Orbia

First 2022 Earnings Results

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CORPORATE PARTICIPANTS

Sameer Bharadwaj – *Chief Executive Officer*

Jim Kelly – *Chief Financial Officer*

Gerardo Lozoya – *Investor Relations Director*

PRESENTATION

Operator
Good morning, and welcome to the Orbia First Quarter 2022 Earnings Results. All participants will be in listen-only mode. Should you need assistance, please signal conference specialist by pressing the star key followed by zero. After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press star then one on the telephone keypad. To withdraw your question, please press star then two. Please note this event is being recorded.

I would now like now let's turn the conference over to Gerardo Lozoya, Director of Investor Relations. Sir, please go ahead.

Gerardo Lozoya
Thank you, operator. Good morning, and welcome to Orbia's First Quarter 2022 Earnings conference call. We appreciate your time and participation today. Joining me are Sameer Bharadwaj, CEO, and Jim Kelly, CFO.

A friendly reminder before we continue, some of our comments today will contain forward-looking statements based on our current view of our business, and actual future results may differ materially. Today's call could be considered in conjunction with cautionary statements contained in our earnings release and in our most recent Bolsa Mexicana de Valores report. The company disclaims any obligation to update or revise any such forward-looking statements.

With that, let me now turn the call over to Sameer.

Sameer Bharadwaj
Thank you, Gerardo, and good morning, everyone. I would first like to take the opportunity to recognize our employees for their resilience and dedication to Orbia and our stakeholders and customers for their faith in Orbia as we advance life around the world. We are facing challenging times across the globe given the devastating crisis arising from the invasion of Ukraine by Russia, inflationary pressures, and the lingering impacts from the COVID-19 pandemic. I am proud of our team who has led the way in maintaining a relentless focus on serving our customers with essential solutions to advance life around the world.

Before going into our numbers, as you may have seen, Orbia is hosting an Investor Day on Tuesday, May 17, 2022, and I'd like to take this opportunity to personally invite you to the event which will take place in Boston. There will also be a live webcast of the event for those who cannot attend in person. During the event, we will provide insight into the company's sustainability aligned business platform, long-term growth and value creation strategy, and multiyear financial targets. I hope you can join us on the date.

Now turning to slide 3, I would like to share a high-level overview of a first quarter 2022 performance. Orbia had another strong quarter starting the year on a high note. Our diversified and integrated portfolio allowed us to deliver robust results which more than offset the impact of continuing macro pressures such as cost increases in raw materials, supply chain disruptions and energy costs, and commercial choices stemming from the invasion of Ukraine by Russia. This represents our fifth consecutive quarter of strong results and significant growth.

Revenues for the quarter total $2.6 billion up 36% versus the prior year, and EBITDA totaled $611 million an increase of 35% compared to the prior year. These results were driven by solid performance across our business groups with continued strong demand and pricing. Our EBITDA margin of 23.5% was at the same level as the year-ago quarter.

Finally, we increased our operating cash flow to $194 million, in spite of increased working capital needs due to higher receivables related to the strong volumes and pricing. Our financial performance is underpinned by a healthy balance sheet that enables us to execute our growth strategy by investing in innovation, geographic expansion, and bolt-on acquisitions.

During the quarter, our Building and Infrastructure group completed the acquisition of a majority stake in Vectus Industries, Ltd., a privately held manufacturer of pipes and fittings and the market leader in water storage tanks in India. This acquisition puts Orbia at the forefront of India's high growth water management industry.

We also continued to grow through strategic partnerships. Fluorinated Solutions signed a three-party letter of intent with Foosung and the Mayor of Kedzierzyn-Kozle, Poland to create a joint venture to meet growing demand for inorganic fluorine compounds used in the production of lithium-ion batteries in Europe.

Orbia Ventures participated in an investor syndicate backing Verdagy, a green hydrogen cell technology developer with new electrolyzer technology. We believe green hydrogen will play a significant role in helping to decarbonize industrial processing at scale. Investment funds raised will be directed to accelerating development and commercialization of Verday's technology.

I would now like to turn the call over to Jim to go through our detailed financial performance in further detail. Jim.

Jim Kelly
Thank you, Sameer, and good morning, everyone. Turning to slide 4, we once again delivered strong top and bottom line results. As Sameer noted, on a consolidated basis, net revenues were $2.6 billion up 36% year-over-year with significant growth in Polymer Solutions, Data Communications, and Building an Infrastructure. EBITDA is up 35% with margins of 23.5% which were flat compared to the first quarter of 2021.

We delivered strong operating cash flow of $194 million during the quarter despite an increase in working capital primarily reflecting higher receivable balances associated with increased volumes and prices. Working capital days were flat compared with year end 2021.

Capital expenditures of $101 million were up 89% in the quarter compared to a lower bass last year as COVID-19 restrictions prevented us from executing certain projects in the beginning of 2021. We closed the first quarter with net debt of $2.9 billion, and our net debt to EBITDA ratio was 1.29 times.

Our effective tax rate for the quarter was 34%. This was driven by the appreciation of the Mexican peso in the quarter. In summary, we have a strong balance sheet that allows us to take advantage of investment opportunities for organic growth and bolt-on acquisitions and to return cash to shareholders during 2022 and beyond.

Turning to slide 5, I'll go through our quarterly performance in a bit more detail by business. In Polymer Solutions, performance was driven by strong top line growth due to robust demand in the construction industry and the ongoing tight supply demand environment that continued to support PVC pricing. Additionally, and as a reminder, last year's results were impacted by adverse weather conditions in the United States Gulf Coast region which negatively affected volumes. Revenues were up 50% year-over-year, and EBITDA was up 38%. EBITDA margin decreased approximately 270 basis points as higher costs during the quarter were not fully offset by pricing.

After a strong start to the year, we're expecting prices in the coming months to remain strong as we head into the peak demand season of the year. We continue to expect the PVC market to remain tight in the coming years with global demand outpacing supply.

For Building an Infrastructure, we continued to see solid growth in both Europe and Latin America. Revenues increased 15% year-over-year, mainly driven by higher pricing. EBITDA was up 10% on top of an already strong baseline in 2021 with a margin of 13.5% down approximately 50 basis points due to input cost increases which were partially offset by pricing and a mix shift to value-added products. This quarter includes contribution of the Vectus transaction, which started consolidating in our results in February of this year.

Now let me turn to Precision Agriculture. Revenues during the quarter increased 14% year-over-year mainly driven by growing demand across most markets including the US, Mexico, and Turkey while India also started to show signs of improvement. EBITDA was flat with a margin of 16.8% down approximately 230 basis points largely due to higher year-over-year raw material and input costs that had not yet been fully reflected in selling prices.

For Data Communications, revenues increased 77% year-over-year, and EBITDA increased by 143%. EBITDA margin was 21.6% an expansion of approximately 590 basis points. The revenue and EBITDA increases were primarily driven by robust volume growth in North America, and more favorable pricing.

Turning to Fluorinated Solutions, revenues increased by 19% driven by higher demand and strong pricing, particularly in refrigerants. EBITDA increased 37%, and EBITDA margin was 37.4% an increase of approximately 500 basis points primarily driven by favorable pricing and product mix which was partially offset by increased input costs.

In summary, this was another quarter of strong financial performance and continued focus on operational and commercial excellence. Let me turn the call back to Sameer.

Sameer Bharadwaj
Thank you, Jim. I'm on slide 6. We continued our commitment to the science-based targets initiative to establish a carbon reduction target that extends to Scope 3 emissions reducing the environmental footprint of our products. During the first quarter of the year, we published Orbia's 13th Annual Sustainability Report covering the role we play in society and our impacts on people and planet together. We strengthened our reporting suite by providing a companion 2021 ESG Data Book which provides a data-driven view of our ESG performance. We also further improved our TCFD-aligned disclosures in our climate report including a more in-depth description of our climate strategy, governance, and risk management.

All these recently published reports show the encouraging progress made towards our goals. Orbia's improved performance has also been recognized by external parties as we were upgraded by key raters, MSCI and Sustainalytics.

Particularly, I want to highlight that we have set a new target to reduce our environmental footprint across the value chain, which is Scope 3 emissions, by 30% by 2030. With this aggressive target, we position ourselves as one of very few companies worldwide to actually set a Scope 3 target following the SBTi criteria demonstrating our commitment to decarbonization and climate action.

Turning to slide 7 and our 2022 outlook. Given the strong results that we achieved during the first quarter, we are increasing our EBITDA forecast for the year to a range of $1.75 billion to $1.9 billion. Our other assumptions remain unchanged from the information communicated in our February earnings call.

Operator, we are ready to take questions.

QUESTIONS AND ANSWERS

Operator
We will now begin the question and answer session. To ask a question you may press star then one on your telephone keypad. If you're using the speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press starting than two. At this time, we will pause momentarily to assemble our roster.

Our first question will come from Alejandra Obregon with Morgan Stanley. You may now go ahead.

Alejandra Obregon
Hi, good morning. Thank you for the call and for taking my questions. Congratulations on the numbers as well. My question is related to Netafim. I was hoping to understand with more granularity what's driving your numbers here. We saw a 14% growth year-on-year. So, first off, in terms of demand, what is it that you're seeing in the different regions?

More importantly, in terms of pricing, how should we think of the pass-through of polyethylene here? It seems that it that it was harder this quarter. So, I was just hoping to understand where you have a greater speed-to-market in terms of your regions. How does pricing typically work in the industry for us to have a better sense here? Really anything that can help us understand growth and what's ahead of you in this division. Thank you

Jim Kelly
So thank you for the question. This is Jim. In terms of the quarterly results, we're very pleased. Netafim is really having a great year so far, and in fact, even last year was having a very good year were it not for the results that we saw in India. You may recall that in 2021, due to COVID impacts in India, the business was challenged there, but even back through 2021 the business was seeing very strong volumes globally, and that has continued into the first quarter of 2022.

Again, going back to 2021, you may recall that we were having difficulty given the competitive nature of the business and fully passing through cost increases as they were presented to the business. We did make progress in that area as we progressed through the year and into the first quarter of 2022. So, part of the margin improvement that you're seeing in the first quarter of 2022 is a continuation of passing on the cost increases that we saw in 2021.

We do anticipate that we will continue to make progress in passing those costs through in the second quarter and believe that by the end of the second quarter all of the 2021 increases should have been passed through. So, that being the case, we do continue to see some logistic cost increases, and we will do our best to pass those through in pricing as best we can in the upcoming quarter, but there is some continuing cost pressure there.

In terms of the ability to raise prices by region, to a certain degree there is a competitive element to this business, where it can be can be challenging, but again, we are seeing a robust environment, and significant demand for the product really throughout the globe, and I should note seeing improvement in India this year as well as compared to what we saw last year.

Sameer Bharadwaj
Very good. Jim, I think that you've covered it essentially. Alejandra, thank you for the compliments. Demand is resilient across the world in Netafim's core segments, and they've almost caught up on price increases to recover costs, and we are pleased to see India on a path to recovery.

Alejandra Obregon
Thank you. If I may have a follow-up on the back of demand specifically. I remember that there were some large projects that you were hoping to kick in into 2022, so is it those projects that are driving demand during the quarter, or do you think it's more linked to pricing entirely? How should we think of it for your end? I think if you can just help us break it down in terms of demand and pricing.

Sameer Bharadwaj
Alejandra, it's a mix of both. So, demand is fundamentally strong. We are seeing good growth in demand in the Americas, in Europe, recovery in India. Demand remains exceptionally strong in Central Asia as well, and so there are some timing issues related to the timing of government subsidy programs, but none that concern us at this time, and as we said Netafim is on a good path to margin recovery by being diligent about putting cost increases through.

Alejandra Obregon
Very clear. Thank you very much, and congratulations again.

Sameer Bharadwaj
Thank you.

Operator
Our next question will come from Luiz Carvalho with UBS. You may now go ahead.

Luiz Carvalho
Thanks for taking the question. I have basically two questions here. The first one is regarding capital allocation. The company has been able to deliver quite good results and smart leverage right now. So, I'd like to try to address here how we should think about the capital allocation strategy looking forward. [Indiscernible] about dividends/potential organic and inorganic growth or even buybacks. How would you consider that?

The second one is mostly about the [indiscernible] to Europe and how you're seeing this conflict between Russia and Ukraine and the lack of natural gas in the continent that may affect your businesses looking forward.

If I may, a third one very quickly. In the past, there was some discussions about potentially listing the company in the US. Just would like to take the opportunity to check how this plan is going right now. Thank you.

Sameer Bharadwaj
Very good, Luiz. Let me take the questions here. On capital allocation, as we have consistently said before, let me start with dividends. You are aware that we have raised our dividend this year in line with increase in earnings including a special dividend, and our expectation is we hope to increase our baseline dividend as our earnings grow over the next several years. We will continue to buy back shares, of course prioritizing growth projects first, and then opportunistically buy back shares at the same levels as we have in the in the past.

Then, in terms of where we will focus going forward, you will hear a lot about our plans on Investor Day on May 17th, and I'm hoping you'll be able to attend in person, Luiz, but what I can share with you is we have line of sight to significantly growing the company in both top line and bottom line over the next several years with most of the growth coming from organic growth projects, 70% to 80% of the growth coming from organic growth projects supplemented with selective bolt-on acquisitions, and again, these bolt-on acquisitions, the nature of these should be such that they either address a gap in our geographic footprint or technological portfolio and come with significant growth and synergies. So, that's our plan for capital allocation over the next several years which you will hear a lot about on Investor Day.

As far as illegal imports are concerned, we are seeing some improvement in the situation with the attention given to it by the European Union and the authorities, the extent of training at the customs level, and the number of seizures that have happened over the past year. At the same time given the supply chain and logistics challenges coming out of China, the supply of illegal refrigerants has been impacted by that. Then, much of these illegal imports who are coming through porous borders in Ukraine and Russia and Turkey, and that has been impacted one by COVID and by the war that's going on right now. So, we are seeing it hasn't come to a stop, but we have seen reduced levels of illegal imports.

You asked a question about the impact of gas on our operations in Europe. You know, we have significant operations Germany where our Polymer Solutions business has its flagship specialty resins integrated facility, and we have seen increases in energy costs that we have been diligently passing on to customers through price increases.

Having said that, the situation is uncertain. You've seen how Poland and Bulgaria have been cut off from Russian gas. Now, while that will have a limited impact on us, it's hard to predict how this war will evolve, going forward, and of course, we will monitor the situation carefully.

I think your last question was around a listing in the US. You know, look, we keep monitoring that, and it's not, like I've always said in the past, it's not a near-term priority. Having said that, we are open to looking at all options for creating value for our shareholders, and this is not something that we rule out at a certain point of time in the future, but the current focus of the teams will be to focus on value creation on the left hand side of the balance sheet, and as we go along this journey, we will continually explore options on the right hand side of the balance sheet that include a potential listing in the US.

Luiz Carvalho
Okay, very clear. Thank you very much.

Sameer Bharadwaj
Thank you, Luiz.

Operator
Our next question will come from Diego Serrano with Credit Suisse. You may now go ahead.

Diego Serrano
Thank you. Hi, Sameer, Jim, Gerardo. Thank you for the opportunity to ask the question. You mentioned that you expect PVC prices to remain strong going forward, so in that sense, how are you seeing these PVC prices for this quarter taking into account that IHS estimates are forecasting high single-digit sequential increase? Could we hear further upward revisions to your guidance portfolio '22 if this price increase were to materialize?

Sameer Bharadwaj
That's a very good question, Diego. Let me bring you back to what we've been saying all along. For

about five or six quarters, we've been saying that there's a fundamental supply demand disconnect in the PVC industry where demand growth exceeds supply growth, and when the industry is running at very high utilization levels it takes the slightest amount of disruption to send prices upward.

Now, what you see going on is, yes of course, there's an impact of the war in Europe, the invasion of Ukraine by Russia, and the way that works is you have high oil prices. With high oil prices, you have high naphtha prices. High naphtha prices, you have high ethylene prices, and that works its way into high PVC pricing. So, what we have seen, the same IHS teams had forecasted a decline in PVC prices over the course of this year, but what we have seen is stability at these levels. There may be slight declines coming from some weakness in demand in some regions, or with the COVID shutdowns in China there is more product from China finding its way into other parts of the world.

Fundamentally, I would point you towards the long term, and the long term view still remains that there's a fundamental supply demand disconnect, that will work to keep PVC prices well above pre-pandemic levels, and it takes a significant amount of time to add new capacity before this will be impacted.

So, all I can say is we do expect some level of stability over the course of the year. Of course, we are dealing with cost increases, the gas prices have gone up in the US, so ethylene costs have gone up. Fluorine is at all time highs, and so it's not devoid of challenges, but overall I would expect some stability to a slight decline over the course of the year, and that's reflected in the increase in guidance that we have provided at an Orbia level.

Diego Serrano
Okay, perfect. Thank you. Just a quick follow up, if I may. You talked about Netafim's pass-through. Could you remind us for Wavin and for Vestolit how long that lag is for the pass-through of rising costs to the price and what we can expect for these margins going forward.

Sameer Bharadwaj
So, in terms of Vestolit, we are pretty quick at passing cost increases through whether it's raw material costs or energy costs, and I would say that time lag is in the order of months. In the case of Wavin, once again, if demand remains strong, they have very strong ability to keep putting cost increases through and they have demonstrated that quite successfully in 2021, and they continue to demonstrate that in 2022. The ability to put cost increases through decreases if there is weakness and demand which has not been the case so far.

Diego Serrano
Perfect, very clear. Thank you.

Sameer Bharadwaj
Thank you, Diego.

Operator
Our next question will come from Liliana Veleon was GBM. You may now go ahead.

Liliana Veleon
Hi, good morning and thank you for the call. I would like if could share with us more color on price volume mix in Polymer Solutions. I mean, we saw high record PVC prices in November but sales are really, really strong. So, I don't know if you could volumes and price mix during this quarter. The second one is in Dura Line. We saw really strong results in LDA, so I just want to know if maybe there's a new contract or better mix or new client, just to understand how sustainable it is. Thank you.

Sameer Bharadwaj
Okay, I think your first question is around volumes in Polymer Solutions, and let me address that at a high level. If you remember, in 2021 we had the Texas freeze, and that had a significant impact of volumes during that period. Also, volumes are affected by plant shutdowns, and so this year we entered this year with an expectation of higher volumes simply from those two effects not being there in 2022. So, that explains the growth and volumes, and keep in mind that we are running at very high utilization levels, and given the strong demand we are able to sell out everything that we can we can produce.

The second question was around—can you please remind me the second question?

Liliana Deleon
Yes, sure. Dura Line—

Sameer Bharadwaj
Oh, Dura Line, yes. Now, Dura Line, keep in mind last year in 2021, Dura Line went through the challenge of putting cost increases through. Given the nature of their contracts, they're longer-term contracts. It takes roughly six months to put cost increases through in Dura Line, and they have successfully demonstrated that over Q4 and Q1. Demand is extremely strong, and this fundamental demand growth is supported by the growth in cloud computing, 5g telecom, strong demand with the hyperscalers like the Amazon Web Services, Facebook, Amazon, and Google, etc. So, there's fundamental strength in demand which we expect to continue, and that is reflected in the results along with the fact that they've done a good job of catching up on cost increases.

Liliana Deleon
Perfect, thank you.

Operator
Again, if you have a question, please press star then one.

CONCLUSION

Operator
There are no further questions. This concludes our question and answer session. I'd like to turn the conference back over to Sameer for any closing remarks.

Sameer Bharadwaj
Thank you very much. Really appreciate everybody on the call and the thoughtful questions. Once again, I would like to take this opportunity to remind everybody about Investor Day on May 17th from 9:00 a.m. to 1:00 p.m. eastern time. We invite everybody to attend in person in Boston as much as possible, but if you cannot attend in person the conference will be available online in a hybrid fashion.

We are really looking forward to sharing with you our view on who Orbia is today, how Orbia creates value for customers in their applications, our view of Orbia in the future as it addresses critical world challenges, our capital allocation strategy, and how we will create value for shareholders. I'd love to engage you in Q&A at the Investor Day meeting on May 17th. So, once again, it's May 17th at 9:00 a.m. to 1:00 p.m. eastern time either in person or online. Thank you very much. Bye-bye.

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