 <b>PHILIPPINE RATING SERVICES CORPORATION</b>	CREDIT RATING REPORT
	D&L INDUSTRIES, INC.

**Date:** April 29, 2024  
**Analyst:** Joan Grace P. Bual

5<sup>th</sup> Floor, ALGO Center  
162 LP Leviste St., Salcedo Village  
Makati City, Metro Manila  
1227 Philippines

+632 8812 3210  
+632 8812 3215  
www.philratings.com.ph

### MONITORING OF ISSUE CREDIT RATING

Amount	Interest Rate	Maturity (Tenor)	Outstanding Rating and Outlook	Assigned Rating and Outlook
P3.0 billion	2.7885%	September 14, 2024 (3 years)	PRS Aaa Stable Outlook	PRS Aaa Stable Outlook
P2.0 billion	3.5962%	September 14, 2026 (5 years)		
<b>Total Outstanding Bonds - P5.0 billion</b>				

**Use of Proceeds:** Primarily financed the Company's expansion plans in Batangas which involved a total estimated capital expenditure (capex) of P10.2 billion and the corresponding working capital requirements.

Obligations rated **PRS Aaa** are of the highest quality with minimal credit risk. The obligor's capacity to meet its financial commitment on the obligation is extremely strong. **PRS Aaa** is the highest rating assigned by PhilRatings.

An Outlook is an indication as to the possible direction of any rating change within a one-year period and serves as a further refinement to the assigned credit rating for the guidance of investors, regulators and the general public. A **Stable Outlook** is assigned when a rating is likely to be maintained or to remain unchanged in the next 12 months.

### RATING RATIONALE

#### 1. Strong market position in the industries that it is engaged in

D&L Industries, Inc. (D&L, the Company) is engaged in product customization and specialization in four principal business segments — Food Ingredients, Oleochemicals and Other Specialty Chemicals, Specialty Plastics, and Consumer Products Original Design Manufacturer (ODM). The Company was incorporated in 1971 and is a pioneer in many of the industries it is operating in. D&L has established itself as a dominant player across markets. According to management, D&L has since remained a market leader or a close second in these industries.

The Company sustained its domestic operations and major expansion plans amid the onset of the pandemic and related challenges. Despite some delays in relation to its project timeline, D&L announced in July 2023 the official commencement of commercial operations of its Batangas expansion facility. The added capabilities from the Batangas facility are expected to support the Company's goal of expanding its export business, as well as the production of higher value-added products.

As the economy continues to recover from the pandemic, D&L is positive that it is more capable to withstand adverse environments with the expertise it has learned through its years of operations. D&L strives to enhance its capabilities in order to maintain a strong market position. The Company is optimistic given the continued strong demand for its products as these mainly cater to essential industries and basic materials.

## **2. Diversification of products offered and markets served**

There is a wide range of product applications under each of D&L's four business segments. These products cater to numerous needs in various industries and are offered to customers belonging to different market segments. Moreover, D&L is able to service both the specialized and more basic products that broaden its presence in different consumer markets.

D&L's diversified business segments and product offerings may balance varying developments in the different industries it serves. This was made evident during the COVID-19 pandemic, as the Company's commodity products performed well and which partly offset the decline in demand for more specialized products. Consumer demand likewise increased for general sanitation and hygiene products, as well as plastic packaging materials. On the other hand, demand weakened in the food ingredients segment as operations of several food establishments were limited. As the economy reopens, greater consumer demand for more discretionary products is already being observed and revenues in business segments are normalizing.

The Company's revenue sources were also geographically diverse, as D&L derived a sizeable portion of its revenues from exports. In 2022, exports grew by 33.3% and accounted for around 31% of total revenues. In 2023, export contribution went down to 27%, on account of the high volume of export orders from earlier periods, as well as the lingering effects of high inflation which moderated demand. Nonetheless, D&L is positive that export contribution will increase moving forward, with the commencement of the Batangas facility that will mainly cater to the Company's export business.

## **3. Innovation-driven specialty products protect the Company from keen competition and ensure continued demand from customers**

D&L categorizes its products into two segments: Commodity and High Margin Specialty Products (HMSP). The Commodity segment includes products that are more basic and less specialized, while under the HMSP segment are products that are customized according to the customers' needs. The higher the level of customization involved, the higher the profit margin for the Company. Technical research and development (R&D) is necessary to produce specialized products according to client needs. Moreover, there is constant development in industries that influence the needs and demand of the market. For these reasons, D&L largely invests in creating strong R&D capabilities to offer quality HMSPs and to keep up with the evolving demand of consumers.

In 2023, total revenues consisted of 38% commodities and 62% HMSPs. This level was similar to the Company's pre-pandemic revenue mix. Given the technicalities of producing HMSPs, clients tend to conduct business with the same suppliers. D&L capitalizes on its longstanding relationship with its clients, which it has built over many years. Management elaborated that although the Company's products may form only a small part of what the clients make, these products are vital to the clients' brand and end-product. Hence, the R&D-driven nature of the products being manufactured has limited the entry of new market players while also ensuring continued demand for the products of the Company.

#### **4. Relatively stable margins amid higher cost and expenses, including incremental costs related to the Batangas expansion facility**

In 2022, D&L's total revenues rose by 40.9% to P43.5 billion, on account of higher sales volume coupled with higher average selling prices. Gross profit margin, however, nominally dropped to 14.0%, compared with 14.8% in 2021, with the slightly faster increase in cost of sales and services. Nevertheless, gross profit in 2022 was higher by 32.9% to P6.1 billion, mainly supported by growth in sales volume.

Operating expenses increased by 44.2% in 2022. Higher delivery charges drove the 34.3% increase in selling and marketing expenses. Moreover, general and administrative expense jumped by 81.1% due to higher depreciation and amortization expense and provision for impairment of receivables. Finance costs were also higher by 66.7%, driven by greater debt levels and higher average interest rates. On the flipside, net other income more than doubled on the back of recognized foreign exchange gains for the year.

Net income in 2022 went up by 25.5% to P3.3 billion, mainly supported by higher revenues. Albeit, net profit margin slipped to 7.6% in 2022, compared with 8.6% in 2021, due to heightened costs and expenses.

In 2023, total revenues went down by 23.0% to P33.5 billion on account of the challenging business environment with the lingering effects of high inflation. On the other hand, cost of sales and services posted a larger decline of 25.7%, in line with the normalization of commodity prices. These resulted in an improved gross profit margin of 17.1%, compared with 14.0% in 2022.

While the third quarter of 2023 (3Q 2023) marked the commercial operations of the Batangas plant, it also included the incremental expenses related to the completion of the facility. Operating expenses and finance cost went up by 19.9% and 159.7%, respectively. Given the foregoing, net income in 2023 was down by 30.8% to P2.3 billion. Net profit margin was 6.9%, lower than 7.6% in 2022. D&L pointed out, however, that excluding incremental expenses related to the Batangas plant, net income amounted to P3.0 billion, lower by only 15.3%, compared with P3.5 billion in 2022. Recomputed net profit margin will amount to 9.0% in 2023, higher than 8.2% in 2022.

#### **5. Conservative debt management and adequate cash flow generation**

D&L maintained conservative debt levels as of end-2023. Total debt stood at P17.1 billion as of end-2023, up by 10.7% from P15.5 billion as of end-2022, due to additional borrowings. On the other hand, stockholders' equity was relatively flat at P20.9 billion, from P20.7 billion as of end-2022, with minimal movements in retained earnings. As a result of the foregoing, the Company's debt to equity ratio was relatively unchanged at 0.8x as of end-2023.

Operating cash was the main source of funding in 2023, and such was largely used for the repayment of obligations for the period. Net cash from operating activities amounted to P2.7 billion, higher than P2.0 billion in the previous year. Cash was primarily used in financing activities which amounted to P1.6 billion and consisted of net repayments to borrowings and lease liabilities. According to management, D&L is moving past peak capex with the completion of its Batangas facility. For this reason, net cash used in investing activities that was mainly spent on property and equipment was more tempered. This amounted to P1.4 billion in 2023, compared with the net cash outflow of P3.1 billion in 2022. Cash and cash equivalents as of end-2023 stood at P2.8 billion.

On September 14, 2024, D&L expects to settle its P3.0-billion Fixed-Rate bonds upon maturity. The Company is seen to comfortably service its obligations given its conservative leverage position.

**BUSINESS REVIEW**

**Company Profile**

D&L is a holding company for a group of companies that engages in customization, development and manufacturing of various products, such as food ingredients, specialty chemicals, raw materials for plastics, and consumer products ODM for personal and home care use. The Company also provides management and administrative services to its various subsidiaries and affiliate companies. D&L registered with the Securities and Exchange Commission (SEC) on July 27, 1971, and subsequently listed on the Philippine Stock Exchange (PSE) on December 12, 2012.

D&L’s corporate structure is shown in Figure 1.



**Figure 1. Corporate Structure of D&L, as of end-December 2023**  
Source: 2023 Audited Financial Statements

Jadel Holdings Co., Inc. (JHI) is the majority owner of D&L, accounting for 62.2% of the Company’s shares as of end-December 2023. D&L was 10.4% directly owned by the Lao family and the balance of 27.4% is

held by the public. JHI is 100% beneficially owned by the Lao family, hence raising the beneficial stake of the Lao family to 72.6% of D&L. PhilRatings notes that no single member of the Lao Family beneficially owns over 10% of JHI or D&L.

## Operations

D&L has four principal business segments: (1) Food Ingredients; (2) Oleochemicals and other specialty chemicals; (3) Specialty Plastics; and (4) Consumer Products ODM. *(Analyst's Note: Kindly refer to Annex A for an overview of each of D&L's business segments.)*

The Food Ingredients segment was consistently D&L's largest revenue contributor, as its share progressively grew from 58.8% in 2020 to 65.7% in 2022. It was followed by the Oleochemicals segment whose revenue contribution also increased and averaged 26.9% from 2020 to 2022. The Specialty Plastics segment came in third and lastly Consumer Products ODM, with average shares of 9.8% and 3.7% respectively.

The revenue contributions of each segment are shown in Table 1.

**Table 1. Revenue Contribution of D&L's Business Segments from 2020 to 2022**

Revenues	FY 2020		FY 2021		FY 2022		FY 2023	
	in mPHP	%	in mPHP	%	in mPHP	%	in mPHP	%
Food Ingredients	12,787	58.8	19,344	62.7	28,565	65.7	20,509	61.2
Oleochemicals	5,584	25.7	7,597	24.6	13,168	30.3	11,846	35.4
Specialty Plastics	2,575	11.8	3,085	10.0	3,279	7.5	3,328	9.9
Consumer Products ODM	1,087	5.0	1,108	3.6	1,111	2.6	1,334	4.0
Others – D&L Parent*	1,845	8.5	2,092	6.8	2,545	5.9	645	1.9
Eliminations	(2,139)	(9.8)	(2,371)	(7.7)	(5,183)	(11.9)	(4,158)	(12.4)
Total	21,739	100.0	30,855	100.0	43,485	100.0	33,502	100.0

\*Pertains to revenues from management and administrative services provided by D&L.

In 2023, the Food Ingredients segment was still the top revenue contributor, albeit with a lower share of 61.2%. The Oleochemicals segment was second, with a share of 35.4%.

D&L categorizes products into two—Commodity and HMSPs. A larger portion of the Company's revenues were historically derived from HMSPs products. These are products that are innovation-driven, tailor-made products that are customized according to clients' needs. The more customized the product is, the higher the expected profit margin. As such, the technical abilities to produce HMSPs is not easily replicated which gives the Company a certain degree of confidence against new market players. The nature of these products also ensures continued demand for the products of the Company.

**Table 2. Sales Mix**

	FY 2020	FY 2021	FY 2022	FY 2023
High Margin Specialty Products (HMSP) as % of Total Revenues	63%	57%	51%	62%
Commodities as % of Total Revenues	37%	43%	49%	38%

The sales mix of D&L, shown in Table 2, exhibited a downward trend in the share of revenues from HMSPs for 2021 and 2022. Consumers were leaning more towards basic products during the height of the pandemic which caused a shift in the sales mix. In 2023, however, the sales mix saw an increase in the proportion of HMSPs, returning to pre-pandemic figures. Due to the shift, overall blended gross profit margin improved to 17.1% in 2023, compared with 13.9% in 2022. Of the revenues from HMSPs in 2023, the Food Ingredients segment contributed 51% share to the total (50% in 2022), followed by the Oleochemicals segment with a share of 27% (30% in 2022).

As commodity prices normalized, D&L allocated much of its resources in growing its HMSP business which is expected to hold a larger portion of the sales mix moving forward. Nonetheless, the Company intends to keep its Commodities business despite having lower margins. D&L continues to see the strategic importance of the business in the form of the following: (1) maintaining customer goodwill; (2) protecting HMSP business by blocking off potential competitors; (3) covering some of the fixed costs; and (4) assuring the quality of HMSP raw materials.

The diversified business segments and product offerings are seen as a key advantage of the Company. Each segment may balance out the decline or increase of the other. The volatile changes in the sales volumes may be seen in relation to the developments in the industries served by each business segment, given the Company's numerous products and their wide range of applications.

**Table 3. Export Contribution**

	FY 2020	FY 2021	FY 2022	FY 2023
Export Sales (in billions PHP)	6.3	10.2	13.6	9.1
Export as % of Total Sales	29%	33%	31%	27%

Revenue sources were likewise diverse. A sizeable portion of D&L's revenues were from exports. In 2022, export sales grew by approximately 33.3% to P13.6 billion and accounted for about 31% of total sales, continuing its positive momentum from the earlier years. In 2023, export sales amounted to P9.1 billion, lower by 33.1% compared to 2022 and its share dropped to 27% of total sales. According to the Company, this decline was on account of the high volume of export orders from earlier periods, as well as the lingering effects of high inflation. In addition, some export customers were still consuming existing inventories.

Approximately 43% and 37% of export sales in 2023 came from the Food Ingredients and Oleochemicals segments, respectively. The balance of 18% was from the Specialty Plastics segment, while Consumer Products ODM took the balance of 2%. Exports were mainly driven by coconut-based products under the Food Ingredients and Oleochemicals segments. According to D&L, coconut oil continues to gain traction in the international market as a natural and sustainable substitute for petroleum-based raw materials.

D&L aims to further capitalize on this demand by entering into more export markets and by leveraging on its R&D expertise to introduce more specialized, coconut-oil based products.

The Company remains optimistic to reach its long-term target export contribution of 50% by 2027, or a 10-year target from 2017, as earlier disclosed by the management. This will be supported by the significant additional capacity from the Batangas facility, particularly for exports and higher value products, which will allow the company to cater to more customers in various markets.

As the Batangas plant started its operations, significant focus will be aimed at bringing in new export business. D&L disclosed that Chemrez Technologies, Inc. (Chemrez) already appointed distributors in key export markets in an effort to lay more foundations for the Company's export business. *(Analyst's Note: Kindly refer to the Production Facilities section for the discussion of the expansion in Batangas.)*

## **D&L's Principal Business Segments**

### Food Ingredients

D&L's Food Ingredients segment is operated through Oleo-Fats, Incorporated (OFI) and D&L Premium Foods Corp. (DLPF). D&L views itself as the leading manufacturer of industrial and specialty fats and oils and other food ingredients in the Philippines. The Company provides these products to a wide range of customers belonging to the food and beverage industry — from manufacturers of snack food, dairy, biscuits and confectionery to bakeries, and domestic and international quick-service restaurant chains.

The Company's product line has now expanded to over 1,000 varieties of food ingredients, including refined oils, specialty fats, and dry and liquid mixes and condiments.

In addition to oils and food ingredients, the Company also produces food safety solutions such as cleaning and sanitation agents. These food safety solutions are supported by professional and technical services.

### *Results of Operations*

In 2022, the Food Ingredients business continued to recover with sales posting a significant growth of 48%. Given that the segment recorded the steepest downturn during the pandemic, D&L also expected it to post the sharpest recovery once conditions improved. Overall sales volume was up by 14.0% year-on-year (YoY), largely supported by the 25% increase in commodities products. Net income from the segment likewise grew by 10% to P954 million. Gross profit margin, on the other hand, was down due to the shift in sales of commodities products versus HMSPs.

In the third quarter of 2023 (3Q 2023), sales for the segment posted a decline of 32% driven by the overall drop of 24% in sales volume. This decrease was led by the lower commodity sales volume as demand levelled in the post-pandemic environment. Gross profit margin of the segment, however, went up in 3Q 2023. Such was supported by the higher sales volume of HMSPs, posting an overall growth of 2% YoY, reversing from the 5% YoY decline in the last quarter. Net income for the Food Ingredients segment likewise grew by 1% for the period.

The segment ended 2023 with gross profits up by 16% and improved margins. Taking into account the incremental expenses from the Batangas plant, however, net income in 2023 was down by 18%. D&L believes that peak recovery for the Food Ingredients segment is yet to be achieved as the economy

continues to open up, likewise bolstered by the Company's continued focus to expand its export business and penetrate new markets.

### Oleochemicals and Other Specialty Chemicals

Operating through Chemrez Technologies, Inc. (Chemrez), its subsidiary Chemrez Product Solutions, Inc. (CPSI), and Natura Aeropack Corporation (NAC), D&L manufactures and distributes coconut-based biodiesel and other oleochemicals (chemicals derived from vegetable oils); resins such as polystyrene, acrylic emulsions and polyester; and a line of powder coatings. The Company manufactures these products for both the domestic and export markets.

This business segment is divided into two: the Oleochemicals division and the Other Specialty Chemicals group. Approximately 76% of the segment's consolidated revenues in 2022 came from the Oleochemicals division, while 24% were from Other Specialty Chemical products.

Encompassing the Oleochemicals division are the commodity biodiesel and high margin oleochemicals. The Company's biodiesel facility is the country's pioneer and, according to D&L, the only continuous-process methyl ester facility. This facility, along with the coco-biodiesel products manufactured in this facility, is accredited with the Department of Energy (DOE) and registered with the Board of Investments (BOI) under pioneer status. Products under the high margin oleochemicals category include glycerin and other coconut-based oleochemicals which are used primarily as surfactants or foaming agents for soaps and detergents. These products are mostly catered to the export market.

Under the Other Specialty Chemicals division, D&L manufactures powder coating, resins and other specialty resin-based chemicals. Powder coatings are protective materials applied to metals and other surfaces to provide resistance against heat, weather, UV light and certain chemicals. It is used in home appliances, metal furniture, fixings and fittings, mechanical parts, tools and equipment and in the construction industry. On the other hand, resins are chemically modified substances manufactured to suit specific uses. Such includes polystyrene resins for the plastics industry, polymer emulsions for the paint industry and polyester resins for the construction, shipping and furniture industries. Other specialty resin-based chemicals include additives, colorants and solvents.

### *Results of Operations*

In 2022, the sales of the Oleochemicals and Other Specialty Chemicals segment registered an increase of 45%, driven by the overall sales volume growth of 28%. Growth was brought about by the continued reopening of the economy and the awareness of consumers for more natural, organic, and sustainable products. Net income posted a solid increase of 47% to P1.4 billion and was the main driver of the Company's net income for the year. Gross profit margin likewise improved in 2022.

Sales for the segment in 3Q 2023 was down by 28%, associated by D&L to the following: high inflation and weaker consumer spending; early onset of the rainy season affecting the demand for construction materials; and highly competitive landscape in the biodiesel business. The robust growth in 2022 also set a high base rate for the current year. Gross profit margin marginally dropped in 3Q 2023, as a result of the aforementioned factors. Earnings of the Oleochemicals and Other Specialty segment likewise dropped by 53%.

In the last quarter alone, the volume of HMSPs under the segment grew by 88%, showing gradual improvement amidst the challenging environment. This was supported by the new production from the Batangas plant. Earnings for full-year 2023 was down by 50% YoY. According to the Company, several catalysts should support medium- to long-term growth for the segment, including: a) the potential hike in mandatory biodiesel blend; b) additional capabilities with the commercial operations of the Batangas plant that will enable the company to do deeper innovations and manufacture higher value-added products; and c) the company's aggressive export thrust with the appointment of distributors in key export markets.<sup>1</sup>

### Specialty Plastics

D&L manufactures a line of pigment blends, color and additive masterbatches and engineered polymers for various applications in the plastics industry through First in Colours, Incorporated (FIC) and D&L Polymer & Colours, Inc. (DLPC). FIC focuses on the domestic market, while DLPC focuses primarily on the export market.

D&L believes that it has the longest history in the domestic plastics color and compound industries with its brands that have been trusted by customers for over 50 years. D&L provides for the customers' color concentrate requirements for films, tapes, moldings, wire and cables, high-end fibers and other engineered polymers. The Company's investments in R&D and modern technology enabled it to provide products with a broad range of color choices and forms, specialty additives for plastics that enable reduced production costs or add desirable properties to plastics; and custom engineered polymers designed to have the precise color and properties required by customers. The Company also offers compounding services that enable customers to offer specialty compounds branded with their own labels.

The Company announced in November 2023 that it is set to launch a new set of products as an alternative to plastics that is equally durable and cost-competitive but is renewable, sustainable, and made from indigenous materials. As of end-2023, the Company has started to fulfill trial orders for a new alternative to plastics.

### *Results of Operations*

In 2022, the Specialty Plastics segment posted 7% higher sales despite a decline of 14% in sales volume. The disruptions caused by the Omicron surge and the global shortage of semiconductor chips used in automotives resulted in lower demand for the segment. Such did not undermine the steady and consistent demand of plastics from medical applications to packaging for deliveries. Net income grew by 11% to P760 million, while gross profit margin went up in 2022.

The segment had a slow start in 2023 with earnings down by roughly 20% YoY in the first half of the year. Sales volumes, however, picked up sharply in 3Q 2023, posting an overall volume growth of 6% YoY, reversing from the 4% YoY decline recorded in the previous quarter. Such resulted in the segment's sales

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<sup>1</sup> On January 4, 2024, the DOE published the draft circular on the guidelines for the implementation of the increase in the country's biodiesel or Coco Methyl Ester (CME) blend after a decade of delayed implementation. The said circular mandates an increase in biodiesel blend from two percent (2%, B2) to three percent (3%, B3) effective July 01, 2024, four percent (4%, B4) effective July 01, 2025, and five percent (5%, B5) effective July 01, 2026.

Source: D&L Press Release dated January 5, 2024 – "Higher Biodiesel Blend - A win for the planet, consumers, and the industry"

to lower by 1% YoY versus 3% YoY in the first half of 2023. Gross profit margin also improved for the period. This tempered the overall decrease in earnings to only 5% for the period. D&L attributed such improvement to the normalization of the global semiconductor supply that has prompted a rebound in the demand for engineered polymers used for automotive applications.

In the second half of 2023, earnings posted a turnaround of 46% increase from the first half of the year. This was driven by the improving global demand for engineered polymers that bolstered the sharp pick-up in volumes in the second half of the year. Volumes went up by 20% YoY. According to D&L, this division is expected to continue to grow over the long term fueled by the Company's R&D investments that are aimed at developing new applications for its products and introducing new technologies.

### Consumer Products ODM

Operating through its wholly owned subsidiary Aero-Pack Industries, Inc. (Aero-Pack) and NAC, D&L customizes aerosol and non-aerosol products across various industries that focus on maintenance chemicals and home and personal care products. It claims to be the first and biggest aerosol manufacturing company in the Philippines, with bulk of its sales coming from the domestic market. The Company offers a full turnkey solution from formulation, design and packaging to production and delivery of the products to the customer. It also supplies three-piece aerosol cans and components, which comprise the majority of aerosol product requirements in both the local and global markets. In addition, the Company offers aerosol contract filling and compounding services.

### *Results of Operations*

In 2022, the continued economic reopening fueled the 10% sales volume growth of the Consumer Products ODM segment. Personal care division of the segment mainly drove such increase, but was offset by the moderated demand for disinfection and sanitation products post-pandemic. Sales in 2022 was relatively flat, while net income went down by 7% to P232 million. Gross profit margin was marginally down in 2022.

In 3Q 2023, continued strong demand for personal care products with the resumption of many face-to-face activities bolstered sales volume growth. Such posted a 65% increase YoY, resulting in an increase of 34% in earnings for the period. Gross profit margin of the Consumer Products ODM segment remained high for the period. The Consumer Products ODM segment ended the year with its earnings up by 12% YoY and volumes higher by 40% YoY.

### **Raw Materials and Price Pass-Through Mechanism**

Of the total costs and expenses, at least 80% were for the purchases of raw materials. At least half of these raw materials were palm oil and coconut oil. Other raw materials include other types of vegetable oils, monomers, resins and other chemicals. These raw materials are sourced from both local and international suppliers. In 3Q 2023, approximately 55% of the raw materials are imported and mostly denominated in US Dollars. Prices of these raw materials tend to fluctuate, as these are affected by several domestic and global factors, including changes in global supply and demand, weather conditions, governmental controls and the relative strength of the Philippine Peso against other currencies. In relation to this, the Company employs a price pass-through mechanism, which enables it to pass on decreases or increases in the cost of raw materials to customers. It takes the Company 30 to 45 days to adjust its selling prices to reflect the change in raw material prices. The lag in price adjustments may become a factor that

could affect margins for the period, particularly in the event of rapidly changing prices. The margins will be positively affected in the period of declining prices in terms of raw material inputs, and negatively when raw material prices are going up. Overall, however, such movements will balance each other out and are expected to normalize over time.

Given the fluctuations in raw material prices and the Company's price pass through mechanism, shifts in revenue levels are therefore characteristic of the nature of the Company's business. As such, D&L focuses its efforts on managing its margins, sales volume and net income.

### **Production Facilities**

D&L employs an asset-light business model, where the Company does not own land or real property, but rather leases them from related parties and third-party lessors. D&L leases production facilities and warehouses, as well as barges and storage tanks used in its businesses. Lease agreements are typically for one to five years and are renewable unless terminated by either party. Approximately 2% of cost and expenses in 3Q 2023 were for rental expenses.

The Company's facilities are strategically located and easily accessible for its suppliers and clients. Such allows for timely and cost-effective deliveries of raw materials from suppliers and of the Company's products to customers. *(Analyst's Note: Kindly refer to Annex B for D&L's production facilities used in the operations of each of its business segments.)*

Capacity utilization is affected mainly by the anticipated seasonality and quarterly changes in demand for the Company's products. Decreased utilization is attributed to the macroeconomic challenges such as high inflation that affected demand for some products, whereas higher utilization is driven by the continued reopening of the economy and the resumption of face-to-face activities which fueled demand for some products. It can be noted that production facilities have room to cater more demand for each business segment.

#### *Update on the Batangas Expansion Facility*

On July 10, 2023, D&L announced the official commencement of commercial operations of the new manufacturing facility in Tanauan, Batangas. The facility sits on a 26-hectare (ha) land, located in the PEZA-accredited First Industrial Township in Batangas. There are three production plants within the facility — one plant will be used by DLPF and the other two plants by NAC. Operations are still in a soft-opening phase with a number of production lines up and running. Since the plant is still in its soft-opening status, the utilization is still very low and, likewise, the contribution to total production capacity is still minimal. D&L expects to run on full operations in the coming months, after the final fine-tuning works on the remaining parts of the facility is completed.

The land footprint of the new plant is 16 ha and is situated in a 26-ha property. D&L announced its plans to construct the new facility in November 2017 and construction officially started a year later. Some delays in the project timeline were experienced with the onset of pandemic-related restrictions on construction, as well as global supply chain bottlenecks. With the start of the facility's operations, D&L is optimistic with its growth by venturing into new global markets with the expansion of its production capabilities. The facility will mainly cater to the export business of the Food Ingredients and Oleochemicals segments, in line with the Company's goal of expanding its global footprint and increasing export contribution to 50%.

Being situated in a PEZA-accredited location, D&L is required to maintain at least 50% of export revenues to take advantage of PEZA tax incentives.

The Batangas expansion facility will allow D&L to manufacture from source — enabling the Company to process raw materials and package them closer to finished consumer-facing products. This will permit the Company to move a step closer to its clients by providing customized solutions and simplifying their supply chain, which is particularly crucial given logistical challenges.

D&L is likewise gearing up towards launching shelf-ready products made from coconut oil, promoting such as a natural substitute to many petroleum-based raw materials. The Company offers a plug-and-play solution for global brand owners who are looking to beef up their sustainable product offerings. The new capabilities brought about by the new Batangas plant will provide manufacturing solutions that are both economical and sustainable.

According to D&L, the expansion in Batangas is seen to accommodate growth for the next 20 years, although the Company may systematically roll out new production lines as and when needed. The progressive, staged rollout of new capacity will allow for a closer control of depreciation and operating costs.

In March 2024, D&L disclosed that Barone International awarded a LEEDv4 Gold Certification to the Central Hub building of the Batangas plant. The six-story Central Hub earned a total of 60 points (out of the maximum 80 points) for its various sustainability features which gained its second highest rating under the LEED certification.

## Customers

D&L's clients are large multinational and local corporations. Significant changes in any of these customers' purchases might have a material impact on D&L's business and profitability. On the other hand, such likewise provides stability and continued demand for the client's products given the expanse and nature of its target market. Many clients have built long-term relationships with the Company considering the contribution of D&L to their brand and end-products. D&L added that the variability of brand loyalty among consumers has a neutral effect on its B2B business given the scale of its client base, as the Company serves competing players in the market.

## Competition

According to D&L's management, the Company retains its position as top or a close second in most the segments it operates in. There has been no significant change since the last rating review. This is owing to D&L being the pioneer in several of its chosen businesses and essentially growing with the respective local industries. D&L's market shares for each of its business segments reportedly range from 30% to over 60%. D&L consistently aims to develop its R&D in order to deliver high quality products to its customers, and in turn retain its leading market position. The R&D-driven nature of the products manufactured by the Company has served as an initial barrier to entry for new market players. The huge capex spending required to build facilities, the applications of the products, and the customers' insistence on working with established suppliers who have a long track record of credibility have further limited the entry of market players. D&L likewise capitalizes on its longstanding relationship with its clients, which it has built over many years. Management elaborated that although the Company's products may form only a small part of what the customers make, these products are vital to the customers' brand and end-product.

## Management and Strategy

There were no changes in the key officers of D&L since its last rating review.

Yin Yong L. Lao is the Chairman of the Board of Directors of D&L. He has been a Director of the Company since 1971 and had previously served as President. He concurrently holds top management positions in other companies within and outside of the D&L Group. He is also a Trustee of the Association of Petrochemical Manufacturers of the Philippines. He graduated from the Ateneo de Manila University with a Bachelor of Arts degree in General Studies.

Alvin D. Lao was appointed as the Company's President and CEO in August 2016, and has accumulated more than 24 years of experience with the D&L Group. He is also a director in several other affiliated and non-affiliated companies. He is the President of the Technology Club of the Philippines (Philippine alumni of the Massachusetts Institute of Technology) and past president of the Entrepreneurs Organization (EO, Philippine Chapter). He graduated from the University of Western Australia with a Bachelor of Science in Information Technology (Honours) and Statistics. He also holds a Master's degree in Business Administration from the MIT Sloan School of Management. PhilRatings positively noted Mr. Alvin Lao's in-depth knowledge of the industry and his very hands-on approach to running D&L's businesses.

Mr. Franco Diego Q. Lao is D&L's Chief Financial Officer (CFO), Treasurer and Chief Compliance Officer since May 2021. He was previously Finance Director of OFI, has over 21 years of experience with the Group and also holds directorship in other affiliated companies. He holds a Bachelor of Commerce major in Accounting and Marketing degree from the University of Western Australia.

D&L's Advisory Board consisted of Dean L. Lao (Chairman Emeritus), Leon L. Lao and Alex L. Lao. Mr. Leon L. Lao and Mr. Dean L. Lao are co-founders of D&L. Mr. Yin Yong L. Lao, Mr. John L. Lao (Vice Chairman), Mr. Dean L. Lao, Mr. Leon L. Lao, and Mr. Alex L. Lao are brothers. Mr. Alvin D. Lao is the son of Mr. Leon L. Lao, while Mr. Franco Diego Q. Lao is the son of Mr. Alex L. Lao. To date, 20 members of the Lao family are involved in D&L. Such demonstrates the Lao family's commitment to the continuity of the business.

While the Company's top-level management is dominated by members of the Lao family, PhilRatings positively noted the appointment of non-family, experienced professionals in leadership positions. Moreover, four out of its seven Board members are independent directors which, as management stated, is a reflection of the Company's commitment to good governance.

Upon the demise of Filemon T. Berba, Jr. (Independent Director), D&L appointed Karl Kendrick T. Chua as Independent Director in June 2023. Mr. Chua was former Secretary of the National Economic and Development Authority (NEDA) and Undersecretary for Strategy, Economics, and Results at the Department of Finance.

As of end-December 2023, D&L and its subsidiaries have a total of 1,093 employees, growing from 810 employees as of end-2021. None of the employee groups have a collective bargaining agreement, as there are no labor unions in any of D&L's subsidiaries and operating facilities.

## Strategy

D&L's management has identified five key business strategies for the Company, which are as follows: (1) maintain market leadership; (2) innovate continuously; (3) capitalize on growing domestic consumer market; (4) enhance production and business processes; and (5) expand globally.

To keep pace with evolving technological innovations and to ensure that it can respond effectively and efficiently to market needs, around 14% of the Company's workforce is assigned to the technical department (R&D and Information Technology). Employees under this department pursue various R&D activities, including product development and application as well as quality assurance. R&D spend for 3Q 2023 amounted to P313 million, approximately 84.1% of full-year 2022 spend of P372 million. This was equivalent to 1.3% of total revenues for the first nine months.

Further to its commitment to R&D and product innovation, management also acknowledges that building a more sustainable future is a strategic action to future-proof its business. Thus, the Company has been investing in and prioritizing sustainability initiatives, such as the practice of green chemistry or the design of chemical products and processes that minimize or eliminate the use and generation of hazardous substances. D&L disclosed its plan to launch new cost-competitive substitutes to traditional plastics that are equally durable but are renewable, sustainable, and made from indigenous materials. D&L will leverage on its R&D investments to develop new applications in relation to its products and create plastics that are more economical and environmentally-friendly.

To further showcase its commitment to a more sustainable future, the Company incorporated sustainability features in its Batangas Facility. The overall design considered energy and water efficiency, reduction of CO<sub>2</sub> emission, and indoor air quality. Moreover, a significant portion of the power requirements the facility will be powered by solar energy. D&L is also exploring other renewable energy sources as fuel for its manufacturing plants. In addition, the Company intends to install its own Continuous Emission Monitoring System (CEMS) to consistently test and track its boiler emissions.

Upon approval of the Batangas industrial park, D&L plans to build a greenhouse for hybrid coconut trees within the compound. The planned greenhouse will serve as an R&D facility for coconut farming technologies, as well as the Company's coconut sustainability initiative that supports the global aim to promote sustainable and responsible sourcing of coconuts in the industry.

## **ECONOMY AND INDUSTRY**

### 2022

In the last quarter of 2022, the Gross Domestic Product (GDP) of the Philippines grew by 7.2%. This resulted in a full-year GDP growth of 7.6%, which marginally exceeded the government target of 6.5% to 7.5% for the year. The top contributors to full-year growth were: Wholesale and retail trade, repair of motor vehicles and motorcycles (+8.7%); Manufacturing (+5%); and Construction (+12.7%). Among the major industries, the Services sector continued to lead full-year growth (+9.2%), followed by the Industry sector (+6.7%), and then Agriculture, Forestry, and Fishing (+0.5%).

Household spending increased by 7% in the last quarter of 2022, and by 8.3% for the year. This was amid inflation reaching 5.8% in 2022, versus 3.9% in 2021. NEDA Secretary Arsenio Balisacan attributed such to the high employment rate supporting consumption despite higher commodity prices. Unemployment rate

was at its lowest in 17 years in November 2022 at 4.2%, down from 4.5% in the previous month. In the last quarter, however, household spending growth was slower than the 10% recorded in the first quarter of 2022 (1Q 2022).

Government spending likewise grew by 3.3% in the fourth quarter of 2022, and by 5% for the year. Latest data from the National Government Disbursement Performance of the Department of Budget and Management (DBM) indicated that Infrastructure and Other Capital Outlays increased the largest (+38.4%) for the month of November. From January to November, the combined allotment and capital transfers to Local Government Units were the biggest government expenditures (+24% and +28.6%, respectively), driven by the financial assistance and special shares from national tax collections.

### 2023<sup>2</sup>

The GDP growth in the last quarter of 2023 was logged at 5.6%, bringing full-year GDP growth to 5.6% in 2023. This was behind the government's target GDP growth of 6% to 7% for the year. The industries that contributed the most to the annual growth were: Wholesale and retail trade, repair of motor vehicles and motorcycles (5.5%); Financial and insurance activities (8.9%); and Construction (8.8%).

All major economic sectors posted full-year increases, as follows: Agriculture, forestry, and fishing (1.2% YoY and 1.4% in 4Q 2023); Industry (3.6% YoY and 3.2% in 4Q 2023); and Services (7.2% YoY and 7.4% in 4Q 2023).

On the demand side, annual growth of Household spending was at 5.6% (5.3% in 4Q 2023) while Government spending rose by only 0.4% (-1.8% in 4Q 2023) for the year. According to NEDA Secretary Balisacan, the latter's slower expansion was intentional as the government aims to achieve fiscal consolidation. This meant prioritizing reduction of fiscal deficit and government debt. Data from the Bureau of the Treasury showed an improved debt-to-GDP ratio of 60.2% in 2023, from 60.9% at the end of 2022.

GDP growth target for 2024 was set at 6.5% to 7.5%, nominally down from the previous goal of 6.5% to 8% growth for this year. Fitch Solutions unit BMI has maintained its economic growth outlook for the Philippines at 6.2% for 2024, banking on the rebound of investments that is expected to continue in 2024. BMI noted that the investment growth in the 4Q 2023 was 11.2%, bouncing back from a contraction of 1.4% in the previous period. BMI added that household spending will continue to fuel the economy as it boosts domestic consumption, particularly as the unemployment rate dropped to its decade-low of 3.6% in November 2023. The high inflationary environment, however, is seen by BMI as a risk to consumption for the year.

The International Monetary Fund (IMF), likewise, saw a positive outlook for the Philippines as it upgraded its economic outlook for the country in 2024. The GDP growth was revised slightly up to 6% in 2024 from the October 2023 forecast of 5.9%, amid the stronger rebound in investments and exports. The IMF similarly noted the Philippines' economic growth to be the fastest in the Association of Southeast Asian Nations (ASEAN) region. For 2025, IMF estimated a growth of 6.1%, still the fastest in the region.

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<sup>2</sup> Sources: <https://www.pna.gov.ph/articles/1217973>

<https://www.psa.gov.ph/content/gdp-expands-56-percent-fourth-quarter-2023-brings-full-year-2023-gdp-growth-rate-56-percent>

### Inflation<sup>3</sup>

Headline inflation rate was at 3.9% in December 2023, the lowest recorded for the year. This was down from 4.1% in November 2023 and much lower than the 8.1% inflation in December 2022. Core inflation rate was 4.4% in December 2023, similarly lower than the 4.7% inflation recorded in the previous month. The slowdown was mainly attributed to the slower growth in prices of Housing, water, electricity, gas and other fuels, followed by Food and non-alcoholic beverages. The former posted a growth of 1.5% in December 2023 (2.5% in November), while the latter grew by 5.4% for the month (5.7% in November). While the price index of the food segment slowed for the month, it was still the highest contributor at 48.5% of overall inflation in December. This was mainly driven by rice (+1.7 ppt); fish and other seafood (+0.3 ppt); and milk, other dairy products, and eggs (+0.2 ppt).

The month's growth brought full-year average inflation rate to 6.0% in 2023, still higher than the government target of 2% to 4% for the year. This likely diminished the chances of key interest rate cuts from the Bangko Sentral ng Pilipinas (BSP). BSP Governor Eli Remolona Jr. stated that further rate cuts will not be considered by the central bank until the inflation rate settles within the target range.

Headline inflation in March 2024 was the second consecutive increase for the year at 3.7% (3.4% in February) driven by higher prices of food and transportation. The inflation for the month brought the average inflation for the three months in 2024 at 3.3%, and within the government's target range of 2-4%.

The target inflation rate for full-year 2024 was pegged within the range of 2% to 4%. First Metro Investment Corporation (FMIC) and the University of Asia and the Pacific (UA&P) forecast that inflation will settle at 3.8% in 2024. This forecast was based on the slightly lower trend in crude oil prices, while imports and better second half harvests will limit rice price gains. The price of rice notably increased further by 22.6% in January from 19.6% in December 2023. The ASEAN+3 Macroeconomic Research Office (AMRO) also forecasts Philippine inflation at 3.6% in 2024, likewise within the government's target.

The Monetary Board left its benchmark rate unchanged at 6.5% in its second monetary meeting for the year in April 2024. This move was widely expected following the increase of inflation in March that was nearing the tail end of the target. The BSP stated that it will retain its hawkish stance while "contemplating" on an easing sometime in the third quarter. BSP Governor Eli Remolona Jr. pointed out that the BSP is not looking at further rate tightening but is waiting for some positive indication of weaker inflation to ease rates. If the results will be the opposite, the easing of monetary rate may be deferred to the first quarter of 2025, as stated by the BSP.

### Industry<sup>4</sup>

Based on the BSP's Consumer Expectations Survey (CES) report in the fourth quarter of 2023, the overall consumer confidence index (CI) was more pessimistic at -19%, from -9.6% in 3Q 2023. According to the survey, consumers attributed their negative sentiment to the following: (a) faster increase in the prices of goods, (b) lower income, (c) fewer available jobs, and (d) the effectiveness of government policies and

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<sup>3</sup> Sources: <https://www.pna.gov.ph/articles/1217191>

<https://business.inquirer.net/453871/bsp-keeps-policy-rate-unchanged-at-6-5-percent>

<sup>4</sup> Sources: Consumer Expectations Survey Report of the Bangko Sentral ng Pilipinas for the 4th Quarter of 2023  
Business Expectations Survey Report of the Bangko Sentral ng Pilipinas for the 4th Quarter of 2023

programs on inflation management, public transportation, and financial assistance to low-income households.

In the next quarter (1Q 2024) and the next 12 months, optimism weakened as CIs declined to 5.6% and 15% from 7.8% and 18.9% in the previous quarter, respectively. This was attributed to: (a) faster increase in the prices of goods, (b) lower income, and (c) fewer available jobs.

Consumers registered higher pessimism in all components — country's economic condition, family's financial situation, and family income.

The opposite can be observed for business owners. Business CI remained upbeat in 4Q 2023 at 35.9% from 35.8% in 3Q 2023, driven by the expectations of the following: (a) an increase in demand for goods and services during the Christmas season, (b) sustained economic recovery to pre-pandemic levels, (c) business expansions in the utilities, trade, financial, and hotels and restaurant sub-sectors, (d) development and launch of new products and services, and (e) brisker consumer spending on the back of higher remittances and inbound holiday travelers, including Overseas Filipinos (OFs).

Business sentiment for 1Q 2024 was less optimistic with an overall CI of 38.2% from 53.8% in the previous quarter. The outlook was reflective of the following expectations: (a) a decline in consumer spending typically following the holiday season, (b) adverse effects of the Israel-Hamas conflict on supply chains, (c) high inflation, and (d) rising interest rates. This is seen to continue for the next twelve months with a business CI of 54% from 59.7% in 3Q 2023.

#### Coconut and Palm Oil<sup>5</sup>

According to D&L, the commodity prices of palm oil and coconut oil tend to be volatile by nature and are heavily influenced by global events that may result in supply shocks. These can be observed during the onset of the COVID-19 pandemic, the UK-Russia war, and the temporary ban of palm oil exports by Indonesia. For this reason, D&L does not take long-term positions for these commodities and hence employs a natural hedge by passing on price changes to customers.

Coconut oil prices were generally on a downtrend in the Asia-Pacific region in 2Q 2023. Overall, lower demand, weakened vegetable oil market, and falling crude oil prices drove the decrease in prices. In particular, the price drop in the Philippine market was brought about by the increased supply and higher stockpiles that additionally put downward pressure to prices.

A similar trend was observed in the prices of palm oil. The largest vegetable oil exported — Malaysia and Indonesia, tightened their export quota for palm oil to contain rising demand in cooking oil ahead of Ramzan. Overall prices remained low at the end of the second quarter.

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<sup>5</sup> Sources: <https://www.chemanalyst.com/Pricing-data/coconut-oil-1316>  
<https://www.chemanalyst.com/Pricing-data/palm-oil-1319>



**Figure 2. Price Chart of Coconut and Palm Oil**

Source: D&L's FY 2023 Analyst Presentation Deck

## Food<sup>6</sup>

The manufacturing industry in the Philippines grew by 2.2% in November 2023. The Food sector was the second largest contributor to such growth, following the computer, electronic and optical products sector which was the top contributor for the month. The Value of Production Index (VaPI) for manufacturing of food products dropped by 3.9% in November, but slower than its decline of 5.2% in October.<sup>7</sup> The slower decline of VaPI for food products in November 2023 was primarily due to the slower annual drop recorded in the manufacture of other food products industry group which includes bakery products, sugar, and condiments, among others.

The United States Department of Agriculture (USDA) expects revenues from the food and beverage industry in the Philippines to grow by 6% in 2023, to approximately \$35 billion from \$33 billion last year. The revival of tourism and hotel activity will drive such growth. The USDA projected slower growth for convenience stores, groceries, hypermarkets, and warehouse clubs, while dining-in restaurants, catering and events will continue to grow. Consumers, however, will be more prudent on spending, marking an end to the “revenge spending” phenomenon.

Environmental sustainability is becoming increasingly important in the food manufacturing industry, according to Market Research Philippines. Local food manufacturers are incorporating local produce with the goal of supporting domestic suppliers and encourage sustainability. This also includes experimenting with recyclable and biodegradable materials as part of a move toward eco-friendly packaging. Not only

<sup>6</sup> Sources: <https://www.psa.gov.ph/statistics/manufacturing/missi/node/1684061906>

<https://www.bworldonline.com/economy/2023/07/09/533130/phl-food-and-beverage-sales-growth-slows-with-end-of-revenge-spending-usda-says/>

<https://www.philippinesmarketresearch.com/insight/unveiling-the-flavorful-landscape-of-the-food-manufacturing-industry-in-the-philippines>

<https://www.indexbox.io/store/philippines-coconut-copra-oil-market-analysis-forecast-size-trends-and-insights/>

<https://www.ofimagazine.com/news/philippines-aims-to-boost-coconut-oil-production>

<sup>7</sup> Value of Production Index (VaPI) measures the change in the monthly production values of manufacturing relative to reference period and base year (2018=100).

do these practices lower the environmental impact of the industry, but also appeal to environmentally conscious customers.

According to market researcher IndexBox, the growth of the Philippine coconut oil market slowed for two years since 2019, and finally recorded an increase in 2022. The market size was driven by higher consumption and is expected to sustain growth in the next years. In terms of export value, coconut oil exports went up in 2022, although relatively measured compared to the 69% increase in 2021. The main destinations of coconut oil exports were the Netherlands, United States, and China, which accounted for a cumulative total of 65% of total exports.

The average coconut oil export price reportedly increased by 30% and peaked in 2022. This is seen to post gradual growth in the next years.

The government is aiming to increase coconut oil production to meet increasing demand. Head of the Philippine Coconut Authority (PCA) Bernie Cruz reported that part of the government's plan was to support farmers by providing hybrid coconut seeds to speed up fruit formation and double yields. This plan was to be implemented over the term of President Marcos Jr. until 2028. According to PCA, each tree in the Philippines currently produces less than half of the amount in Indonesia and India. The target is to double the yields through replanting trees and producing coconuts in four to five years compared to the current seven years.

### Oleochemicals<sup>8</sup>

The global oleochemicals industry was valued at almost \$29.0 billion in 2022, according to India-based research firm Astute Analytica. This was driven by major manufacturers in Malaysia, Indonesia, and the Philippines. The growth of the market was driven by the growing applications of oleochemicals, including pharmaceuticals, paints and coatings, construction, and personal care. In addition, the development of green and sustainable practices led to oleochemicals being a popular alternative to petrochemicals. Demand for the use of oleochemicals in cosmetics and personal care products also grew with the rising health consciousness of consumers. Furthermore, plant-based diets and veganism led to higher consumption of plant-based oils and fats in food and beverages.

Astute Analytica likewise identified some factors that may temper the market's growth, which are: the high cost of raw materials used in the production of oleochemicals; volatility in crude oil prices; and fluctuations in supply and demand. Notwithstanding such, the market is projected to expand by a compound annual growth rate (CAGR) of 6.8% from 2023 to 2031.

Soaps and detergents are expected to be a major driver of the global market, accounting for over 31% of total market revenue. Continuing demand in this sector will come from the growing preference for environmentally-friendly and sustainable cleaning products. Moreover, the increase in population and greater awareness for hygiene and cleanliness are also contributing to the demand for the products.

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<sup>8</sup> Sources: <https://www.globenewswire.com/news-release/2023/02/21/2612334/0/en/Global-Oleochemicals-Market-to-Touch-Valuation-of-US-52-277-78-Million-by-2031-Driven-by-Players-from-Indonesia-Malaysia-and-the-Philippines-Astute-Analytica.html>

## Plastics<sup>9</sup>

The Department of Environment and Natural Resources (DENR) enacted the EPR Act of 2022 that requires businesses to recover their plastic packaging waste. Companies with total assets of more than P100 million will be required to create a system to recover 20% of the plastic waste that the company produced in the previous year. A fine of P5 million to P20 million will be imposed for companies that fail to comply.

DENR Secretary Antonia Yulo-Loyzaga added that companies are responsible for allocating resources to support the collection, recovery, transportation, processing, recycling and disposal of plastic packaging wastes in environmentally sound ways. The Philippines joins other countries that promote the EPR including United States, Canada, Japan, Singapore, India, South Korea, Chile, Mexico, Columbia, Peru and Brazil. The aim is to promote 60% recovery and recycling of plastic by 2030, as well as opportunities for technology transfer and assimilation in plastic waste management, particularly for different plastic waste streams.

PhilRatings notes that such opens opportunities for more sustainable plastic packaging solutions. D&L is seen to be in a good position given its capabilities to offer specialty compounds and additives to traditional plastics. Moreover, this gives the Company an avenue to introduce its planned launch of new products that are new alternatives to plastics.

The plastics industry in Southeast Asia has shown an upward trend, according to the report of Ireland-based Research and Markets. Global plastics and its products producers may shift production capacity to these regions given lower labor costs in Southeast Asian countries. On the other hand, rising market demand for plastics and their products in Southeast Asia will prompt global producers to increase their exports to these countries. With sustained economic growth in this region, market demand for plastics and its products is seen to strongly continue.

## Aerosols<sup>10</sup>

London-based market researcher Euromonitor International reported that demand for coatings and paints showed an uptrend in 2021, after the easing of the COVID-19 restrictions. Euromonitor attributed such growth to the revival in home improvement demand. Data from the Philippine Statistics Authority (PSA) showed that the revival in construction activity made growth in wholesale and retail prices of building materials reach their highest level in 14 years in 2022. Despite the uptick, the growth of the market was still slower than in pre-pandemic. Positive outlook was expected in 2023 that may push market growth to near pre-pandemic levels.

The global aerosols market was valued at \$77.5 billion in 2022 and is projected to expand by a CAGR of 6.1% by 2030 and reach \$124.4 billion. Identified growth drivers for the aerosol market is the growing population and rising demand for natural beauty products. As the population grows, more people seek to improve their hygiene. This is particularly true for millennials who are more environmentally conscious

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<sup>9</sup> Sources: <https://www.packaginginsights.com/news/the-philippines-bolsters-epr-law-requiring-businesses-to-recover-20-of-plastic-packaging-waste.html>

<https://www.researchandmarkets.com/reports/5702066/research-report-on-southeast-asia-plastics>

<sup>10</sup> Sources: <https://www.polymerspaintyournal.com/market-report-the-philippines-set-to-make-a-strong-comeback/>  
<https://www.vantagemarketresearch.com/industry-report/aerosol-market-1966>

and prefer more personalized products. Contributions from companies that create products that cater to this lifestyle have contributed to the recent growth in the aerosols market.

US-based market researcher Vantage Market Research sees projected expansion to be supported by new technological advancements in two key areas — production and application. Companies are investing in newer technologies such as 3D printing that enables smaller and more precise aerosols to be manufactured. These will likely result in increased demand for aerosol products in pharmaceutical, personal care products, and insecticides. In terms of application, aerosols are getting recognition in its role of increasing air quality. An example of such is nanoparticles that can improve air quality by acting as barriers against particles and allergens released by people and pets.

Personal care products held the largest market share in the market in 2021. The Consumer-Packaged Products segment is seen to post the highest revenue growth rate over the projected period, mainly due to the increasing demand in the food and beverage, cosmetic, and pharmaceutical applications.

## FINANCIAL REVIEW

**Analyst's Note:** *PhilRatings' calculation of certain ratios may be different from what the Company uses and publishes.*

**Table 4.1. Balance Sheet**

In Php Millions	2021	2022	2023	3Q 2023
Cash and cash equivalents	5,223	3,250	2,844	2,975
Receivables, net	5,339	5,618	5,657	5,163
Inventories	7,326	8,745	9,056	7,797
Property, plant and equipment	8,431	11,540	12,527	12,249
Total assets	36,326	40,760	42,625	41,355
Total debt	13,790	15,478	17,135	14,172
Total liabilities	17,221	20,109	21,758	21,054
Total equity	19,105	20,651	20,868	20,300

**Table 4.2. Income Statement**

In Php Millions	2021	2022	2023	3Q 2022	3Q 2023
Total revenues	30,855	43,485	33,502	33,902	24,715
Cost of sales and services	26,291	37,418	27,789	29,485	20,411
Gross profit	4,565	6,066	5,713	4,417	4,304
Operating profit	3,361	4,331	3,634	3,306	2,831
Finance costs	142	236	613	142	388
Income tax expense	577	777	725	624	651
Net income	2,643	3,318	2,295	2,540	1,792

**Table 4.3. Statement of Cash Flows**

In Php Millions	2021	2022	2023	3Q 2022	3Q 2023
Cash inflow (outflow) from operating activities	204	1,984	2,654	304	3,610
Cash inflow (outflow) from investing activities	(3,593)	(3,135)	(1,432)	(1,912)	(1,074)
Cash inflow (outflow) from financing activities	6,467	(782)	(1,627)	(1,043)	(2,820)
Net cash effect	3,078	(1,933)	(405)	(2,651)	(284)

**Table 4.4. Select Financial Ratios**

	2021	2022	2023	3Q 2022	3Q 2023
Gross profit margin (%)	14.8	13.9	17.1	13.0	17.4
Net profit margin (%)	8.6	7.6	6.9	7.5	7.3
EBITDA interest cover (x)	25.3	21.8	7.8	23.3	7.3
Return on average assets (%)	8.6	8.6	5.5	8.5	5.7
Return on average equity (%)	14.3	16.7	11.2	16.7	11.3
Debt service coverage ratio (x)	0.4	0.4	0.3	0.3	0.3
Current ratio (x)	1.8	1.5	1.2	1.7	1.5
Debt to equity ratio (x)	0.7	0.7	0.8	0.7	0.7
Total debt to capitalization (%)	41.9	42.8	45.1	42.6	41.1
Average collection period (days)	53	46	59	48	60

## Profitability

### 2022

D&L's total revenues rose by 40.9% to P43.5 billion, on account of higher sales volume, coupled with higher average selling prices. Both net sales and service income increased by 41.0% and 5.0% to P43.4 billion and P105 million, respectively. Of total sales, 31% came from export sales, slightly down from its contribution of 33% in 2021.

Gross profit margin nominally dropped to 14.0%, compared with 14.8% in 2021, with the slightly faster increase in cost of sales and services. Such grew by 42.3% to P37.4 billion in 2022 due to higher prices of raw materials. Nonetheless, gross profit in 2022 rose by 32.9% to P6.1 billion, mainly supported by growth in sales volume.

Operating expenses increased by 44.2% in 2022. Higher delivery charges drove the 34.3% increase in selling and marketing expenses. Moreover, general and administrative expenses also jumped by 81.1% due to higher depreciation and amortization expense and provision for impairment of receivables. Finance costs were higher by 66.7% to P236 million, driven by greater debt levels and higher average interest rates. On the flipside, net other income more than doubled on the back of recognized foreign exchange gains for the year.

Given the aforementioned, net income in 2022 amounted to P3.3 billion, up by 25.5% from P2.6 billion in 2021. Notwithstanding such, net profit margin slipped to 7.6%, compared with 8.6% in 2021, due to heightened costs and expenses.

## 9M 2023

Total revenues in the first nine months went down by 27.1% to P24.7 billion. The decline was on account of the challenging business environment with the lingering effects of high inflation. Moreover, while the third quarter marked the start of commercial operations of the Batangas plant, it also included the incremental expenses related to the completion of the facility. Net sales decreased by 27.2%, and was slightly offset by the 1.3% increase in service income.

Export sales likewise declined to a contribution of 27% of total sales, compared to its 33% contribution in 3Q 2022. Such was attributed to the slower sales due to high inflation and the consumption of existing inventories by some export customers.

The Food Ingredients segment continued to contribute the largest amount to total revenues at 60.4% (3Q 2022: 98.6%), followed by Oleochemicals at 25.7% (3Q 2022: 39.3%), Specialty Plastics at 9.8% (3Q 2022: 10.9%), Consumer Products ODM at 4.3% (3Q 2022: 3.6%), and the balance of less than 1% from other revenues of the Parent Company.

Cost of sales and services were lower by 30.8%, in line with the normalization of commodity prices. Resulting gross profit was marginally down by 2.6% to P4.3 billion. Notwithstanding such decline, gross profit margin improved to 17.4%, compared with 13.0% in 3Q 2022, on the back of the sales mix favoring HMSPs.

Operating expenses increased by 32.5% driven by higher rental, depreciation expenses, and business taxes and licenses. Finance costs likewise grew by 173.4% mainly due to higher interest rates.

Given the foregoing, net income in 3Q 2023 was down by 29.5% and amounted to P1.8 billion, from P2.5 billion in the same period last year. This translated to a net profit margin of 7.3%, marginally lower than 7.5% in 3Q 2022. The recognized incremental costs in relation to the completion of the new facility in Batangas added weight on costs for the period. D&L pointed out that excluding expenses related to the Batangas plant, net income amounted to P2.3 billion, partly lower by 10.9%, compared with P2.6 billion in 3Q 2022. Recomputed net profit margin will amount to 9.5% in 3Q 2023, higher than 7.8% in 3Q 2022.

## Projected Period

Projected revenues and net income are seen to post modest growth over the projected period as the Company kept a conservative position while considering macroeconomic conditions and its effect to the market. Albeit, margins will be strong on the back of controlled costs and expenses.

## **Cash flow and Liquidity**

### 2022

Net cash provided by operating activities amounted to almost P2.0 billion in 2022, significantly up from P204 million in 2021. This was supported by the growth in bottom line and coupled with a more tempered increase in receivables compared to the previous year. Bulk of cash was used for the acquisition of property and equipment, which was mainly in relation to the construction of the Batangas facility. Such primarily consisted net cash outflow in investing activities amounting to P3.1 billion.

Net cash used in financing activities amounted to P782 million in 2022. D&L paid dividends to shareholders totaling P1.7 billion in 2022, as well as payments of lease liabilities and interest from borrowings. Such was partly counterbalanced by net cash inflow from the additional borrowings and loan payables.

Year-end cash and cash equivalents stood at P3.3 billion in 2022, down by 37.8% from P5.2 billion as of end-2021. Current ratio slipped to 1.5x in 2022, from 1.8x in 2021, mainly due to faster growth in short-term borrowings. PhilRatings notes that all outstanding external short-term borrowings of the Group are covered by surety and corporate guarantee agreements. As of end-2021 and 2022, there was no default from the borrowings covered by the surety agreements and corporate guarantee.

Trade receivables stood at P5.6 billion as of end-2022, up by 5.2% from end-2021. Average collection period of accounts receivables computed by D&L improved from 50 days in 2021 to 43 days in 2022. The Company's cash conversion cycle likewise decreased to 101 days from 120 days in the previous year.

D&L does not have any foreign-denominated debt. The Company's exposure to foreign exchange risk is minimal and is mainly related to trade receivables. According to management, D&L is in a good position to naturally hedge foreign exchange (forex) risk through the balancing of its imports and exports. The Group also maintains a sufficient level of cash in foreign currency to comfortably service its debt obligations.

### 3Q 2023

Cash and cash equivalents stood at P3.0 billion as of end-September 2023, lower by 8.5% from as of end-2022. Generated cash was largely used in dividend payments as well as the acquisition of property and equipment.

Net operating cash amounted to P3.6 billion in 3Q 2023, significantly up from P304 million in the same period of 2022. This was mainly driven by the net cash inflow from movements in inventories, receivables, and due to related parties.

According to management, D&L is moving past peak capex with the completion of its Batangas Facility. For such reason, net cash used in investing activities was more tempered at P1.1 billion in 3Q 2023, compared with the net cash outflow of P1.9 billion in 3Q 2022. Such was primarily spent on the acquisition of property and equipment.

Net cash used in financing activities amounted to P2.8 billion in 3Q 2023. This consisted mainly of dividend payments amounting to P2.0 billion, and the rest were repayments to borrowings, lease obligations and corresponding interest payments.

As of end-September 2023, current ratio was unchanged at 1.5x from as of end-2022.

Net trade and other receivables decreased by 8.1% to P5.2 billion as of end-September 2023. Bulk of the total or 53.8% was current, and 12.9% of the receivables were more than 90 days past due but no accounts were impaired.

Based on Company computations, average collection period lengthened to 55 days (43 days as of end-2022) and cash conversion cycle likewise increased to 138 days in the 3Q 2023 (101 days as of end-2022). These were also mirrored by PhilRatings computations.

### Projected Period

Cash flows will be healthy and sufficient during the projected period as D&L focuses on the payment of its obligations, including the Company's P3.0-billion Fixed Rate Bonds maturing on September 14, 2024. Disbursements for investing activities will be moderate after the Company completed the construction of its Batangas plant.

Current ratio will be kept stable and D&L will remain in a comfortable position to service its debt obligations.

## Capital Structure

### 2022

Total assets expanded by 12.2% as of end-2022 and settled at P40.8 billion. While cash levels were lower by 37.8% from the previous year, progress in the construction of the Batangas plant increased property, plant, and equipment by 36.9%, which mainly drove the growth in total assets for the year. Inventories and receivables likewise rose, driven by higher raw material prices, and added to the increase in total assets.

Total liabilities went up by 16.8% to P20.1 billion as of end-2022, primarily due to the 18.9% increase in borrowings from additional short-term debt. Total debt stood at P15.5 billion, up by 12.2% from P13.8 billion as of end-2021. Stockholders' equity likewise grew to P20.7 billion, up by 8.1% from end-2022, driven by retained earnings. Due to the aforementioned, debt to equity ratio was maintained at 0.7x from end-2021.

Total capex in 2022 amounted to P3.5 billion, up from P3.2-billion capex spend in 2021. Most of the disbursements were on DLPF and NAC, with allotments of 52.2% and 36.3% of the total, respectively. These expenses were mainly in relation to the expansion of each subsidiary in the Batangas Facility.

### 3Q 2023

As of end-September 2023, D&L's total assets went up by 1.5% and stood at P41.4 billion. The higher balance of property, plant and equipment due to the near completion of the Batangas Facility mainly drove expansion of total assets. Such increase offset the 10.8% decline in inventories due to the lower average prices of key raw materials.

The Company maintained its conservative leverage position. Debt to equity ratio was relatively unchanged at 0.7x as of end-September 2023. Total debt went down by 8.4% due to the maturity and settlement of borrowings, from P15.5 billion as of end-2022 to P14.2 billion as of end-September 2023. Stockholders' equity dropped by 1.7% to P20.3 billion, from P20.7 billion as of end-2022, after the declaration and payment of dividends.

As a result of the foregoing, the Company's debt to equity ratio was relatively flat at 0.7x as of 3Q 2023 from as of end-2022. Moreover, total debt to capitalization ratio went down to 41.1% as of 3Q 2023, from 42.8% as of end-2022, mainly due to the decline in total debt.

Budgeted capex for 2023 was set at P1.1 billion, less than half of the actual capex in 2022. D&L expects to spend lesser capex after the completion of the Batangas Facility, and such was mainly allotted to the regular maintenance of existing plants

### Projected Period

The Company will maintain a conservative leverage position going forward, adding more flexibility to the capacity of D&L to manage its obligations and funding requirements. With the completion of the Batangas facility, D&L sees capex to slowdown during the projected period.

## Financial Flexibility

As of September 30, 2023, D&L had more than adequate available short-term credit lines with various foreign and local banks, which the Company may tap for funding of major projects and expenses.






D&L is also publicly listed in the Philippine Stock Exchange, and had a market capitalization of P43.9 billion as of April 15, 2024. D&L's status as a listed Company provides it with further opportunities to tap into the equity market should the need arise.

## Update FY2023

D&L ended 2023 with a net income of P2.3 billion, down by 30.8% from 2022. Total revenues declined by 23.0% to P33.5 billion, mainly driven by lower sales volume, as well as lower average selling prices. Finance costs increased by 159.7% to P613 million, largely due to the booking of interest expenses in the income statement that were previously capitalized during the construction period of the new plant in Batangas.

D&L mainly attributed the slower performance to higher interest expenses and operating expenses relating to the new plant in Batangas (i.e., costs that are now part of expenses rather than capitalized). According to the management, once commercial activity of the Batangas facility ramps up and slowly achieves economies of scale, D&L sees related expenses to taper and will result in gradually improving earnings. This was a similar scenario to the various plants that D&L had built in the past where incremental costs of the new plant may affect near-term income.

Excluding the incremental expenses related to the new facility, net income amounted to P3.0 billion, lower by only 15.3%, from P3.5 billion in the previous year. Net profit margin, excluding the incremental costs, will be higher at 9.0% in 2023, compared with 8.2% in 2022.

	 Food Ingredients		 Oleochemicals & Other Specialty Chemicals		 Specialty Plastics		 Consumer Products ODM		 D&L Industries - Consolidated	
% of Revenues	61%		26%		10%		4%		100%	
% of Net Income*	31%		27%		31%		10%		100%	
Sales	P20.5 bn	-28%	P8.6 bn	-22%	P3.3 bn	+2%	P1.3 bn	+20%	P33.8 bn	-23%
Net Income	P780 mn	-18%	P688 mn	-50%	P782 mn	+3%	P259 mn	+12%	P2.3 bn	-31%

**Figure 3. Summary of Group Results for Full-Year 2023**

As of end-2023, cash and cash equivalents stood at P2.8 billion, lower by 12.5% from as of end-2022. Cash was largely used to pay dividends to shareholders and obligations, as well as to acquire additional property and equipment. Operating cash amounted to P2.7 billion, supported by earnings for the year. Net cash used in investing activities amounted to P1.4 billion, lower than P3.1 billion in 2022, due to lower capex

needed in the Batangas plant. Net cash used in financing activities totaled P1.6 billion, mainly consisting of dividend payments and net repayments of borrowings.

Leverage position remained conservative, with a debt to equity ratio of 0.8x. Total debt increased by 10.7% to P17.1 billion, while shareholders' equity increased by 1.0% to P20.9 billion, as of end-2023. Actual capex in 2023 amounted to P1.4 billion (P3.5 billion in 2022). Such is expected to go down further with no major capex requirements in the pipeline. The lower capex will, in turn, increase free cash flows that will add more flexibility to comfortably service obligations.

According to D&L, NAC and DLPF, D&L's wholly-owned subsidiaries operating the Batangas facility, have both surpassed their first-year export commitment with PEZA, as of February 2024. The two subsidiaries combined have delivered 175% of their export commitment to date.

Export sales accounted for 27% of total sales in 2023 and consisted of the following: Food Ingredients (43%), Oleochemicals (37%), Specialty Plastics (18%), and Consumer Products ODM (2%).

D&L highlighted its optimism in expanding its operations with the added volume and capacity from the Batangas facility, particularly for its HMSP segment. In the last quarter alone, the volume of HMSP spiked by 40% YoY. This growth is a positive indication of future profitability given better margins for products sold in this segment.

## ANNEX A

## D&amp;L's Business Presence

Business Segment	Operating Company (Date of Incorporation)	Products and Services	Market
Food Ingredients	Oleo-Fats, Incorporated (May 4, 1987)	Fats and oils, specialty food ingredients, food safety products	Domestic + exports mostly to Asia plus to the US and European Union (EU)
	D&L Premium Foods Corp.* (June 29, 2017)		
Oleochemicals and Other Specialty Chemicals	Chemrez Technologies, Inc. (June 1, 1989)	Oleochemicals (coco- biodiesel and high value coconut derivatives)	Domestic + exports to Asia and developed economies such as US, United Kingdom (UK), EU, Australia (AU)
	Natura Aeropack Corporation* (July 20, 2016)		
	Chemrez Product Solutions, Inc. (November 16, 1988)	Powder coating, resins and other specialty resin-based chemicals	
Specialty Plastics	D&L Polymer & Colours, Inc. (March 30, 2006)	Engineered polymers for various applications such as auto, construction, electrical, etc.	Domestic + exports to Asia
	First in Colours, Incorporated (November 17, 1988)	Pigment blends, color and additive masterbatches	Predominantly domestic
Consumer Products Original Design Manufacturer (ODM) - previously referred to as the Aerosols segment	Aero-Pack Industries, Inc. (September 29, 1989)	Aerosol and non- aerosol products for personal and home care and maintenance chemicals	Predominantly domestic
	Natura Aeropack Corporation* (July 20, 2016)		

*\*D&L Premium Foods Corp. and Natura Aeropack Corporation are currently in soft-opening stage and operating with low-level operations. The operations of the companies are based in the Batangas expansion facility which commenced commercial operations in July 2023. These companies are Philippine Economic Zone Authority (PEZA)-registered and will export to Asia and developed economies.*

## ANNEX B

## D&amp;L's Manufacturing Facilities

Business Segment	Facility Name	Products Produced	No. of Production Lines	Rated Capacity (in metric tons per annum)	Capacity Utilization as of 3Q 2023*
Food Ingredients	Mercury Plant (Quezon City)	High-value food ingredients, marine fats, refined vegetable oils, hydrogenated oils	40	260,000	>60%
	MRI Plant (Manila)	Refined vegetable oils, fractionated oils	12	240,000	
Oleochemicals and Other Specialty Chemicals	Oleochemicals Facility (Quezon City)	Amides, methyl esters, glycerides	6	110,000	53%
	Resins Facility (Quezon City)	Polystyrene, emulsions, unsaturated polyesters	3	55,000	38%
	Powder Coatings Facility (Quezon City)	Powder coatings	3.5	3,840	76%
Specialty Plastics	DPLC (Laguna)	Plastic colors and additives, engineered polymers	22	70,000	70%
	FIC (Quezon City)	Plastic colors and additives	7	15,000	80%
Consumer Products ODM	Aero-Pack (Quezon City)	Aerosol and non-aerosol products	8	30,000,000 cans per annum	<60%

\*Based on the FY 2023 Analyst Presentation Deck