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AGT Food and Ingredients Inc.
Fourth Quarter 2015 Financial Results
Conference Call Transcript

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Speakers: **Murad Al-Katib**
President and Chief Executive Officer

Lori Ireland
Chief Financial Officer

Omer Al-Katib
Director, Corporate Affairs and Investor Relations

OPERATOR:
I would now like to turn the conference over to Omer Al-Katib, Director, Corporate Affairs and Investor Relations. Please go ahead, Mr. Al-Katib.

OMER AL-KATIB:
Thank you, Operator. Good morning and thank you all for joining us on AGT's Fourth Quarter 2015 Conference Call. On the line with us today we have Murad Al-Katib, President and CEO of AGT Food and Ingredients, and Lori Ireland, our Chief Financial Officer.

Before we get started, I would like to remind everyone that today's call may include forward-looking statements. Such forward-looking statements are given as of the date of this call and involve certain risks and uncertainties. A number of factors and assumptions were applied in the formulation of such statements and actual results could differ materially. This call may also include references to certain non-IFRS financial measures.

For additional information with respect to forward-looking statements, factors and assumptions, as well as a reconciliation to IFRS measures, we direct you to our news release, our website, as well as our recent filings on SEDAR.

With that, I'd like to turn things over to Murad for some comments and then questions. Murad?

MURAD AL-KATIB:
Thank you, Omer. Good morning to all of you on the call. Thank you for your interest in AGT Foods.
The 2015 year has been a record year for AGT Foods, with record revenue at $1.7 billion for the full year and $101 million Adjusted EBITDA, record volumes moving through our system. Both are milestones important to AGT Foods and very satisfying accomplishments for our business. We look forward to the continued growth through our targeted investments and consistent performance, even in difficult global economic conditions.

We expect our traditional business in pulses and grains to continue delivering the positive foundation for our company. We expect our recent investment in bulk handling and logistics to provide benefit to our ability to supply our customers and our own processing operations with raw materials and quality products, while targeting our value-added processing infrastructure to the activities that they are best suited for.

We expect our Food Ingredients and Packaged Foods segment to continue to grow and transform our company to a leading supplier of quality food ingredients to food companies, retailers and consumers, complementing our traditional business and leveraging the global management, origination, processing and logistics strengths that AGT benefits from. Further, our investment in our Minot food ingredient facility and this production platform for the production of pulse ingredients from a full range of pulses is very important to continuing to grow the business unit. I'd like to speak to our plans for Minot in a little bit, but I'd like to ask our CFO Lori Ireland to give us a summary of the period. Lori?

LORI IRELAND:
Thanks, Murad. Hello. AGT reported adjusted EBITDA of $32.9 million for the quarter ended December 31, 2015 and $101 million for the year ended December 31, 2015. 2015 Adjusted EBITDA increased by 16.1% over the 2014 Adjusted EBITDA of $87 million.

Sales revenue increased in all segments for the year ended December 31, 2015 compared to the year ended December 31, 2014, as well as when comparing the quarter ended December 31, 2015 to the prior quarter and to the same period in the prior year. This is due largely to an increase in bulk shipments of pulse crops that utilized available rail capacity and allowed increased throughput of product for value-added processing in other facilities.

Inventory increased at December 31, 2015 compared to the prior year, from $341.8 million to $430.3 million. The increase is due to a very large harvest in Australia received during the fourth quarter as well as higher commodity prices, particularly in lentils and beans.

Higher prices affecting many commodities affected working capital utilization and net debt calculations in the latter part of 2015. For example, inventory in Australia was approximately 20% higher in price per metric tonne at December 31, 2015 when compared to December 31, 2014. Inventory in Turkey was over 30% higher in price per metric tonne at December 2015 when compared to December 2014.

In some factories, physical inventory at December 31, 2015 actually decreased when compared to December 31, 2014, but since the value increased significantly, AGT's overall inventory value increased. We estimate that approximately $55 million, or over 60% of the increase in inventory, is due to higher commodity prices.

The increased prices also affect accounts receivable, as the sales prices to our customers increased as well.

AGT's operating line was affected by the higher commodity prices and net debt and therefore increased when compared to September 30, 2015 and to December 31, 2014. In addition to working capital requirements affecting net debt, the acquisition of Mobil in October of 2015 and WCRR in June 2015, which totalled approximately $45 million, affected this number. However, due to the timing of these acquisitions, AGT did not get a full year's earnings benefit from them. The AGT global footprint has grown and the business is working capital intensive. Managing assets remains a focus for Management.

Net working capital as a percentage of trailing 12 months revenue is an indicator of net working capital required to drive each dollar of revenue. The ratio has declined from 20.71% at December 31, 2014 to 17.07% at December 31, 2015. This demonstrates AGT's continued focus on turning inventory and collecting cash effectively.

Non-cash foreign exchange was $23.9 million for the year ended December 31, 2015 and includes a snapshot of outstanding foreign denominated accounts receivable and accounts payable as well as outstanding foreign exchange contracts and includes the contract related to the high yield bonds. Note that this is a non-cash item and will fluctuate depending on the strength or weakness of foreign currencies when compared to the Canadian dollar. The amount is excluded from Adjusted EBITDA due to the non-cash nature. AGT has treasury processes in place to ensure that the need to purchase foreign currencies to settle debt will be minimized if it will result in cash losses on foreign exchange.

The increase in general and administrative and marketing sales and distribution expenses for the year ended December 31, 2015 compared to the prior year is due largely to increased average share prices which impact the share-based compensation accrual as well as certain acquisition costs and related additional overhead.

Finance expense includes costs associated with the cross-currency swap on the high yield bond interest that are recorded in both unrealized foreign exchange and in finance expense throughout the life of the contract. Though these costs affect unrealized foreign exchange and finance expense, these are non-cash adjustments which have no impact on Adjusted EBITDA. The expense also includes a fair value adjustment on this instrument.

AGT also utilizes various trade finance instruments and the costs associated with these instruments are also recorded in finance expense. On a normalized basis, finance expense is in the range of $6.5 million to $7.5 million per quarter when considering interest on bank indebtedness, long-term debt, bond interest and various trade finance instruments.

AGT tracks Adjusted Earnings per share as it is reports this value exclusive of the non-cash foreign exchange effects of our global business, whether that means a gain or a loss, because Management feels that inclusion of both gains and losses that result from snapshot non-cash IFRS effects do not accurately reflect the cash flow generating ability of our business. Adjusted earnings per share improved to $0.64 basic and fully diluted for the three months ended December 31, 2015 from $0.51 basic and fully diluted for the three months ended September 30, 2015. Net earnings per share increased to $2.04 basic and $2.02 fully diluted for the year ended December 31, 2015 compared to $1.76 basic and $1.75 fully diluted for the year ended December 31, 2014. Thank you.

MURAD AL-KATIB:
Thanks Lori. As you can see, AGT's business is performing well within our expectations and forecasts. We expect continued positive performance in 2016 with strong demand for pulses, staple foods and ingredients translating to shipped volumes of our product.

As well, we target the transition and integration periods of new business units as a result of our expansions, investments and capitalizing on operational efficiencies to provide additional gains for our operations globally. The big announcement we have made along with our quarterly results is the addition of additional fibre milling capacity as well as a fourth production line at our Minot food ingredients facility. These investments are expected to increase our fibre processing and granulated pulse flour production as well as the overall production capacity for proteins and starches.

We feel these expansions are required to match our forecasting on potential volumes as our business grows in the pulse ingredient for the human food sector as a result of success with our partner Ingredion to ensure that we can deliver on the new business while maintain the volume business we have built in pet food. This expansion follows our previous expansion on de-flavouring and enhancements of our pulse ingredients from Minot anticipated to be completed shortly, with the commissioning plan to commence in Quarter Two 2016, as well as the infrastructure investments that are facilitating our ability to add capacity as needed with low capital cost, as the building and infrastructure were built in early 2016 to accommodate this future growth.

We plan to commence installation of additional milling in June 2016, and the additional processing line, which would be the fourth production line, is planned to commence installation late in the third quarter of 2016. Both lines are expected to be commissioned in the first quarter of '17. This, in addition along with the de-flavouring and product enhancements already underway, makes the Minot facility truly a flagship of our company and creates great opportunities to grow for our food ingredient platform.

As a part of this announcement, we're also examining the feasibility of adding a pulse flour and fibre processing capacity to our production facility in Turkey. With the infrastructure we have there and with its proximity to European markets, Turkey adds logistics and production advantages to the food ingredient business unit to satisfy anticipated growing demand in these markets for pulse food ingredients.

Let me be very clear. Management is pleased with the progress to date in the food ingredients business. The road ahead to continue our penetration in the complex foods sector is one that has a longer development cycle, as food companies better understand the attributes and benefits of our product offerings. We are already down the path with a strong pipeline of projects with many global food companies having seen new products being launched over the past periods. We will have de-flavoured product for sale in the next quarter.

We will prepare for the needs of the future pipeline by having dedicated production capacity that may be dedicated to certain pulse ingredient production. For example, we need lines that can run faba beans while we run peas, or to run lentils while we run peas. The announced investments will allow us to be a fully integrated processor of food ingredients from pulses, meeting the needs of our customers as they further define these needs in their product development cycle. We will be very flexible in our production, able to move from product to product with lower downtime and higher efficiency.

We're meeting the needs of our customers. The remainder of 2016 will be an important transformational time in this segment as we complement the pet food and feed sales with sales for human food. This will take some time, but I'm excited by the fact that we've developed a strong base business and cash flow in this business to sustain the next level of effort that it will take to deliver the scale and sales in the human food markets.

Speaking of the strength of this segment, the packaged foods side of our business is largely driven by our pasta business in Turkey. Arbella has continued to perform strongly with facilities operating at full capacity, necessitating the investment in a sixth long-cut pasta production line that is currently in commissioning, with the line planned to begin test production in April 2016, with packaging equipment installation scheduled for completion in June 2016. Additionally, we are adding a seventh line to produce specialty pasta, including American lasagna, vermicelli nests and noodle specialty pasta. That line was previously announced, but I wanted to report that the line is expected to be completed in mid-2016. Additional expansions to introduce specialty pasta including pasta from pulse ingredients or gluten-free and other products are being investigated as well, with product and formulation developments ongoing and commercial launches expected in the coming years.

These investments in further pasta processing are of course connected to our investment in bulk loading and transportation through the acquisition of durum wheat handling and rail transportation assets in west central Saskatchewan and central Saskatchewan region. With the addition of terminal capacity at the Canadian port of Thunder Bay, these are all moves that are expected to improve margins in this line of business in the coming years by more efficiently supplying raw material durum wheat from Canada for milling to our operations in Turkey and to our customers around the globe.

Speaking of our legacy segment, we're pleased with the way this segment continues to perform, providing the foundation for growth in our business. An average crop came off in 2015; we expect a potentially larger one in 2016. With record prices in Canada for lentils and peas this year, we expect our growers to respond with increased acres that we estimate may exceed 10 million acres of lentils and peas for the first time in Canadian production history. We expect strong prices in the world marketplace are likely to drive additional production in 2016 in Canada, in the United States and in Australia, setting the stage for potential plant utilization gains to contribute positively to our business.

Exports from our origins of operation have been strong, particularly in Canada with very high levels reported in 2015. This trend is expected to continue in 2016, supported by significant production levels that we expect later in 2016. India and the Subcontinent markets and the Turkey and Middle East/North Africa region are principal destinations for Canadian pulses. These markets are important to the relative strength of our legacy segment and we expect imports of pulses to these markets to continue as their own production is not adequate to supply their market needs, with deficient monsoons in India and continued lower production reported in Turkey.

To further support the positive contribution in this segment, our investments in logistics and processing infrastructure, we expect will benefit our business with a large crop and strong customer demand expected in 2016. The investments support our traditional processing infrastructure with a return to the value-added processing activities they were intended for, as well as providing the opportunity to move significant metric tonnes invoiced in our system to provide additional operating leverage with regard to operations in the key Canadian origin, and of course supply of lentils and durum wheat to AGT customers in end-use markets, and AGT's own operations in Turkey and India and the regions that each supplies.

We have increasingly clear demand visibility into 2016 harvest with an order book sale for the fall new crop having already begun, well ahead of a normal cycle. We see this as a signal that there may be a concern with regard to 2016/17 supply and it may be driving importers to buy forward to secure their local market positions.

We expect there may be supply constraints in Canada upcoming in the Quarter Two period prior to harvest in 2016; however, this is a very short-term production constraint and supply availability constraint, with this demand being filled with whatever product is available at the time in advance of 2016 harvest; then, unmet demand can be filled in Quarter Three and Quarter Four. In essence, we're projecting that any volume weaknesses in our platform in the first seven months of the '16 year will be made up by the strong export pace we project for the latter months of 2016.

So overall, before we go to questions, AGT's business is reporting consistent gains and growth in our business as we evolve and expand. We have strategic plans in place with regard to expansion; we're acting on our strong performance recently, demonstrating that these strategies of our Management are the correct ones to grow our company given the strong market demand, significant supply of pulses and staple foods available and the strong demand from our global customers around the world. We'll continue on our path for growth to increase shareholder value while growing our business.

Again, I thank you for your interest in AGT Foods. Omer, I think we'll go on to some Q&A.

OMER AL-KATIB:
Operator, can we take the first question, please?

OPERATOR:
The first question is from Peter Prattas of AltaCorp Capital. Please go ahead.

PETER PRATTAS:
Good morning everyone. Nice quarter. You've announced a number of expansions, so I was wondering if you can talk about what your total capital budget is for 2016 including maintenance CapEx and maybe go through what each component will cost and what each component adds to your overall capacity. Thanks.

MURAD AL-KATIB:
Maintenance CapEx budgets, Peter, are running about $12 million to $15 million a year. That's fairly consistent with our depreciation and amortization. The capital budget forecast submitted to our Board for 2016 is $25 million. We actually expect that that cap budget may be a little bit less; it will probably be somewhere around $20 million versus the $25, and if I break down the capacity expansions that we've talked about, just to be very clear, to start with the packaged food segment, the pasta line number six that we talked a little bit about it in my comments and in the MD&A, that was a capital budget item that was—I think it was largely funded in the 2015 capital budget actually, as was the vermicelli nest. I think maybe $2 million or $3 million of that was just the final packaging and those kinds of things that were funded in this year.

The de-flavouring line capital expenditure that's commissioning now at Minot—again, largely in our 2015 capital budget.

So the new announcements of food ingredient: fourth production line, along with the additional granulated semolina and fibre processing, we're estimating to be around $10 million. It'll add roughly about 35,000 tonnes of protein and starch capacity for 2016 and around 10,000 tonnes to 15,000 tonnes of additional flour and fibre granulated capacity. So count it around 45,000 tonnes to 50,000 tonnes of total additional volume that will be added. It'll in essence increase our volume by about 50% in the Minot facility, taking it from just over 100,000 tonnes to around 150,000 tonnes of production.

In addition to that, we have a number of small CapEx items around the world. I think we've got $5 million to $7 million in our Canadian platform, one or two in Australia. It just goes around the world where the balance comes up to around $20 million.

Those will set us up nicely. Those projects are underway and we'll have them largely completed before calendar year end to be contributing into Quarter One of 2017.

PETER PRATTAS:
Great. Where does that get you to for the ingredients group in terms of total volume capacity?

MURAD AL-KATIB:
About 150,000 tonnes. We had about 105,000 tonnes of capacity prior. I guess if we count granulated flour prior it was about 125 and we're adding around 45 to 50. It'll take us up to probably closer to 170 to 175.

OPERATOR:
Our next question is from Steve Hansen of Raymond James. Please go ahead.

DAN CHEW:
Hey guys, it's actually Dan Chew proxying for Steve this morning. Just a quick question here on the supply challenges you mentioned in your preamble and the MD&A. Not really dissimilar to last year just given the strong export case, and frankly not that surprising you flagged this, but can you maybe just talk about how you guys are better equipped here on your new platform and is there any other differences between this year versus last year that we should be thinking about. Thanks.

MURAD AL-KATIB:
Thanks. Good question. I mean even last year supply constraints were there and they were really quite significant, and I think if I look back we still delivered around $26 million EBITDA in Quarter Two. In fact I think that might be our second-best quarter ever.

Supply constraint doesn't necessarily mean poor financial performance. I think that where we are today is we have a very balanced geographic platform, and so when Canadian supply is constrained, margins in Canada go up, margins in our processing operation in Turkey go up, and margins in our food ingredient platform are very stable and kind of delinked from the supply side. So, I think that ultimately we're well equipped to deal with it, it's going to be a very temporary, you know, three-four month kind of phenomenon, and I do believe strongly that with the bulk capacity that we now have that we didn't have prior, with the addition of West Central Road and Rail and Mobil Capital, with the railway additions, we have a very big handling and processing capacity for the bulk side that will allow us in the third and fourth quarter to make up any volumes that we don't do in the second quarter. I think that when we look at the totality of a four-quarter forward, I think you're going to see very, very positive results for AGT.

OPERATOR:
The next question is from Greg Coleman of National Bank Financial. Please go ahead.

GREG COLEMAN:
Yes, thanks very much. Sorry to keep on this, but I just want to understand a little bit of the cadence for the year. So, if we are talking about a little bit of potentially the supply chain being capacity constrained in through Q2, would you expect to see a bit of a surge in Q1, drop down in Q2, and then grow back as we go into the last bit of the year?

MURAD AL-KATIB:
That's probably what we expect, Greg. I think that you will have a little bit of a supply constraint over Quarter Two, as we saw last year. I mean, if you look at the results in last year, I don't remember the exact percentage, but off the top of my head my volumes were probably down 25% or something in the second quarter, yet my profits

were up. I can't really relate how the earnings are going to look in terms of that progression, but I do think that from a volume handling perspective we're going to have some supply constraint.

I do think that again, because of that large bulk capacity that we do have now, when that demand is unfilled in the second quarter into the third quarter, there's going to be a very strong August/September/October/November shipping period that I think we're going to be able to make up a lot of the gain, so you'll see a bit of a spillover from Q2 to Q3.

GREG COLEMAN:
Then just keeping on the volume theme—thanks for that—just keeping on that volume theme, the very, very strong volumes you saw in Q4 there, you talked about the strong Australia harvest and how that contributed to it, but we did see margins on a per tonne basis pull back slightly on the legacy processing business. I would have expected a bit of an expansion. Is this a strategic decision on your part to try to drive volumes a little bit higher, being a little bit tighter on the pricing there, or is that just kind of noise in the system from one quarter to the next?

MURAD AL-KATIB:
Yes, I think that ultimately—you know, when I look at the fourth quarter, there was some bulk volume done, both in the pea sector, durum wheat and pulses side, that was probably some of the volume that we may not have done in the past, and so we're definitely going to seize that opportunity, Greg, as we go forward. When we did the bulk investment, we did say that the margin profile of the bulk segment may be slightly less, but at the same time it will allow us over time to return the processing plants back into more value-added production. So, I think that what you'll see over a full cycle period is those lower margin tonnes we do will be offset by some higher margin tonnes that we're able to do from our plants. We used to ship a lot of bulk red lentils out of our plants that are now going to go through the West Central Road and Rail railway system, that now free up our Rosetown facility to do more processed green lentils and red lentils. So, I think that that will allow us over time to recover those margins.

You know, sequentially, prices were going up dramatically and I think that some folks look at escalating prices as something that actually helps our margins, but I can tell you that when prices go up as fast as they went up this year, even though we're keeping our commodity position relatively square, it gets tough to maintain your margin when prices are escalating very, very quickly. Buyers resist the pass-on, and at times, with really significant quick escalation, margins do get a little bit constrained. So, we've been happy with the bit of the price pull-back, we think that it's important. Our growers are very happy with the high prices, but we want fluid demand, and we're expecting the new crop prices to come down a bit and ensure that fluid demand returns to our system.

OPERATOR:
Once again, if you have a question or a follow-up question, please press star, then one. The next question is from Anoop Prihar of GMP Securities. Please go ahead.

ANOOP PRIHAR:
Good morning, just a couple of quick factual questions. First of all, what was your capacity utilization in Q4, as well as on a full-year basis?

MURAD AL-KATIB:
The capacity utilization, Anoop, was running around—in our traditional assets, so not including the West Central Road and Rail bulk infrastructure, because… let me start there. If we look at our capacity that we report on our value-added processing facilities, we reported around 1.635 million tonnes of capacity, I think, and from that, around 1.35, or 1.335 million of that is in the pulse and grains processing segment. If we back out the bulk tonnes that we did in the fourth quarter, Anoop, we were running around 1.1 million tonnes for the year, which is running around 85% utilization of our assets over the course of the full platform year. That's very high utilization. In the fourth quarter, our plant utilization went up over I think it was around 92%.

What that is telling us is exactly what the strategy is, which is take some of those bulk tonnes out, bring that capacity back to around 20% available, so bring it down to 80% in our plant, and take the tonnes that were in that boost up to that 92% utilization and put it in the bulk platform at West Central Road and Rail and the railway system. So, I'm expecting utilization to continue running very high in Quarter Three, Quarter Four, Quarter One next year, and I think that that will allow us to continue to show the operating leverage gain that you're seeing here in terms of sequential EBITDA growth.

ANOOP PRIHAR:
When you were talking about your SG&A and marketing costs, I think you indicated that they were somewhat inflated by some non-cash stock comp. So on a cash basis, what's your run rate SG&A and marketing all-in and annualized?

MURAD AL-KATIB:
Lori's just grabbing that figure. Yes, Anoop, our marketing, sales and distribution—or sorry, in our SG&A costs, we had some one-time acquisition costs in there, and then in addition to that, the share-based comp—so this is like our restricted share unit comp. You know, for investors, stock has done very well, and on the restricted share units, of course, the effect of that comp is in the quarter as well.

LORI IRELAND:
Yes, and they're combined about $18 million a quarter now with the new acquisitions.

ANOOP PRIHAR:
So, $18 million a quarter is your cash run rate?

LORI IRELAND:
Yes.

ANOOP PRIHAR:
Okay.

LORI IRELAND:
For the two of them.

MURAD AL-KATIB:
That excludes the—

LORI IRELAND:
That'll exclude the share-based comp, yes.

MURAD AL-KATIB:
Yes. So, about $18 million, Anoop.

ANOOP PRIHAR:
Okay, and then a last question. Obviously, there was a big jump in working capital consumption just as a consequence of the seasonality associated with Q4. Now, you typically give some of that back in Q1, again, just seasonally. So, what's your best guess right now as to how much working capital you think you might be able to release in Q1?

MURAD AL-KATIB:
I think Q1 and Q2, Anoop, you've got to let it go through the system. When we look at commodity prices at year end, if I compare December 31, 2015 to December 31, 2014, commodity prices were up roughly about 30% overall. So when we look at the consistent amount of volume in our system, we end up with about 30% higher prices year-over-year. So when we take that effect, there's roughly about $30 million to $40 million of inventory effect and $30 million to $40 million of receivable effects. So, when we look at that, even though we are a bigger company now, I'm quite hopeful that over the course of Quarter One and Quarter Two, $30 million to $40 million of the working

capital should reverse itself. We are seeing commodity prices in the new crop down by roughly about 20% from where they are even currently, and they're almost—we're up at around, let's say on lentils, 40% to 50% higher than average. We're now around, say, 30% higher than average, and we'll bring that back down even closer as we get the new crop, so I think that the working capital levels will normalize a bit over the coming quarters.

ANOOP PRIHAR:
Thank you.

OPERATOR:
The next question is from Marc Robinson of Cormark Securities. Please go ahead.

MARC ROBINSON:
Thanks. You touched on this a little bit. I guess I'll ask it a little bit more directly. With this big incoming crop, we've already seen prices come down a little bit, and I guess all things equal, they're likely to come down maybe more meaningfully. I'm just wondering how you expect a declining price environment through 2016 to affect earnings.

MURAD AL-KATIB:
Well, there's two things, Marc. I think, again, as I said, with the fact that we keep our commodity position very, very close—I mean, we are pretty much a back-to-back seller, and with that, our long position to run our factories is really kept close to our production schedule. One of the positive things that we think will happen with declining prices is that demand will again be stimulated. I mean, we got to a point where—when you get to very historically high price levels, importers start to feel very nervous, right? We were starting to feel, again, at the end of the fourth quarter and into Quarter One—you know, with the India new crop being harvested as we speak, even though it's not a great harvest, it's still being harvested. There was a little bit of angst within the importing community around the world. With high price levels historical, new crop coming in India and new crop coming in Turkey, there was a general feeling that price levels had to come down.

Now, when you compare within pulses, every pulse is actually at historical high prices right now, but you've got to recognize that cereal grains are not, oil seeds are not, and so from that perspective we're seeing the effect that farmers are planting more here. I think demand is going to be strong enough to absorb it all, but from an importer perspective, a reduction in prices I think is going to be good to have them, ensure that fluidity and normal demand continues on its normal pace. So, I think that's one effect that I think we're going to see.

You know, a declining price environment, to me, doesn't give me a worry on my margins overall, again, because I keep it very, very tight. The opposite is true, though, as I mentioned earlier. When commodity prices are escalating very, very quickly, sometimes we get caught a bit and we're unable to pass it on. So from that perspective, I think that a reset is necessary, Marc, and we're seeing it reflected in new crop pricing already.

MARC ROBINSON:
So, net-net, considering what that'll do to working capital, it could be meaningful, you could pull a lot of working capital out, I guess with declining prices and your ability to hopefully maintain margins and maybe even have some sort of demand boost as a result of lower prices, you think, net-net, lower prices could actually be positive?

MURAD AL-KATIB:
Well, we're expecting a lower price environment to accompany our positive outlook that we put into our filings. So we are expecting with this type of production level—you know, farmers will be happy, they will make a very good return at an average yield, and importers will be able to function and buy regularly, and AGT will benefit with strong earnings.

MARC ROBINSON:
Okay. Thanks.

OPERATOR:
The next question is from Stephen Aldridge of BMO Capital Markets. Please go ahead.

STEPHEN ALDRIDGE:
Yes, hello. Good morning everybody. Can you comment on your dividend policy going forward?

MURAD AL-KATIB:
Yes. Stephen, you know what, we've maintained the dividend always, so even in the times where we had constraints on our earnings, we were certainly still a very strong believer in yield and growth. We continue to be in that boat. With working capital levels at such high levels right now, you know, free cash flows are going to into debt reduction and to fund the growth CapEx. Once commodity prices come back down and we continue this growth trajectory, we will in the future take a look at whether there's an opportunity to increase that dividend. I don't see it in the next couple of quarters, for sure. We do have that discussion at the Board level every quarter. We're very committed to a dividend, we're very committed to the growth story, and we're also committed to increasing our yield over time. So, be sure that we'll be taking a look at that as we continue to ramp up our free cash flow profile.

OPERATOR:
The next question is from Bob McWhirter of Selective Asset Management. Please go ahead.

BOB MCWHIRTER:
Just turning back to the overall capacity and the increases that are expected, if I understood you correctly, you talked about roughly 1.3 million tonnes of pulse processing capacity, you suggested that the Minot increase would be 50%, going from 100,000 to 150,000 tonnes, therefore, there'll be 50,000 tonnes on a base of 1,300 or 1.3 million, which is roughly a 4% increase in overall capacity. Is that a fair summary as to what's happening?

MURAD AL-KATIB:
Yes, it is, Bob, but that's on the value-added processing. When we added the West Central Road and Rail, and the short line rail infrastructure, we are actually adding up—Bob, every time you load a unit train, which is 100 railcars, of pulses or durum wheat, if we repeat a unit train on a 40-week-per-year frequency, we add 400,000 tonnes of capacity. I can tell you that our target will be to ensure that we're moving unit train capacity, unit train per week the entire year, so we're going to be targeting to get to 52 unit trains as a minimum. That's 500,000 tonnes through the bulk handling system.

So, our growth and our capacity on our pulse business is largely going to be in our bulk processing capacity. That will then free up part of that 1.35 million tonnes that we have on the value-added side to get back to cleaning, sizing, destoning, optical colour sorting, bagging and shipping value-added pulses. So, we'll almost have a double effect of that, the bulk capacity—will increase our bulk capacity, but also frees up our value-added.

BOB MCWHIRTER:
Okay, and because I don't know the numbers—you talked about pet food being a percentage of sales and adding on top of that, the kind of move towards human sales—can you talk about how much pet food are as a percentage of sales, what the margins are, and then, in contrast, what the margins are on the—

MURAD AL-KATIB:
Well, I can just give you a notional direction. Pet food today would be around 80% of our sales, and what you see for the margin is largely pet food margin. I can tell you the human food margin we expect to be materially higher. What the capacity increases that we've announced, Bob, are going to do for us is it's going to allow us to be able to produce the human food, food ingredients, while not sacrificing the pet food demand that we already have. I mean, we're running at very high utilization right now on the

three production lines and the lag in installing the next lines is largely due to the fact that, you know, equipment takes time to order and to get in, and there's a lead time from the time we place orders.

The human food side is largely going to be focused on pulses other than peas. So, yellow peas is the main pulse for the pet food market because it's the cheapest pulse, but the human food side is going to be focused a lot more on faba beans and lentils. They are more neutral in their taste initially, and when we put them through our de-flavouring line, they have a very positive profile that food companies are telling us they like in terms of what they're going to incorporate for their product launches.

OPERATOR:
The next question is a follow-up question from Greg Coleman of National Bank Financial. Please go ahead.

GREG COLEMAN:
Yes, just two quick ones. Right on the back of that previous question, can you remind us, please, what the split is on the ingredients side between pet food and human food at the moment?

MURAD AL-KATIB:
It's about 80/20, Greg.

GREG COLEMAN:
Then, just a detailed one on the modeling. You've got non-recurring and other charges of $3.6 million for the quarter. We always see a bit of that non-recurring show up, but it's a bit larger than we've seen historically. I think you talked a little bit around it regarding M&A…

MURAD AL-KATIB:
Share-based comp, Greg, that's the largest one, and then the Mobil Capital, Last Mountain Railway and Big Sky Railway acquisition costs. We had a very significant acquisition cost, in particular related to environmental due diligence. There was a very material amount of due diligence done on the environmental side because we were acquiring 570 kilometers of track bed, and so all of those costs of the due diligence were all expensed through and put in as one-time. That number, again, with the share-based comp, because the share price has been very positive in the quarter, is quite high. We don't expect that number to be high going forward. It's really transactional-based, so I don't foresee that continuing.

OPERATOR:
We have a follow-up question from Peter Prattas of AltaCorp Capital. Please go ahead.

PETER PRATTAS:
Hello again. The ingredients performed well, but I would say relatively less so from a volume perspective, although you did see some volume increase, I think, with pasta ramping back up. Can you update us on the volume capacity of that whole broader food segments category including the packaged food, and tell us when you might get back to that sort of 70,000 plus tonne per quarter level that you achieved back in Q2 of '15? Thanks.

MURAD AL-KATIB:
What was the level this quarter, Lori?

LORI IRELAND:
We were at…

MURAD AL-KATIB:
I don't have it right in front of me, Peter, but I can tell you, Peter, that…

LORI IRELAND:
We were at 60,000, just over, 61,000.

MURAD AL-KATIB:
Okay, just at 61. Peter, I can tell you that the food ingredients capacity utilization was very high. You can't really see that go up much until we get the fourth line put in place. I mean, we really don't have a lot more tonnes to ship. From the perspective of getting back to 70,000, I think that the 70,000 Q2 was a result of some very strong pasta sales.

LORI IRELAND:
Yes.

MURAD AL-KATIB:
We see the pasta outlook being quite positive going forward with the new line coming on, so I do expect that we should see those volumes continuing to increase. I'm actually quite pleased with the capacity utilization on the food ingredients side. We're running around over 90% utilization. We've got a little bit of utilization left to start up the de-flavouring line and that warranted our need to announce the expansion. I think that you saw it continuing to ramp because we were just ramping line one to line two to line three. Now, it's time for a bit of stability and I'm going to focus a bit on margin improvement through the de-flavouring line, until we get the new capacity up from the

first quarter. Stay tuned, I think you're going to see some positive results coming over the next number of quarters in that segment, as well.

OMER AL-KATIB:

Thanks a lot, Murad. Everyone still with us on the call, that brings us to the end of our time for questions in this session. I'd like to thank you all for joining us on our call today. I'd like remind everyone, if there's anyone still on the call, that if you do have follow-up questions, you can feel free to contact us at our Regina head office and we'd be more than happy to follow up with you. Again, thanks for attending this conference call with AGT and I certainly would like to wish you all a very good day.

OPERATOR:

This concludes today's conference call. You may now disconnect your lines. Thank you for participating and have a pleasant day.