Alliance Grain Traders Q2 2010 Earnings Conference Call Transcript

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Speakers:

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President and CEO

Lori Ireland
Chief Financial Officer

Gaetan Bourassa
Chief Operating Officer

Omer Al-Katib
Director, Corporate Affairs and Investor Relations

OPERATOR:
At this time, I'd like to turn the conference over to Omer Al-Katib, Director of Corporate Affairs and Investor Relations. Please go ahead, Mr. Al-Katib.

OMER AL-KATIB:
Thank you and good afternoon. Thank you for joining us and welcome to our Second Quarter Conference Call. On the line with us today, we have joining us Murad Al-Katib, President and CEO of Alliance Grain Traders. We also have Lori Ireland, our Chief Financial Officer, and Gaetan Bourassa, our Chief Operating 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-GAAP financial measures.

For additional information with respect to forward-looking statements, factors and assumptions as well as reconciliation of GAAP measures, we direct you to our news release and our recent filings on SEDAR. I'll now turn things over to Murad for some comments, and then we'll go to questions.

MURAD AL-KATIB:
Thanks, Omer. Good afternoon. Thank you for joining us on the Alliance Grain Traders Second Quarter Conference Call. We appreciate the opportunity to discuss the performance of our company as well as the opportunities that lie ahead for us.

Second quarter of 2010 was a very challenging one. A number of factors have contributed to these challenges, resulting in lower reported numbers than we have traditionally seen.

While our total sales for the quarter saw growth, we did report lower earnings and net income. We would like to share with you some of the factors that contributed to this.

As you know, in quarter one, we saw the slowdown in buying from international markets, which is a normal timing issue that arises every year in the convergence period between old crop and new crop. However, unlike previous years, in quarter two, we saw international buyers postponing their purchase decisions in a market of declining prices and very good replenished international supplies.

Simply, we believe the buyers feared losses on purchases bought at higher prices, even with ample supply available in the marketplace. Turkey is, for the most part, rebounded to more normalized production levels, and reports from Canada and the US are for a record crop level for lentils and most other pulse varieties.

Buyers were afraid to be caught holding the bag for a product they would have to sell at lower levels. As a result of such purchasing delays, local stocks in most key consumption markets are estimated to be at historical lows. This has impacted our overall results for the quarter.

Other factors such as heavy rainfall and overall diminishing supply we have seen in Western Canada and Northern Plain States have impacted our ability to bring what product is available into our facilities for processing during this past quarter. While buyers were hesitating to buy, farmers, occupied by concerns over the wet conditions and impact it would have on their crops, were not delivering their grain into our system.

Ultimately, these factors led to lower sales in our traditional product, say, in particular, lentils and an erosion of margin on our value-added pulse of the staple food business. We were forced to rely on sales of lower margin commodities such as peas to maintain our capacity utilization.

Additionally, in some of our origins, less product was available to process and export. As opposed to reducing staff or hours, management made the decision to keep our people at work and our plants continuing to function by redeploying our people to execute previously planned capital expansion projects.

Completion of these projects is on track for harvest, and we feel they will pay dividends in the quarters to come. We're optimistic about the balance of the year and our ability to develop sales opportunities in all four of our core staple foods platforms.

While we reported higher sales of $149.2 million, as a result of these factors, we reported adjusted EBITDA of only $4.7 million, down from $5.1 million last year and a decrease in adjusted net income to $2.4 million from $3.04 million last year. All of our second quarter 2010 financial results and notes too, that are available on SEDAR and from our website at www.alliancegrain.com.

We really see these factors that have impacted our quarter diminishing as the 2010 year progresses and the 2011 year begins. I want to share with you how we feel AGT is positioned to capitalize on the opportunities going forward in the year.

First is the significant amount of product supply that is expected to be available in the world. In North America, Canada and the US, we're showing signs of estimated record production levels for almost all types of pulses. Turkey is recovered to normalized production levels with some reports showing the highest production levels since 2006, 2007.

Australia has been reporting a positive start to the 2010 crop cycle with good moisture levels. Demand in India looks to continue to be strong. There are all positive indicators for the replenishment of global supply and a return to normal supply and export levels.

These supplies will find their way into consumption markets that they're destined for as buyers will have to fill not only their local market demand for pulses and staple foods, but also to replenish the pipeline that has been diminished from postponing buying decisions.

The significant pent-up demand for our products, we feel, should start to push our exports in the later part of this year. The ample projected stocks, in all origins in the market demand is good news for AGTI and our shareholders.

Our multi-origin strategy was developed to capitalize on these types of conditions as well as protect us from crop shortfalls in the inevitable years that these conditions can happen in some regions.

Obviously, we cannot ignore the reports of heavy rainfall in much of Western Canada. That has affected crops and resulted in lost acres. However, the loss of acres has affected traditional cereal and oil seed crops much more than pulses as many pulses were planted in May before the start of the significant rainfall.

Farmers did manage to put more lentils in the ground as conditions allowed later on in June as we had dry periods, resulting in statistics Canada and agriculture Canada to reporting an estimated feeding level of 3.36 million acres of lentils in Canada. Other pulses report similar, yet not as dramatic increases. Warmer weather in the mid-summer has allowed pulses, which need warm weather as they're finishing maturity to finish properly.

Our overall expectations are for a good quality and quantity of crop in Canada and the US. Of course, we still do have a few weeks until the final harvest.

This comes at a period where all origins are producing, or projected to produce well. We see this as the start of the realization of the plans we put in motion with or expansions into the US and Australia, the acquisitions we completed in Canada and, ultimately, the transformational acquisition of Arbel in Turkey.

The second factor I wanted to cover, to discuss is the steady demand for pulses and staple foods is anticipated to continue. The positive demand is expected to allow AGTI to drive its efforts for better capacity utilization globally as more products produced means more products to process and export.

The normalization of production in Turkey with the completion and integration of the Arbel acquisition is expected to allow AGT to further enter new markets. Arbel, with its close proximity as well as warehousing and production facilities, allow for the opportunity to further penetrate the Middle East, North African markets.

Non-traditional pulse markets like North America and Western Europe are continuing their focus on chickpeas consumed as humus beans consumed year-round, proving opportunities for our facilities in Canada and the US.

Demand in the India subcontinent is estimated to continue high, as it has been for the past few years, with potential for increased shipments at continued good margins from all of our origins, including Australia.

AGTI operating divisions in this way will be well positioned compared to our regional competitors to fill the pent-up demand in local markets around the globe not only for our pulse products, but for other staple foods like our Arbel line of pasta, our rice products, our other milled wheat products like bulgur and the other products we produce like popcorn sunflower seeds.

With regards to our expansions, we have not wavered from our strategy of well-placed, tuck-in acquisitions to complement the organic growth we see on the horizon. Acquisition opportunities that make sense and that provide strategic advantages, whether in processing capacity, freight and logistics or warehousing in key markets, continue to be our focus.

In the past, we have commented on our efforts to smooth the seasonality of our business. The replenishment of the local market supply through 2010 and into 2011 should, we believe, lead to a return to strong sales to fill demands.

This, we feel, will compensate for lower sales volume of some of our core value-added commodities that we have seen recently and continue with our strategy for supplying markets with quality proteins, staple foods on a year-round basis.

We cannot ignore the fundamentals of our company. Our capacity is well placed. Global production looks to rebound. In one month, harvest will start in Canada and in the US.

We feel optimistic about the opportunities and challenges ahead, and we feel we're well positioned to continue on the growth plan to build on the foundation we've established.

I thank you for your interest in Alliance Grain Traders. I'm joined by members of our executive management and will be pleased to answer questions with the remainder of the time. Thank you.

OPERATOR:
Thank you, sir. We will now begin the question-and-answer session.

Your first question is from Robert Winslow of Wellington West Capital Markets. Please go ahead, sir.

ROBERT WINSLOW:
Good afternoon --.

MURAD AL-KATIB:
Robert Winslow, I always take first question. Go ahead, Robert.

ROBERT WINSLOW:
Just trying to get some clarity on the record revenues $150 million, yet talking about not having enough product to put through your facilities. It sounds like it was a product mix issue. Was that because --?

MURAD AL-KATIB:
Yes, it's definitely, Robert. It's a product mix issue. I mean, if you look at the carry-in stocks of pulses, in particular in Canada, we have very significant carry-out of peas.

If you look at our segmented revenue information on the geographic segmentation, I mean, really, the story of the demand change in this quarter is an extremely telling thing. So if you look through to that note, you'll see segmented revenues on the Europe, Middle East, North Africa, which, of course, North Africa, Middle East is our main --.

ROBERT WINSLOW:
Yes.

MURAD AL-KATIB:
Market of concentration. You'll see that revenue went from, I think, just off the top of my head, about $137 million or so down to about $18 million.

So this is really just a complete collapse of the market demand as a result of an anticipated Turkish crop coming very large and prices actually adjusting by hundreds of dollars down. It crippled demand with importers fearful of getting caught, as I said in my comments, holding the bag.

So what that did was it left us in focus on markets like Asia. I have to be honest, Robert. I look at every situation with the future view, too. We're entering new markets. I mean, we were very active in the pea market in China. We were very active in the pea markets in India over the course of this period. The margins aren't what we traditionally enjoy.

ROBERT WINSLOW:
Yes.

MURAD AL-KATIB:
But at the same time, we will continue to push into those markets and continue to try and build our position in those markets and improve our margins as we go forward so that we can continue to drive the utilization of our plants.

So the Asia concentrates, if you look at that segmented info, you could see, again, a very telling story of focus on Asia, focus away from our traditional core strength area of North Africa, Middle East.

That's coming back around. We're seeing, just as we expected, importers are now into the Ramadan season.

So Ramadan started last Wednesday. Already, we're feeling the demand tremors where the importers didn't import enough product for their Ramadan demand and recognized by the end of the Ramadan period they're going to be out of product. So we're ready with our Turkish plant to feed them in the short term, and Canadian and then US new crops are coming.

ROBERT WINSLOW:
Got it. Thank you.

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

MARC ROBINSON:
Hey, guys. How are you?

MURAD AL-KATIB:
Hey, Marc. How's it going?

MARC ROBINSON:
Fine, thank you. You sort of touched on this at the end of Robert's question. But, really, what I'm after is any sort of commentary you can provide on whether you're seeing the early signs of that demand recovery already in Q3.

Then the B part to that question is, if under more normalized conditions, whether you'd expect any change in the margin profile.

MURAD AL-KATIB:
Yes. Gaetan, you're on the call, I believe, right? I apologize because I'm in Turkey. So I think Gaetan you're on the call.

GAETAN BOURASSA:
Yes, I'm on the --.

MURAD AL-KATIB:
Okay.

GAETAN BOURASSA:
Yes. I mean, what we're seeing now is buyers from many markets coming to us with that pent-up demand that Murad mentioned. It's kind of a wait-and-see game, though, because no one wants to plunge in deep because they're scared that Canada does have good yield potential.

So I think over the next two weeks it'll be a telling sign. The sales will start to roll in, and our capacity for October, November will fill up quickly.

MARC ROBINSON:
Then with respect to --.

MURAD AL-KATIB:
Yes, I think that the Marc, just as a further commentary to Gaetan's comment, I mean, this is all a find game, right? We're already feeling it. The inquiry volume is coming up. We know as a result of the fact -- you have to recognize that AGT doesn't just sell product. We have our market intelligence in the markets; we know what stocks are there. We know the pipelines are empty.

At the same time as buyers aren't wanting to plunge into the market, we're also not seeing growers selling. Until they get the crop in the bin with a late seeding and the period that we're at right now, the critical finish period, growers that have sold new crops have sold, we bought it, we sold it.

Growers that don't want to sell are waiting for another couple of weeks until they get the product in the bin. As soon as the product comes, our facilities are ready to roll.

MARC ROBINSON:
Okay, and with respect to the margin profile, once we're well into, let's say, late Q3, early Q4, same sort of margin profile that we've traditionally been used to seeing?

MURAD AL-KATIB:
Marc, I want to tell you. There's no fundamental change in this story. The ultimate markets are sound. We had a complete transition of what I would call a three-year transition happen in one quarter, where you had historically high prices crack down. You had supply diminished in one of the most important production regions; Turkey, for the last two seasons.

All of that came into one particular period. You had the markets that were basically paralyzed. Nothing's changed; margin profiles, demand fundamentals.

This is not product that people decide today, I want to buy, tomorrow, I don't. If they make that decision, it's a temporary decision. That demand doesn't go away because the pipeline needs to be replenished.

MARC ROBINSON:
Okay, that's good. Thank you.

OPERATOR:
Next question comes from Christine Healy of Scotia Capital. Please go ahead.

CHRISTINE HEALY:
Hi, guys.

MURAD AL-KATIB:
Christine Healy, how are you?

CHRISTINE HEALY:
I'm good, thanks. First question is on pasta. If you look at the segmented disclosure, the revenue looks a little low there. I'm hoping you can talk to that, how the pasta business performed in the quarter, maybe give us a sense for how much of the EBITDA contributed in the quarter.

MURAD AL-KATIB:
Yes, a couple of things, Christine; I guess for the benefit of everybody on the call, I have to say I'm in Turkey. So I haven't seen the segment as detailed as I usually do.

But we actually are going to be filing out a clarification. I'm not sure how we're going to do that yet, but we will do that. For the follow-up on this call, we'll be clarifying.

The pasta that was sold from Turk Pulse -- we have the three companies in Turkey. So we have Arbel, Turk Pulse and Durum, which is the Arbella company. But for the exports side, we do use Turk Pulse to do a number of the export market sales of pasta. Those were on a clerical error inadvertently lumped in with pulses.

CHRISTINE HEALY:
Oh.

MURAD AL-KATIB:
So because they were a TurkPulse sale they were lumped into that category. So, actually, the pasta, semolina and bulgur sales were, I believe -- Lori, you could help me out with this -- but it was about $6.2 million higher than what the segmented note says.

LORI IRELAND:
Yes, that's right.

MURAD AL-KATIB:
Is it $6.2 million? You could just clarify that number.

LORI IRELAND:
Just over $6 million Canadian, maybe lower for quarter one, higher for quarter two.

MURAD AL-KATIB:
Yes, so it was just a classification error. So we'll sort out with our advisors as to what the best way to get that information widely distributed. But so to clarify, Christine, it says $3 million. It's actually about $9 million.

So if we look at it, the pasta fundamentals continue strong. I just spend the last week, actually, at Arbel going through each one of the operations. We ended up crossing 50 countries of export in Arbella. The margin profile continues as we projected, and it is the business unit in Turkey that is absolutely on track eight months post-acquisition, or nine months post-acquisition.

So I'm very pleased with the development. Definitely, without the pasta side, the results wouldn't have been $4.7 million adjusted EBITDA. So it was a very significant contributor to that.

CHRISTINE HEALY:
Okay, and what's the status of selling Arbella in Canadian stores?

MURAD AL-KATIB:
Well, I can tell you that there's Arbella on a ship somewhere on its way to Canada. So we'll be doing the launch out in Canada in the very near term. So I would expect that in the next 30 to 45 days you'll start to see it in GTA, Quebec. That's the first launch. It'll be an Ontario, Quebec launch to start.

We'll take a real managed approach on it. I mean, for us, Canada is a pride thing, too. But at the same time, I'm all about making margin. So we want to do a managed launch, make sure we get into the right retail and start a long-term strategy.

CHRISTINE HEALY:
Okay, and then moving onto deployment of cash because I'm sure a lot of people are looking for some information on this, if the pasta facilities are running at 80% or so capacity, what is the timing of adding a new line?

Also, on the rice, you've talked previously that this is doing well as a core growth area. So when can we see some expansion on that business segment?

MURAD AL-KATIB:
Yes, I mean, definitely. The deployment of capital is high on everyone's mind. Those of you that have had the opportunity to get to know me recognize a couple of things; I don't overpay for businesses.

So we're going through make versus buy decisions. I would expect within the short term we're going to have those worked out, and you're going to see deployment of capital starting here early in the fall.

So the pasta side, I mean, definitely. You see, the way, just to clarify, the way the pasta business works is we added in September, October of 2009 a long-cut pasta line; so long-cut meaning spaghetti, linguini, fettuccini.

When you give those products to export markets, it creates demand for the short-cut varieties. So a retailer in Israel, for instance, or a retailer in Japan who take the spaghetti says this is selling well. Now I want penne, rigatoni, and I want elbows.

So each line type creates the demand for the next line. So the examination now is to continue down the path of adding more short-cut capacity to go along with the long-cut capacity we had last year.

The Arbella story is build out capacity, build out sales, build out margin. You're not going to see us in the near term going out and doing large third-party acquisitions on the pasta side focused outside of Turkey because Turkey is really our focus on the brand side in terms of what we've developed for brand. The rest of it is a focus on distribution, retail and quality and price advantage on the export market.

On the rice side, Christine, the leased rice mill continues to run. You can see from the segment that it is contributing.

But, really, the real margin comes from owning your own rice mill and buying patty rice directly from farmers and transforming patty rice into brown rice, brown rice into white rice, use color sorting, polishing, packaging and retail distribution to capture the margin directly from the rice farmer, directly to the retail markets in the region that consumes medium-grain rice.

So you'll see movement on that initiative coming up in the coming months as well.

CHRISTINE HEALY:
In the coming months? Okay. You just gave away something there. Your exclusive rights product, you guys talk about this all the time, the B90 chickpea, Skyline navy beans --.

MURAD AL-KATIB:
Yes.

CHRISTINE HEALY:
Can you give us some kind of sense on when we can see the full benefit of this in your earnings and maybe some idea as to what the impact could be, how much material this could be for your facilities?

MURAD AL-KATIB:
Yes, I mean, it's interesting. The two major varieties that we're really going to see the benefits of in this crop year are the B90 chickpea, which is a seven-millimeter chickpea that is actually aimed at the hummus markets on the grinding side and also on the canning side for Europe.

So let's say in the Italian market the B90 is actually a preferred canning chickpea because it starts as a seven-millimeter, but after it's hydrated, it becomes a nine-millimeter. So they really like the hydration properties of this particular chickpea.

So the exclusive world-wide commercialization rights for North American production started in earnest for this crop year. So we ended up on a closed-loop production system with growers throughout Saskatchewan and North Dakota. I think we have some in Eastern Montana as well. That product should be harvested starting end of August, early September. We'll start to see those running through our plants.

The B90 is a significant program. It will be one of the drivers that is forecast to take Alliance to become the largest, or certainly one of the two largest. I think we will be the largest in the world in chickpea export in 2010, 2011.

So this will be a part of the smoothing the seasonality game. I mean, we've spent a lot of time talking about beans. But chickpeas as well have the potential for us to grow to well over a 100,000-ton program throughout Canada, US, Australia and Turkey. We're also continuing to become active in the Turkish chickpea markets to drive the utilization and capacity at Arbel.

So that's one of the big programs of the B90. The other is the King Red Lentil. The King Red Lentil is being billed as the boldest, largest red-split lentil in the world. That's a branding initiative we started about two years ago.

This is the first year of commercial production of the King Red, and we'll have somewhere in the range of about 25,000 tons or so to sell in the world, or maybe a bit more. That's going to be a very significant branding program for us.

It basically takes production. It closes the loop, makes farmers grow, deliver it back to us. We can brand and extract a premium as we market throughout the world.

CHRISTINE HEALY:
Okay, that's great. That's it for me. Thanks, Murad.

MURAD AL-KATIB:
Thanks, Christine.

OPERATOR:
Next question is from David Pupo of Macquarie. Please go ahead.

DAVID PUPO:
Hi, Murad.

MURAD AL-KATIB:
Hey there. How are you, buddy?

DAVID PUPO:
I'm good, you?

MURAD AL-KATIB:
I'm all right.

DAVID PUPO:
Let's go back and beat the horse on Europe, Middle East and North Africa, the difference and the sequential drop of second quarter from the first quarter. What I'm wondering about is how you're so confident given the fact that you're not talking incredibly positive on third quarter.

The first quarter was so large. How do you know that that product has been sold through to the end-user and it's not going to be there through the third quarter, through the fourth quarter and your whole year turns out to be less satisfactory than expected?

MURAD AL-KATIB:
Well, there's a couple of things, David. I mean, remember, as I said earlier on, we're not just a sales company. We're not just a trading co that relies on information that comes from the market. We have distribution on the ground in key consumption markets.

Remember, this is part of what we've been saying the last few conference calls. We're running distribution in Egypt now. We're running distribution in Turkey with the Arbel acquisition. We're running distribution in the India subcontinent in terms of warehousing distribution. We have our key buyers on the ground.

So we have a very good sense of what the stock that's moving through the country, what's coming in, what's being imported, what's being consumed. All of that factors into the decisions.

I can tell you that one of the key demand factors for us and why I feel that the outlook on the demand is going to be kick-started is stocks were limited to begin with and we now have Ramadan and we're right in the middle of it. Ramadan and the holy month of Ramadan, people think of it as a fasting period but don't recognize the consumption of these items that actually do take place after people break fast.

So from that perspective, we're seeing very significant move in the market in products. So we're very confident that stocks are dwindling and that they will be replenished.

If I made the sense that Q3 was not going to be a satisfactory quarter, I want to reiterate one thing. Turkey's utilization is running well. So we didn't have product in Q2 in Turkey.

So remember, the crop in Turkey doesn't get harvested until around the 10th or the 15th of June. So by the time we receive product in any volume in processes, we have maybe five to seven days of the quarter that actually take into account Turkish new crop.

So Turkey is running, and, frankly, even the first dribs and drabs of Canadian product has started to arrive. But we expect within the next one week to 10 days, North Dakota, Eastern Montana will start, and within the next 10 days to 14 days, Saskatchewan will begin in earnest. So we do have very large capacity that we can fill in the late August, September periods to deliver results for this quarter.

So I am optimistic. I mean, I think for us its supply; it's demand. It's there. Of course, the crop's not in the bin. I mean, we still have in any ag business weather risk until harvest completes. So we'll keep our eye on late August frost and those kinds of things. But assuming normal weather, things look okay.

DAVID PUPO:
Okay, so looking back --.

MURAD AL-KATIB:
Now, David, just remind me of -- because your question was kind of a complex one. So what else do you want me to talk about?

DAVID PUPO:
I'm trying to look back at the first quarter and use history because you're still a new company and your growth trajectory is so aggressive. I'm trying to use the difference, the delta, between the second quarter and the first quarter in the Europe, Middle East and North Africa and try to determine if you looked back at the first quarter what drove that quarter to be so big.

What types of information, data, etcetera, can we use to be modeling fourth quarter, first quarter of next year and third quarter of the year beyond? I'm not asking you to build my model. I'm trying to understand the nuances of this business that seem to be huge fluctuations from quarter to quarter as we've seen you grow into a larger company.

MURAD AL-KATIB:
Yes. I mean, there's a couple of things; I don't think you can take the Q2 fluctuation in earnings that you saw and equate that to a normal scenario. I mean, we have not had a volatile commodity. Pulses have been, very relatively speaking, a very stable commodity over the past 10 years.

So when you look at a historically high price adjusting and you look at a complete crop failure in 2007 in Turkey with only 68,000 or 70,000 tons of production, recovering up to 280,000, and this year the US Ag attaché, this last week released his estimate of 510,000 tons of lentils in Turkey, so you can see a progression from 70,000 to 270,000 to 510,000. I mean, this is not normal supply.

So when you end up in a position where all of those things corrected themselves in one quarter, it just continued to freeze everybody.

DAVID PUPO:
Okay.

MURAD AL-KATIB:
So I don't think that you will see that type of volatility. I don't think there was anything extraordinary in quarter one that drove demand beyond what was normal. We have to recognize it's a staple protein consumption that's growing around the world and Alliance's huge results. We're driven by the fact that we've become a multi-origin, diversified company in our space.

DAVID PUPO:
Okay, so you just --.

MURAD AL-KATIB:
We have market reach, David, that no one else has in our business.

DAVID PUPO:
Yes. So okay. So you made a very important point. You do not see the first quarter as, let's call it for lack of better terminology, channel stuffing.

MURAD AL-KATIB:
No, definitely not. That's why your comment of why do I feel like that stock will stay around; David, the stocks are -- overall, the large consumption markets are relatively empty. So we don't have a channel that's stuffed full. We saw no demand that it's going to continue.

DAVID PUPO:
Okay.

MURAD AL-KATIB:
So that's definitely not the case. At least that's our opinion. I mean, we can't get into every importer's warehouse and tell you what's in there. But we can get into the major importers because they're all our customers. So, yes, I definitely don't feel this quarter one is an aberration

DAVID PUPO:
Okay, great answer. Thanks very much.

OPERATOR:
Next question is from Anoop Prihar of GMP Securities. Please go ahead.

ANOOP PRIHAR:
Good afternoon. This is --.

MURAD AL-KATIB:
Hey, Anoop. How are you?

ANOOP PRIHAR:
Good, thanks. Just a couple of questions; first, coming back to the pasta of business, even after we adjust for the restatement, if you will, it looks like the revenues there this quarter were $9 million versus, call it, $18 million in Q1.

So I believe earlier in the call you characterized the pasta business as being strong. But I look at this and your revenues are down quite materially on a sequential basis. So on what basis do you characterize that as being strong?

MURAD AL-KATIB:
Well, we have a couple of things. I mean, there is some seasonality in the pasta business. So we see that in the quarter two period where we're transitioning from cooler weather to warmer weather. So we saw a bit of that.

But, basically, when I look at -- for me, the characterization of the pasta business as strong is that we continue to make our advances in the distribution. We are continuing to drive our utilization. We were at a level, Anoop, in the second quarter where we had actually, as a result of strong business in the first quarter -- I can tell you that our warehouses and everything were empty.

So we ended up in a second quarter in a position where we met sales. We were also able to replenish our stocks to get ready for fall season again. So I think that, ultimately, when I look at the sales forecast going forward, I do characterize it as strong.

ANOOP PRIHAR:
My understanding of the pasta business was that it was materially less sensitive than the lentil business. That was one of the primary benefits to your platform was that it softened the shoulders.

MURAD AL-KATIB:
It definitely does. Again, when I look at it, as I said, it delivered consistent earnings this quarter. As we grow the volume in the pasta side, it provides us with shoulders to get us through times when the pulse business is less so. So, ultimately, when I look at the pasta business, I still foresee significant growth.

ANOOP PRIHAR:
I look at the crop forecast for this year, and I guess for Canadian lentils the forecast is something in the neighborhood of 1.6 million, 1.7 million tons. So I'm just curious. Can you give us a sense of what you think the on-farm storage is in Canada capacity-wise?

MURAD AL-KATIB:
You're just talking about the raw on-farm storage?

ANOOP PRIHAR:
Yes.

MURAD AL-KATIB:
Gaetan, do you want to take a run at that one? I could try too. But, I mean, it's just really, Anoop, but it's really just a guess.

GAETAN BOURASSA:
Yes, I mean, a common number that people throw out is a year-and-a-half storage, I think, so.

ANOOP PRIHAR:
1.5 years of storage?

MURAD AL-KATIB:
Yes, 1.5. I was going to use the same one. But it's anecdotal, I mean.

ANOOP PRIHAR:
That's fine.

MURAD AL-KATIB:
So we always kind of say that in normal yields we can store a year and a half of total production.

ANOOP PRIHAR:
Okay, all right. Then just coming back to Turkey for a second, I mean, you said the crop came off in mid-June. Did you see a marked increase in activity there then in July and August?

MURAD AL-KATIB:
Sorry, a market decrease did you say?

ANOOP PRIHAR:
Increase. Did you see a big --?

MURAD AL-KATIB:
Oh, yes, of course. I was going to say no, not a market decrease.

ANOOP PRIHAR:
Can you give us a sense of --?

MURAD AL-KATIB:
Yes, a market increase in activity, I mean there -- I can tell you I've had the benefit of spending the last week in Mersin, and it's happily a hive of activity.

ANOOP PRIHAR:
Okay. Would it be fair to say that the capacity utilization there is somewhere in the 70%, 80% range right now?

MURAD AL-KATIB:
You know what, Anoop? It's too early to tell. I can tell you that we continue to look at building out sales opportunities.

I will tell you one thing that's important in Turkey is to build out everything else beyond lentils. So the pasta is taking care of itself. We're building out the bulgur utilization because we have huge bulgur capacity that's not being utilized today.

So we're building that out. Chickpeas and beans, we want that line not to be running just with lentils. We want it to be running with chickpeas and beans. That all contributes to this moving of the seasonality of the business.

So the boosting of utilization at Arbel to go from -- I think we used the estimation of 18% utilization last year with the crop problems, and then it boosted up to maybe 50% last year in the fall period because of a Canadian crop. We're targeting to get to utilization of where Canada, US and Australia are. That's the work in progress.

ANOOP PRIHAR:
Do you still think it's reasonable then to assume utilizations on a full-year basis after it's all said and done of getting up into that high 60% range, which I think is what we've spoken about in the past as being a target?

MURAD AL-KATIB:
Well, I know pasta will be higher than that. Did you just say pasta? I'm sorry. Your voice kind of cut out there.

ANOOP PRIHAR:
I guess I'm talking about the consolidated entity.

MURAD AL-KATIB:
Yes, the consolidated entity, yes, our target would be to try and get that to the high 50s, 60s utilization.

ANOOP PRIHAR:
Okay, thanks.

MURAD AL-KATIB:
Sorry. Turkey, right?

ANOOP PRIHAR:
Well, when we talk about, I think it was 65%, 60%. I beg your pardon, 65%, 67% utilization. I think we're talking about all facilities. Are we not?

MURAD AL-KATIB:
Well, we were saying that our utilization was running around that in Canada, US, Australia and that in Turkey it was slightly lower. We were working towards making sure that the group utilization was around that level, yes.

ANOOP PRIHAR:
Right, okay. Thanks.

MURAD AL-KATIB:
Sorry, you confused me a bit with the Turkey versus consolidated. I was just a little bit confused.

OPERATOR:
The next question comes from Sandy El Baroudi, a private investor. Please go ahead.

SANDY EL BAROUDI:
Could you just comment on these exchange rate changes, please?

MURAD AL-KATIB:
Yes, Sandy. You know what? In both GAAP reporting and in IFRS, in the International Financial Reporting Standards, we have to do a snapshot of our foreign exchange position. So, Lori, I think it's just best. Do you want to give Sandy a real layman's, for all of us laymen, a view of the foreign exchange losses?

LORI IRELAND:
Sure. So at each reporting period, Alliance has a number of outstanding foreign exchange contracts that we book through banks to hedge our foreign currency risk.

What we have to do at each reporting period is we have to take our outstanding book of contracts and the average rate on those contracts. Then we have to say, okay, on June 30, if we had to execute all those contracts, how much would the US dollar cost us to purchase in Canadian dollars?

What had happened is our average foreign exchange rates on the open contracts was around 103 to the US. The spot rate on June 30 was more in the range of 105. So we have a snapshot unrealized loss on those contracts.

In addition, we have to take all of our outstanding US loans both in Turkey and Canada as well as in Australia. We also have to compare those to the local currency and take a snapshot of those as well.

So it's an entry that's done each quarter, and it's recalculated every quarter. It's required for reporting, and it does tend to go back and forth quite a bit because the dollar fluctuates so much.

MURAD AL-KATIB:
Sandy, I think that there's one thing I want to add to that. This is a non-cash effect. This is why we, as the analysts that cover Alliance, look at adjusted EBITDA, adjusted net income.
For all of our investors, we've started to list the EBITDA, the foreign exchange gain or loss and the adjusted EBITDA afterwards, because, realistically, when you're looking at the earnings of the Company, these are not cash items. They're not actual losses or actual gains. They're only for reporting purposes. That's why they need to be backed out.

SANDY EL BAROUDI:
Thank you very much.

MURAD AL-KATIB:
You're welcome, Sandy.

OPERATOR:
We have a follow-up question from Marc Robinson of Cormark Securities. Please go ahead.

MARC ROBINSON:
Hey.

MURAD AL-KATIB:
Hi, Marc.

MARC ROBINSON:
A quick question; can you give us a sense of what your net long exposure was to any of these commodities through the quarter, if any?

MURAD AL-KATIB:
You're talking about like just basically any net exposure to any of which of the commodities that we hold?

MARC ROBINSON:
Yes, exactly, so where you've bought something --.

MURAD AL-KATIB:
Marc, let me tell you. We always say we have very little effect of changes in the commodity price to our net profit or loss. The only change in that is product that we ship from Canada, US or Australia into Turkey for processing.

So I can tell you that there were not very significant amounts. There may have been some long positions of lentils that had been shipped very late in quarter one that would have arrived in quarter two and then part of the adjustment in commodity price in Turkey. Outside of that, I wouldn't consider there to be major effects.

MARC ROBINSON:
Okay. So the --.

MURAD AL-KATIB:
I mean, green lentils, chickpeas, the other ones, we run a very tight commodity position. But let me not be clear. We do have commodity risk in this business as we do in any business. We attempt to mitigate that by limiting any material long and short positions.

Marc, you know the fundamentals of our business. You've now even had a chance to visit all of our factory or many of our locations in the world. We fundamentally buy products from farmers, drive them through our facilities and sell them to our customers. We don't store product to benefit, and I'm glad we didn't because the commodity prices adjusted downwards pretty materially.

MARC ROBINSON:
Right, and that's --.

MURAD AL-KATIB:
Did it have any effect on the quarter? Yes, definitely. It had small effects. It made a difficult situation slightly worse.

MARC ROBINSON:
Okay.

MURAD AL-KATIB:
But it wasn't in big material losses.

MARC ROBINSON:
Okay, and so Anoop asked about the sort of targets of capacity utilization. I don't think you've answered it. Can you tell us what the utilization was approximately this quarter?

MURAD AL-KATIB:
Quarter two, I mean, quarter two is -- utilization-wise, I mean, listen, guys. The utilization is utilization in our core business, okay? This quarter demonstrates that I can deliver revenue any time. We have marketing strength that no other company has in our business. But I don't care about revenue. I care about margin.

So, yes, we had to utilize our factories because we had to pay our bills. Remember, for those of you who have gotten to know me, I view the fact that I have to pay the bills with your money and with my money. We have to pay the bills.

So utilization was actually higher than I would have liked this quarter because we drove business through that was not in our traditional margin profile. But we did it in order to pay bills.

MARC ROBINSON:
Okay, so --.

MURAD AL-KATIB:
So from that perspective -- what's that?

MARC ROBINSON:
I was going to say for me to get a sense of how low that margin per ton actually went, it's helpful to get the utilization number so you can figure out what that implied margin per ton is.

MURAD AL-KATIB:
Yes, I mean, Gaetan, it was $149 million of sales. Gaetan, do you have any comments on how utilization was this quarter versus last?

GAETAN BOURASSA:
I would say, what did we run, probably about 60%.

MARC ROBINSON:
Okay, and that's system-wide?

MURAD AL-KATIB:
Yes.

MARC ROBINSON:
Was Finora not open at all this quarter?

MURAD AL-KATIB:
The Wilkie plant shut down -- was it last week of April, Gaetan?

GAETAN BOURASSA:
That's right.

MURAD AL-KATIB:
Yes, it shut down the last week of April. We're doing a complete upgrade adding three Z4 plus color sorting lines. That facility is, by far, it's become one of the crown jewels in the Alliance repertoire. When we're done with it, it's going to reopen on the, what, 23rd, 24th of August I think. So it's a lean, mean fighting machine, Marc. It's ready to roll now.

MARC ROBINSON:
That's 60% --.

MURAD AL-KATIB:
So the largest plant with largely out of our location for the quarter.

MARC ROBINSON:
That 60% utilization is including or excluding Finora as part --?

MURAD AL-KATIB:
It would be excluding.

MARC ROBINSON:
Okay.

MURAD AL-KATIB:
That plant and the Rosetown plant were actually decommissioned for most of the quarter.

MARC ROBINSON:
Okay, that's good.

MURAD AL-KATIB:
Decommissioned, now just to clarify; decommissioned undergoing planned capital expansions to be ready for a very large new crop.

MARC ROBINSON:
Yes, okay.

MURAD AL-KATIB:
So, not decommissioned as in not coming back on line, they're on line and ready for the new crop.

MARC ROBINSON:
Okay, thank you.

MURAD AL-KATIB:
Omer, do we have anything more queued up there or?

OMER AL-KATIB:
Yes. I think, Joe, were you announcing the next caller?

OPERATOR:
The next question is from Steve Anderson of Venator Capital Management. Please go ahead.

STEVE ANDERSON:
Hey, Murad.

MURAD AL-KATIB:
Hey, Steve. How are you, buddy?

STEVE ANDERSON:
I'm good. I'm just trying to follow up on Anoop's question a little bit and understand more of what happens in Europe, Middle East, North Africa. Did you say it went from $130 million last quarter to $18 million in sales this quarter in that region?

MURAD AL-KATIB:
Yes.

STEVE ANDERSON:
So does that mean that these guys fill the bins up going into the first quarter, run them down, run them dry -- and you're saying they're pretty dry right now -- and then fill them up again all the way? How does it work, typically?

MURAD AL-KATIB:
I mean, ultimately, you have to understand. These are widely consumed items where there is a --.

(Multiple speakers)

STEVE ANDERSON:
-- right?

MURAD AL-KATIB:
What's that?

STEVE ANDERSON:
Consumption patterns aren't going down.

MURAD AL-KATIB:
No, definitely not. In fact, we're seeing now -- the other thing we've got to factor into this whole equation for going forward is, remember, the adjustment in price downwards was one of the factors that paralyzed demand because of the fear of loss. But the adjustment of prices downward stimulates consumption.

So on a catch-up basis, consumption is actually stimulated by lower prices. So from that perspective, we have an empty pipeline and a demand profile that looks even stronger.

STEVE ANDERSON:
So you're sitting with these bins empty as far as you're concerned through Middle East, North Africa, right?

MURAD AL-KATIB:
We're tapping them and we're hearing hollow sounds, Steve. That's our view today.

STEVE ANDERSON:
So does that mean these guys have to come to the spot market there by pushing up prices, increasing your margins for the next little while? Like is there a rush buy for them through Ramadan? Is that what you're saying?

MURAD AL-KATIB:
No, Ramadan is pretty much covered. I mean, we're already almost into the first week.

STEVE ANDERSON:
Yes.

MURAD AL-KATIB:
But what I'm saying is we're feeling the inquiries coming because they didn't buy. So what they bought was a hand-them-out buy. They drew down stocks, and we think they'll have to replenish.

When they replenish, remember, we've got transit time issues from Canada, too, where it takes 45 days to get to market. But Turkey is right on the doorstep. We've got a very big capacity ready to rock and roll here, too.

STEVE ANDERSON:
Yes, and when they replenish, they replenish typically all the way? Or how does that work? Is it --?

MURAD AL-KATIB:
Remember, you can only postpone consumption so long because these are not luxury items. These are need-to-have commodities. When you get to a point where in the market there's no stocks, they need to replenish and they can't and they'll do it over time, they have to do it right away.

So this is where we're saying that with available supplies, online in Turkey and big crops coming and capacity ready, we feel that demand fundamentals in the Middle East, North Africa and, of course, the India subcontinent are going to continue strong throughout quarter three, quarter four, quarter one.

STEVE ANDERSON:
So forgive me if I'm wrong here. But it looks like when you have these guys fill out their bins they've got about two quarters of supply in market in country, right? Then, typically, they would buy partway through a quarter and replenish a portion of that, and they just chose not to this time. So it's not really channel stuffing. It's more --.

MURAD AL-KATIB:
Well, just there's another factor here, too. Remember, winter consumption is the predominant consumption, right?

STEVE ANDERSON:
Okay.

MURAD AL-KATIB:
So you just came through the period where if you look at weather patterns in this region, I can tell you that today in the little city that I'm in, in Turkey the temperature was 38 degrees Celsius.

STEVE ANDERSON:
Yes.

MURAD AL-KATIB:
Okay? But we're getting into the consumption season. So in addition to the fact that they drew down stocks and the seasonality of the business, they're coming into the peak consumption period again.

STEVE ANDERSON:
Do they typically look to -- like, should we be looking for that one 30-day, $18 million delta the opposite way this quarter? Or is that too much to look for?

MURAD AL-KATIB:
You know what? I can't be that specific. I can't say because we're only one player in it, right? We happen to be the largest. But, certainly, as our sales go, I can tell you that our regional competitors weren't busy during this period. So, yes, we should see some changes to reflect the delta, as you called it.

STEVE ANDERSON:
Okay, great. Thanks a lot.

MURAD AL-KATIB:
Thanks, Steve.

OPERATOR:
The next question is a follow-up from Robert Winslow of Wellington West Capital Markets. Please go ahead.

ROBERT WINSLOW:
Yes, in the MD&A Murad, you mentioned what's happening in India. I'm wondering. There's some severe weather, has been some severe weather in Pakistan. I'm wondering if that has any effect from both the supply, primarily from the supply side. I'm trying to go from memory here that weather or not Pakistan is a big player producer in the pulse side.

MURAD AL-KATIB:
Gaetan, can you take a run at that first and then I'll add?

GAETAN BOURASSA:
Yes, sure can. We're starting to feel a little bit of follow-up from Pakistan where they're coming into the market looking for the early shipment slot. There's been some emergency aid announced.

In the normal year, they'll take about 50,000 ton of red lentils from Canada. So we think there's a good chance that'll move up this season. On the chickpea side, definitely the numbers should move up with -- and there's some problems in Turkey and India as market is moving up as well. Canada should be in good position with its smaller crop to take some more of that to chickpea market as well.

MURAD AL-KATIB:
Robert, I'll follow on in your India comment. I mean, the severe weather that we saw in Pakistan on the flood side, there are reports of shorter monsoon rains this year in India.

So, again, how that will all play out of their supply of their main pulses harvest in -- so lentil harvest there is in March. So it's still a long ways away. But we're forecasting strong demand fundamentals.

I mean, the India subcontinent in general, the demand supply gap is widening. This is all part of a very strong focus of ours into that region. Even in some of our public disclosures, you've seen us be very direct about further expansion in the India subcontinent both on warehousing distribution and local processing because we believe that this is not a temporary phenomenon. This is one that is going to be continuing for years and years to come.

ROBERT WINSLOW:
Great, thank you.

OPERATOR:
We have a follow-up question from Anoop Prihar of GMP Securities. Please go ahead.

ANOOP PRIHAR:
Just a quick follow-up; in Q1 -- sorry, beg your pardon -- in Q2, we talk about the revenues being impacted by greater proportion of lower margin product being sold primarily peas. I'm wondering. In addition to the peas, were there any canary seed or mustard or anything else in there that brought that mix down? Or was it primarily just peas?

MURAD AL-KATIB:
Gaetan. Gaetan, are you there?

GAETAN BOURASSA:
Yes, I missed the question.

MURAD AL-KATIB:
Okay, Anoop, can you repeat that question for us, please?

ANOOP PRIHAR:
Certainly. I was just trying to understand a little more. In talking about the Q2 results, we said that the results were impacted by a higher proportion of lower-margin business, which was

primarily peas. I was wondering if, in addition to peas, is there any other lower-margin product, canary seed or mustard or anything along those lines, that was part of the mix? Or was it just peas?

GAETAN BOURASSA:
Yes, we dabble a little bit of course, always in canary seed. The thing about field peas, when you jump into a container the way we are, 85% of the world peas would move to bulk markets via bulk vessel. So it's very competitive. So the fact that we did it all in containers and managed to get by this quarter is remarkable, in my opinion.

ANOOP PRIHAR:
Could you --?

MURAD AL-KATIB:
Anoop, the other thing I should say is there was some business. Like one of the things that now that we should point out is there was a very large rice tender that we participated in as well. That rice tender was somewhere in the range of about $16 million, $17 million. That was for the Turkish government, so with Egyptian rice into the Turkish government.

That was just merely Egyptian rice processed, traded to the Turkish government. So that wouldn't have been running through any of our plants at all. So that would be one aberration that would have brought our sales figure up. That wouldn't be at a processing margin. It would have been just a trading margin.

ANOOP PRIHAR:
So can you just give us a sense in Q2 the percentage of revenue that would have come from peas versus what it would have been in Q1?

MURAD AL-KATIB:
I would venture to guess. If you look at the segmented revenue geography note that I mentioned earlier, out of the large proportion of the Asian business, I would say 80% of that is peas and the first quarter you would have had negligible peas. You would have had maybe 5%.

This was a big pea quarter because it was available stock. See, when you're having widespread rain and you can't get the limited lentil stocks off farm and you want to get them into your plants to process them, you turn to what you can get. Peas were readily available.

So we turned to peas. We drove our utilization. We got some stuff out and generated some margin.

ANOOP PRIHAR:
Okay.

OMER AL-KATIB:
That brings us to the end of our questions. I'd like to thank you all for joining us today. I would like to remind everyone still on the call that if you have any follow-up questions you can feel free to contact us at our Regina head office. We'd be more than happy to follow up with you.

Again, I'd like to thank you all for attending our conference call. Have a good day.

OPERATOR:
Ladies and gentlemen, this concludes today's conference call. You may disconnect your lines. Thank you for participating and have a pleasant day.