, South Carolina operating in North America here. Ward, South Carolina is going to be key to 2024 for us as it comes back online here. The plant is completely rebuilt. We are still landfilling a significant amount of product right now that we can't process in our system. So as we guide higher next year, if you say what – you always have to assume fats and oils prices and protein prices in there and energy. But most importantly for us, it's being able to bring back our system to full strength on the Eastern Seaboard.

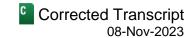
Operator: The next question comes from Derrick Whitfield of Stifel. Please go ahead.

Derrick Whitfield

Analyst, Stifel, Nicolaus & Co., Inc.

Good morning, all, and thanks for the 2024 commentary this morning. For my...

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Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Welcome.

Derrick Whitfield

Analyst, Stifel, Nicolaus & Co., Inc.

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...first question, I wanted to lean in on DGD and focus on the sustainable margins of your business, which really should drive the value of that business beyond 2024. When we analyze your sustainable margins by assessing the value of your feedstock streams relative to a marginal unit of production, there appears to be a very meaningful, positive spread with what you own differentially versus industry. As you optimize the economics of DGD, is it reasonable to assume that that sustainable margin you've talked about in the past at above \$10 per gallon still stands even with depressed D4 RIN prices given your ability to increment talent at DGD?

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

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I mean, fundamentally, Derrick, that's what we believe. I mean, clearly the volatility in Q3, the turnaround offline 37 days, we disrupted our logistics both inbound and outbound there and, moved both to Q4 that should have loaded, et cetera, et cetera. The D4 RIN plays an important part in the value of that business down there. Clearly, we were not a hedger of D4 RINs and we got caught in the volatility there with higher fat prices, lower – a lower green premium as we say and you saw that flow through. But overall, our thesis still remains the same. As Suann pointed out to me, she said, even under any situation, our investment case in this was \$0.79 10 years ago on a \$3.23 a gallon bill. We still believe in that. We believe it's even better now, given our CI advantages, given our both inbound/outbound logistic advantages.

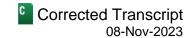
I mean, keep in mind, why are fat prices a little lower in North America, because Diamond Green is the largest importer now of fats in North America because it has the logistical capability to convert and pretreat those fats. So that's phase 1. Phase 2, as the script alluded, we're working hard with interested parties and we won't say who the interested parties are, so please don't ask. But we're very close, and SAF is real, the demand is real and the margin opportunities as we've explained out there remain very real and doable. So if you look at this business, in 2024, Matt said, okay, I think there's a chance we could get the LCFS implementation online a little sooner, even if it doesn't come, till the back end of the year, just the fact when CARB publishes and everybody says, oh, here is the script, here's the playbook, that's positive and we'll see an improvement there.

Number two, as we look around the world for next year, the SAF side, our plant is progressing nicely. We made it through hurricane season. I know technically that's got another week or two, but it looks like we've made it through hurricane season. We'll be buttoning it up. Steel is up, equipment is there and you know, hopefully as we progress through the wintertime and next summer, it will be mechanically complete and doing a normal start-up here. And that's if you look at it two to three years from now, you'll have 250 million gallons of SAF in 2024 or I mean 2025 for sure. You know, and then, SAF 2 is on the drawing board here.

Clearly, as we've communicated to people, that decision won't be made until we have complete, proof-of-concept of both the technology and the margin structure. But, at the end of the day, if you look at 2024, 2025, 2026, you can start to think out that our portfolio will include, a substantial gallons of SAF along with RD and then we'll have – we'll own that arbitrage again as we go forward. So it's a – as we look forward, we don't see any downside, from our case. You know, there may be a little lull here that the market seems to want a price in.

Matt, anything else you want to add?

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Matthew J. Jansen

Chief Operating Officer - North America, Darling Ingredients, Inc.

I would just say that one thing to keep in mind is that as this SAF comes online, the feedstock is renewable diesel. And so our plan is [indiscernible] (00:24:374 for 250 million gallons. And so when we turn on with that plant, that's 250 million gallons of RD that's coming out of the RD market and going into the SAF market. So that's another, let's say, friendly component to the – even the outlook for RD.

Derrick Whitfield

Analyst, Stifel, Nicolaus & Co., Inc.

That's great. Maybe staying on DGD. Wanted to see if you could offer some additional color on the apparent delay you're seeing in RD capacity expansions, whether delays or simply just difficulty of running at nameplate, which is more challenging than I think we all appreciate. We see the same, but I'd like your views on that as well.

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Yeah. And I'll tag team this with the team in here. I mean, clearly as we look around the horn, we're both buyers and sellers of fats and oils around the world. And when I say buyers, I mean that's the DGD hat, and sellers, that's the Darling hat. And clearly, we're not seeing the demand from the renewable guys in North America. In fact, we're actually – we're buying material back from them. I think I guess if we say frustration that might be too strong. Our curiosity and a bit of frustration is that when people started, whether it was Bloomberg or others putting out these S&Ds on D4 RINs, they forget multiple components of it.

Number one, they assume if Phillips 66 announces a plan, it's going to be online in January 1 and run a capacity. If Vertex, if PBF, I mean, HollyFrontier finally hit 52% capacity, yay. You know, at the end of the day, you just keep reading this stuff. Well, that doesn't generate the level of RINs that they're saying and then the world doesn't understand when you export material, which a significant portion of Diamond Green because of its location on the Gulf Coast goes around the world, at the end of the day, those RINs get retired in 60 days. There's a delay there. So, at the end of the day, you kind of have to go back and rebalance this thing with reality. So, we're buying back fat. We're not selling and that selling means they don't have the pretreatment units that they claim they do or they would be buying the cheapest fats in the world.

Matt, anything else you want to add?

Matthew J. Jansen

Chief Operating Officer - North America, Darling Ingredients, Inc.

You know, as I think many of these are learning, this is not necessarily an easy business to operate. And whether it's the – call it the CI component or the quality of the raw material and the pretreatment component requires more CapEx. And someone tried to cut corners and save on CapEx, then they find out that, gee, now this product, we can't process it or it's – at the capacity that we want it. So, this is a – it is a complex and not easy business to operate in. And I think some of these people are finding that out.

Operator: The next question comes from Dushyant Ailani of Jefferies. Please go ahead.

Dushyant Ailani

Analyst, Jefferies LLC



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Good morning, guys. Thank you for taking my question. The first one I had was on the guidance that you've given for 2024, the \$1.7 billion to \$1.8 billion. Could you talk a little bit more about what margins do you expect for the Food and Feed segment?

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Not really ready to go there yet, Dushyant. I mean, as I look at it, when we take a shot at producing guidance here, what you can back into here is you can say, what are you thinking on Diamond Green Diesel? Well, we're thinking that we're going to run it at above nameplate capacity and we're going to make a \$1, \$1.10 a gallon next year and it doesn't include any SAF gallons coming on early at this time. It's just too early to make that prediction. And so it's not hard to back into that number. And so at the end of the day, where it lands, whether it's in Food or Feed, we're still we're thinking that the numbers are going to roll up between \$1 billion, \$1.1 billion, maybe a little more in the core business, depending on where fat prices recover. And as we've said, if the – if renewable diesel capacity is there and has pre-treatability or even if it doesn't have pre-treatability, fats and oil prices can't stay where they're at. You know that if you look at the – whether it's a soybean oil S&D, we're at a multi, multiyear low.

And RBD margins which most of these guys are running, are now 1,100 over. So that's \$0.11 higher than we're

Matt, Bob, anything you want to add to?

operating at. So that's – so, that's how we kind of cast that looking forward.

Robert Day

Executive Vice President - Strategy, Darling Ingredients, Inc.

I think that's right. I mean, we're just at a - it's a generally tight S&D scenario and we're - a lot needs to happen as far as crop production in South America. And that's really going to determine what we see with respect to certainly protein levels and ultimately oil levels as well.

Dushyant Ailani

Analyst, Jefferies LLC

Thank you. That's helpful. And then one question I had was just kind of your thoughts on buybacks given where the stock price is today or maybe just in general. I know that the goal is to kind of get to that 2.5 leverage. But any thoughts on entertaining higher buybacks given where the stock is trading today?

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

You know, it is a discussion point with the board. We have adequate capacity to do that. Clearly, our focus today is, as we said, is to repatriate cash and get the total debt down and get to at least a discussion point of investment grade as we have some maturities coming in in 2026 and 2027. So it's not off the table. You know, clearly every year, we will buyback any executive compensation or dilution for sure. And after that, then it's opportunistic. And as the year goes along and as Brad says, I have a little extra cash, we've been given the authority to make those decisions. So nothing's off the table here.

Operator: The next question comes from Paul Cheng of Scotiabank. Please go ahead.

Paul Y. Cheng

Analyst, Scotiabank

Thank you. Good morning, guys.

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Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

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Good morning.

Paul Y. Cheng

Analyst, Scotiabank

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Two question please. Good morning, Randy, just trying to understand sequentially from the second to third quarter the Feed Ingredient revenue is down, the sales volumes is actually flat and all the market indicator whether its UCO, tallow [indiscernible] (00:31:29) is actually up. We're trying to understand that what causing the sequential revenue jump from second to third quarter in the [ph] bid (00:31:39) business? That's the first question.

Brad Phillips

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



Yeah. Yeah. Paul, this is Brad. When you're looking sequentially, we have, for lack of a better word, leading lags in a lot of our contracts. And so there's timing differences there that will often and when you get quick movements that Randy talked about earlier between second and third quarter price movements and then with the way the contracts work and the lead in the lag, that can cause a little bit of kind of discolor there, I would say.

Paul Y. Cheng

Analyst, Scotiabank



And so, Brad, should we – based on that means in the fourth quarter we should see comparing to the market indicator, your revenue, we see more of an upside or that the lag effect is going to take longer than that?

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.



Yeah. Typically, what you're going to see then is if you think of it this way and today around the world, we have a significant amount of our internal produced fats and oils, whether they're in Europe or Brazil or North America headed to Diamond Green Diesel. And so as those were – if you want to think about it, what we produced in August, it is sold and it doesn't arrive and be processed until October and September is kind of November and October now is December, January. And so, as we said in – earlier in the script, so you had a move up of fat prices in Q3 that then were sold and purchased. And so those will flow through and those should deliver a pretty good fourth quarter in that – in the Feed Ingredients segment.

Operator: The next question comes from Andrew Strelzik of BMO. Please go ahead.

Andrew Strelzik

Analyst, BMO Capital Markets Corp.



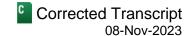
Hey. Good morning. Thanks for taking the questions. My first one is on Diamond Green Diesel and I think Randy kind of over time you've talked about \$0.90 or \$1 being the cost advantage or the minimum kind of margin to think about for DGD versus the marginal producer. And you kind of talked around this I think a little bit earlier, but I was hoping if you could be a little bit more specific. But do you think that that number has changed at all with new capacity has come on, et cetera or is that still the right way to think over time about the baseline DGD margin?

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.



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Yeah. Hi.

Andrew Strelzik

Analyst, BMO Capital Markets Corp.

Hi.

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

I don't really see anything changing that competitive advantage out there right now. I mean, I'm looking around the table and I don't know.

Matthew J. Jansen

Chief Operating Officer - North America, Darling Ingredients, Inc.



I agree that's something that we consider as a competitive advantage. We can – we're going to continue to leverage that advantage going forward, trying to stay, let's say, ahead of the game. And that's, again, with the even with the SAF project, it's going to separate us even further from our competition.

Robert Day

Executive Vice President - Strategy, Darling Ingredients, Inc.



If I could just add. I think one thing to keep in mind is part of that advantages is DGD's ability to blend all different kinds of feedstocks and the price relationship amongst those feedstocks changes a lot from time to time. So the relative advantage is not something that you can pinpoint and be as static. But generally speaking, I think the advantage that we had before continues to be the case today.

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.



Yeah. And I think, the DGD mixology has become even more complicated given, whether you've got [indiscernible] (00:35:27) coming from Rotterdam, from our factories or you got tallows and yellow grease coming from Brazil and UCOs from the Asian countries. You know, you got a timing of when those arrive and then you've got a usage you can't – we don't really run feedstocks neat in a sense. So we make a mix that meets our customers' needs, that allows us to get the highest yield that we can and the longest catalyst life. And so, it becomes a far more complicated thing. But the competitive advantage like I said, versus run an RBD, soybean oil, it right now is \$0.88 a gallon. So that's not even a CI differential there.

So you know, I think, as you've seen through the year, remember, Port Arthur is still waiting on its pathway. We anticipate at any time. So Port Arthur has not had the economics that it will have next year again. And then that's Port Arthur pre-SAF. So, I think the advantage is very sustainable and widens out over time. Like I said, I don't want to be somebody that doesn't say there's going to be less volatility due to timing here, but it's very achievable.

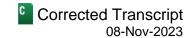
Matthew J. Jansen

Chief Operating Officer - North America, Darling Ingredients, Inc.



You know, and on top of that advantage, there's the other value of our integration with our Feed business. And we're producing, even the local fat supplies that are in the US and Canada that a large percentage of that ends up in DGD. And then again, one of the other things back to DGD is the producers' tax credit going forward. We think that the DGD is again, one more time have more advantage than the others in, when that calculation comes into place. So again, we like our position.

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Andrew Strelzik

Analyst, BMO Capital Markets Corp.

Okay. That was a really helpful color. I appreciate that. And just my second question on the – following up on some of your commentary around some integration benefits that remain or opportunities that remain. We know I think that there's some Valley contracts that go into effect January 1, is that really what you're talking about? And is there any way to quantify that or more broadly, are you seeing, given kind of the bigger asset footprint with all the acquisitions, et cetera, that there's even more opportunity broadly beyond Valley to continue to optimize? Thanks.

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Yeah. You know, and I think those comments were in the script. I mean, clearly, the US operations and procurement teams have made great strides at Valley and then our international team down in Brazil. You know, taking a private company to public is no small task on either continent here and then if you will, say, making them Darling. And you know, we tend to be conservative, we tend to risk manage and we have a margin expectation in our core ingredient business that's very well-known and our return standards are etched in [indiscernible] (00:38:35) there for us. And so at the end of the day, we've made the success of the Valley integration, as we said, has been the ability to improve the raw material procurement contracts and all the little terms and conditions in there.

And then ultimately, as I said earlier, we – we're still short, massive capacity on the Eastern Seaboard that's ready to come online, but as you know and as we've shared with others, we're waiting on motor controlled gear that's due to be delivered here this winter. Otherwise, we'd have that plant back up, but the supply chain, we're still moving stuff inefficiently to plants just to support our supply base out there that once Ward comes up next winter or next spring, I mean, then the Q1, we should be back in good shape there. And then we've got capacity expansions going on down in Brazil right now that are just in the commissioning stages that should be accretive to us next year.

So I mean, the world looks pretty darn good next year. It doesn't look like we'll have 3% to 5% growth of raw material tonnage as we've seen over the last several years. There's a little bit of contraction of animal numbers out there, whether it's disease or whether it was just margin and feeding people. But at the end of the day, you're setting up pretty nice for next year.

Operator: The next question comes from Sam Margolin of Wolfe Research. Please go ahead.

Sam Margolin

Analyst, Wolfe Research LLC

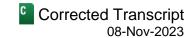
Hi. Good morning. Thanks for taking the question. My first question is on just the fat environment. You've talked a little bit about the relationship to the vegetable oil complex, but is there a scenario where fats prices next year decouple from veg oils just because if the whole – if the pressure in the system is originating from RINs oversupply, you solve that with lower biodiesel production which would disproportionately impact soybean oil supply demand versus fats. And then if there's a corresponding LCFS rally that might further benefit tallow and yellow grease prices relative to veg oils. Is that a scenario that you think is possible?

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

A

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I really don't think so. And, number one, I think, as we've said all along, clearly the Gen 1 technology of classic biodiesel would be the one that would become challenged. But the reason it would become challenged would be because there would be RD capacity that then would take that supply. You know, you'd just kind of have to do the numbers. If Martinez is really going to run 730 million gallons, that's 3 million tons of raw material. If P 66 can do half of what they think they can, that's another 1.5 million, 2 million. And then then you still got, the PBFs and you got the Vertexs, you got REG, Geismar, all these guys that seem to be new demand out there.

I mean you can see the scenario quickly change. Now, the question is where – what does D4 RINs do. Bob, do you want to take a shot at that?

Robert Day

Executive Vice President - Strategy, Darling Ingredients, Inc.

Well, I think I think you're right on, Randy. You know, I think the only way that we would decouple is if RD production were to plummet because of challenges in running and operating. But if that were to happen, RIN values should go higher and that would significantly benefit our broader network. But, we don't really see that happening. What we see is, overall RD production, having some challenges, but continuing to have a significant demand pull and keeping prices – relative prices in line between fats and oils.

Sam Margolin

Analyst, Wolfe Research LLC

Got it. Okay. And then this is a follow-up, but, it's also on the fats outlook with the LCFS proposal. I mean, obviously, a lot of people are looking at that through the lens of RD margins, but it seems like it would impact the fats market too over time because CI would become more important to values, to intrinsic value of different feedstocks. And so – but of course, it's very regional specific. It's only California. So I was wondering what your thoughts on that are if you think maybe the LCFS proposal is actually a bigger deal for tallow than it is for underlying RD margins.

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

I think we would believe that. We would think it clearly favors low CI as does SAF. I mean clearly, I think if we down the whole conversation today down to one thing it's about timing. RD is a good business. It's got growing demand globally. SAF is going to be a great business. It's got incredible growing demand. We've got maritime fuels. And oh, by the way, they all favor low CI feedstocks and we're stuck in this rut of saying, well, what are margins going to be, where is D4, where is LCFS? And, at the long term, as we've always said, the competitive advantage of the Gulf Coast real estate, whether you're shipping SAF by pipeline, boat to Europe or to California, it's just going to really work out pretty nice.

Matt, I don't know.

Matthew J. Jansen

Chief Operating Officer - North America, Darling Ingredients, Inc.

Yeah. The only other thing to keep in mind is that obviously the LCFS is specific to California, but as we're doing business in other markets, the LCFS is a reference in our valuation when we're using to determine whether product is sold to another market or to California. So one way or another that LCFS valuation is built into all of the RD sales regardless of whether it goes to California or not. So that's a – that's an important component not to overlook.

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Operator: The next question comes from Ben Bienvenu of Stephens. Please go ahead.

Ben Bienvenu

Analyst, Stephens, Inc.

Hi. Thanks. Good morning. I wonder if we could talk about 2024. Randy, you talked about \$1.7 billion to \$1.8 billion of EBITDA. What do you think that translates to for free cash flow? And then what are your priorities for free cash flow as we start to see CapEx budgets potentially come off of peak at DGD notwithstanding the SAF expansion that you want to engage in?

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Yeah. And I think, we had this discussion with our board. I mean, as you guys look to valuing the company here, ultimately we can talk about combined adjusted EBITDA, but it's actually what is the dividend plus the core ingredient business, and then how much CapEx are we going to spend and you know what's in the M&A pipeline. And so when we look to DGD and we say above nameplate, \$1.10 a gallon, you can come up with an easy \$500 million in dividends there. And then you look at our core ingredient business. And if we're at a \$1 billion, \$1.1 billion, there's your number right there, \$500 million CapEx. If we – that's got you know probably \$100 million of growth projects of the new plants we've talked about building. And then you look at it and you say you got an interest bill of around \$230 million...

Matthew J. Jansen
Chief Operating Officer - North America, Darling Ingredients, Inc.

\$230 million. Yeah.

Randall C. Stuewe
Chairman & Chief Executive Officer, Darling Ingredients, Inc.
....and cash tax of...

Matthew J. Jansen
Chief Operating Officer - North America, Darling Ingredients, Inc.

\$160 million.

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

...\$160 million and then, some limited buybacks in there that could be higher if we're doing a little better or whatever. But, that – you quickly, quickly pull down debt down to around that sentry point \$9 billion level.

Matthew J. Jansen

We do have one pending transaction that's out there, and on...

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

Chief Operating Officer - North America, Darling Ingredients, Inc.

Miropasz.

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Matthew J. Jansen

Chief Operating Officer - North America, Darling Ingredients, Inc.

...Miropasz in Poland, which is €110 million that is expected to close likely in Q1. But outside of that, I would say 2024 is an M&A light year on new acquisitions.

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

I'd call it an M&A holiday.

Ben Bienvenu Analyst, Stephens, Inc.



You've earned it. Very good, very helpful and make sense. On the third quarter in the Feed business, I want to ask about in the UCO segment. The pricing seems to be much weaker year-over-year than, broader UCO quotes would suggest. Is there something discrete or specific that's happening in that third quarter that we should be mindful of as we think about the relationship between pricing in that segment and the pricing of used cooking oil out in the marketplace?

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.



You know, this is Randy. Year-over-year, I think prices were \$65 down to \$55. You know, so off about 20-percentish. Remember Q3 a year ago, Diamond Green Diesel III was not operational yet and so we were still trading a bunch of material around the world. So as Brad said earlier, you got some leads and lags, you've got some quality premiums, you got, some trading that was going on there. But I don't know, anything else you want to add, Brad?

Brad Phillips

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



No. That's it. Oftentimes, when we're exporting in the past, there can be some premiums built in there with thewith that exporting. So that'll all flush out now that we have all three units on and are...

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.



Right.

Brad Phillips

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



...going forward.

Operator: The next question comes from Matthew Blair of TPH. Please go ahead.

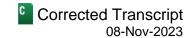
Matthew Blair

Analyst, Tudor, Pickering, Holt & Co. Securities, Inc.



Hey. Good morning. Thanks for taking my questions. I guess the first one is, I think in your recent guidance, you talked about that you anticipate DGD margins higher in Q4 versus Q3. And I wanted to see if that's still held, on our modeling it seems like you would receive a pretty nice tailwind from the hedging side of things, but we were

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worried that there would still be some of that price lag impact from your feedstocks versus the low D4 RINs in Q4 that might weigh on margins. So wanted to check on that first.

Matthew J. Jansen

Chief Operating Officer - North America, Darling Ingredients, Inc.

A

Yeah. I would say that's a – that's the reality of the way our book works. We do have – we have you know, we have to manage the pipeline through DGD. There's anticipated purchases. And so we're chewing through that but I would say that the – if you think about the progression through the quarter, December will be better than October.

Matthew Blair

Analyst, Tudor, Pickering, Holt & Co. Securities, Inc.

Yeah. We see that too. And so just to be clear that the guidance is still that Q4 DGD margin is higher than Q3?

Randall C. Stuewe

Analyst, TD Cowen

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

We – clearly, we're going to make more gallons. I mean, that's an absolute and right now, if we had to look at it, as Matt said, as each month goes on and that margins widen and our spot margins, as you can see, are much better, we should have a hedge gain coming back provided there's no major rally again in the heating oil market. And that's assuming D4s and LCFS really kind of flat.

Operator: The next question comes from Jason Gabelman of Cowen. Please go ahead.

Jason Gabelman

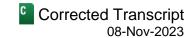
Yeah. Hey. Thanks for taking my questions. My first one is on the 2023 outlook and it's a two-parter. The first part of it is, you had initially or previously guided to \$1.875 billion, you reduced that. In hindsight, where do you think you were off from the prior to current guidance? And then as you think about the \$100 million EBITDA range for 4Q, how do you think about what's driving the high to low end of that range? And I have a follow-up. Thanks.

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

Yeah. I think there's three letters that drove most of it, DGD in Q3 clearly was a – didn't deliver what we thought it was going to be. And clearly, we're being somewhat conservative on DGD Q4. Right now, it looks like, DGD has got to deliver for us to get to the high end of the range in Q4 and then the fat prices that that didn't get recognized in Q3 because they were sold to DGD in Q4 have to flow through. So you know, like we just said, there's timing issues here that puts you that kind of range. You know, I continue to look at myself in the mirror and say, why am I even trying to guide this thing after [indiscernible] (00:51:49) years? So, it's just like – this is – but we have a pretty good feel for it.

I mean, as we came in – and I'll just remind the listeners, as we came in sequentially out of Q2, we said seasonally we would be lower in Q3 and we were and you know, so plus or minus 5% is not bad. What we didn't see coming at us was the DGD, all the volatility that hit there due to, whatever you want to call it though, the war in the Middle East and D4 RINs collapsing and everything there that could have happen to you happened. You know, the buyer took this offline. You know, that was another 10 days for our minor disruption, as we call it. And, the team did a magical job, but it just, you got to power down and power it back up. And that's six days with three

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or four days of repairs. So those, that took another, I don't know, 20 million gallons or offline or whatever it was. So that's why we're a little more bullish Q4 than we were in Q3 here.

Jason Gabelman

Analyst, TD Cowen

All right. Great. And my follow-up is on the 2024 outlook. And it seems like there is a decent amount of crushing capacity for soybeans coming online in the US. And as we sit here, soybean oil pricing is still decently above where it was kind of relative, I guess, to where it was prior to COVID. So it does seem like there's potential for some downside next year. And I know you touched on it earlier, but I was just wondering if your outlook factors in all that new crushing capacity coming online in North America and how that can impact vegetable oil prices. Thanks.

Matthew J. Jansen

Chief Operating Officer - North America, Darling Ingredients, Inc.

Yeah. Hi. This is Matt. I would say, yes, that is factored into our expectations, with oil or — and including protein. So, these new plants are known projects. It wouldn't surprise me similar of what we're seeing in the RD space if some of them get delayed for a myriad of reasons. You know, one of the things we really haven't talked about lately is the — with the — this increase in interest rates that we've seen, CapEx and the money it takes to build and operate is — has gone up. So that — I mean, that's just the reality of the business. But at the end of the day, yes, they — we're — we incorporate that into our expectations.

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

Bob, you got anything to add?

Robert Day

Executive Vice President - Strategy, Darling Ingredients, Inc.

Yeah. I think I would just add that, near-term imports have had a bigger impact on added crush capacity in the United States for oilseed crush. And the other thing is that we are, overall as an industry, increasing renewable diesel capacity at a much faster pace than we're adding oil production capacity. Short term, we've got a lot of oil in the system and we've seen pressure on prices. But if you – even getting out 12 to 18 months, it's going to be pretty tough for the soybean oil industry to keep up with demand as we see it.

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

Randall C. Stuewe

Chairman & Chief Executive Officer, Darling Ingredients, Inc.

All right. Thanks, everybody, for your questions today. As always, if you have additional questions, reach out to Suann. Please stay safe. Have a great holiday season and we look forward to talking to you in the future.

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

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