

18-Sep-2023

Campbell Soup Co. (CPB)

TD Cowen Sipping & Snacking Summit

CORPORATE PARTICIPANTS

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

Carrie L. Anderson

Executive Vice President & Chief Financial Officer, Campbell Soup Co.

OTHER PARTICIPANTS

Robert Moskow

Analyst, Cowen & Co. LLC

MANAGEMENT DISCUSSION SECTION

Robert Moskow

Analyst, Cowen & Co. LLC

Thanks again for being with us for the next installment of TD Cowen's Sipping & Snacking Summit. I'm Rob Moskow, senior analyst covering the food industry. And with us in this segment are President and CEO of Campbell Soup Company, Mark Clouse; and EVP and CFO Carrie Anderson. Since joining Campbell in 2019, Mark and his management team have taken a pragmatic approach to managing canned soup while investing in and consolidating its big snack business to generate profitable growth. Additionally, the company recently acquired Sovos Brands, which operates one of the fastest growing brands in the entire grocery store and a personal favorite on pasta night in my home, Rao's.

Thank you so much for joining us, Mark and Carrie, and good to see you.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

Great to see you, Rob.

Carrie L. Anderson

Executive Vice President & Chief Financial Officer, Campbell Soup Co.

You too.

QUESTION AND ANSWER SECTION

Robert Moskow

Analyst, Cowen & Co. LLC

Q

All right. Thank you. All right. So I'm going to start with some kind of broader kind of industry questions and then dive in to Campbell. We have 45 minutes. And for those who are listening, feel free to send questions on the message board and I'll be sure to get to them. So, let's start with consumer behavior. Been very confusing over the past year, especially compared to last year, because consumers are rather suddenly cutting back on their spending in the grocery store. Last year, demand was highly inelastic. And Mark, on the fourth quarter call, you provided some interesting thoughts on how these dynamics impacted your business during the summer and why you think it'll get better during the soup season. So can you dig more into that? And maybe explain the consumer research you did to kind of come to those conclusions?

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Sure. Yeah. So, I think always in these moments of seeking to take the complicated and make it simple, this is one of those moments where it's not particularly easy to do that. So we'll do our best to try to put it into a couple of different buckets. So, we really talked about three different areas that we saw influencing our business into a certain degree, more broadly, influencing the categories that we participated in. And I think they probably each kind of sit on the continuum of magnitude of contribution, but also, let's call it, intuitive or not intuitive that may help you kind of get your arms around at least how we're seeing it through our lens or through our perspective.

The first one is one that we all know and appreciate but arguably maybe got a little less of the press time or air time a year ago that may have diminished the awareness on its kind of sustained impact in that baseline of 2022 that I think we really probably realized a little bit more as we were really unpacking the fiscal fourth quarter of 2023, and that was COVID. And really, the dynamic that you saw through the summer where these variance spikes, where we get the news of the day, new variant, and if you remember what was going on at that time, we were rolling out substantial pricing, and a lot of that debate or the discussion was on elasticity. And Rob, to your point, many of the categories really felt almost inelastic, right? We're taking the pricing. We're still seeing pretty stable volumes. There wasn't really – certainly nothing near the norm of historical levels of elasticity.

I think probably in that kind of, let's call it, part of different variables, I do think COVID played a bigger role than we certainly called out or anticipated. But when you went back and looked, especially at categories that traditionally don't perform as well in the summer like soup, you really saw a pretty dramatic bump each time we ran into one of those. And I guess the good news, bad news story is, as you kind of exit the month of September, that dynamic, we really didn't see much in the winter. It was a more normalized baseline.

I am sure the threat of COVID still played a bit of a role, but I do think it was one of those things that created perhaps a bit more conviction or confidence to the lack of elasticity that might have had a more distinct and different variable or driver than just pricing alone. And so I think that's a part of the story. And arguably for us, in the summer and especially in the fourth quarter, as we started to tease apart contribution, there was a pretty big chunk of what we saw or we're experiencing. And I think we're happy that as we get into October and beyond, that we don't see as profound as a driver.

I think the second area is one we all know, right, which is pricing. And as we cycle that pricing, what we're all waiting for a little bit is the fact that the volume kind of replacing that. And I think as time goes on, we will see that.

But I do think both for us, the COVID component that I just talked about, and then the third area, which is really the consumer behavior space, has probably slowed that recovery a bit more than we would have hoped or necessarily expected. But I do think that as you imagine that curve on pricing, there is a start and a finish to that. And as we get into the back half of the year and at a minimum are lapping some of the consumer dynamics, I'll talk about in just a second.

I think the confidence that you hear from us and improvement, right – and we're not talking hockey stick, but a stabilization and then some positive contribution from vol mix as we get into the back half we continue to feel very good about. And that plus – finally brings us to the third area and maybe the most interesting, which is some of the consumer behavior evolution that we're seeing. And I think for a while now, we've certainly seen value playing a role. But honestly, as you looked at the categories, the resiliency in some of the categories were not behaving the way that you normally do in economic pressure where you see a lot of trading down. Although we do see that in a couple of categories, that wasn't like a broad narrative and that was a little bit of a head scratcher I think for many of us that have been through these cycles in the past.

And so as we dug into it deeper, what we actually saw happening is that there was almost a prioritization that consumers were doing. We saw that the basket size were getting smaller, but instead of trading down on the, say, buying the same items for cheaper items, what we actually were seeing was a distortion toward the more relevant categories for the moment. So those things that were more seasonally relevant, we saw a higher index to the ones that were less. And of course soup in the summer, where it's always a lower ranking, we saw that dropping even a little bit lower. And then, conversely, that paired with still some of the value, whether it's consumers moving to what we would call more stretchable meals or kind of more servings per dollar, if you will, as they were picking categories or migrating from maybe single serve to more kind of, let's call it, simple meals that allows you to feed more members of the family for the same dollars.

So, as far as what's the basis of that, really not a complicated analysis. It really started with understanding household penetration changes year-over-year. So where were we seeing less households buying categories and how did that vary depending on the category you were in? And one of the things we noticed was snacking was holding up extremely well and we were kind of like, that seems a little odd that it's not at least experiencing the same pressure as some of the other categories.

And that's when we kind of started to see this bifurcation between categories like snacking, which are, no matter what the season of the year, number one or number two. It's the highest household penetration for consumers and this variance versus kind of lower rank. So soup in the summer is the 34th ranked category by household penetration. Why we feel that the trends will likely improve in this dynamic is that moves to number 10 when we get into the winter. And so, as we move through into October and then certainly holidays in November and into the winter, we would expect the prioritization of soup to kind of improve.

Now, at the same time, we're already benefiting from the fact that categories like pasta sauce or cooking and condensed, where that stretchable meal or value concept we're doing very well. And although I don't think we're seeing as much broad scale trade-down as one might have expected, we are seeing it in some places like broth, where they tend to be a bit more commoditized segments. And so, that pressure is a little bit more pronounced there.

And so, that kind of gives you the landscape as we see it. I mean, I think it's fair to say that anybody that's telling you they know the day and the week that it's going to – that things are going to change or improve is probably certainly overplaying what I would see as being a little bit of still how the sequence of events unfold.

But what I will say is, as you get to the back half of the year, many of these things that I'm describing are already in the base. So even if you were to see consumers continuing to behave in a similar ways today, you'd still have that as a comparable. It's a lot easier to cycle than what we'll experience in the next couple quarters.

And that's why you see our plan for the year being a little bit of this phasing through. And as I've described before, a bit of difference between the high end of our guidance and the low end of our guidance is a little bit of how this transition occurs. And so, I think we're being appropriately pragmatic, but with a fair degree of conviction that we will see improving trends as time goes on.

So Rob, I don't know if that helps kind of give you a little more depth into it, but that's really kind of how we saw the dynamics unfolding.

Robert Moskow

Analyst, Cowen & Co. LLC

Q

Yeah. I think you hit on every point. I would like to know, you kind of gave us your kind of your 70:30 rule on the soup portfolio. And a lot of people who've followed this category for a long time, including me, have been a little disappointed that there hasn't been more growth, and also that Campbell's market shares have also declined over time. And can you talk a little bit more about the segmentation analysis you did in your portfolio?

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah.

Robert Moskow

Analyst, Cowen & Co. LLC

Q

And then, when you went to the trade with your merchandising plans for this soup season, how did it influence your merchandising strategy?

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. So great question, and I appreciate the fact that any time you start to re-carve up a category, there's always a healthy dose of skepticism. Are we trying to use math to our advantage? But what I'll tell you is, in really trying to understand a little bit of the disconnect in perspective, but also just helping people better understand the category. I mean, I think one of the things that jumped out at me in the fourth quarter, as an example, was, when we pulled broth out of the soup category, our shares were relatively stable. And if you look at that portion of the category over time, we've pretty steadily grown share. When you add broth into it, it kind of distorts the view of the business because broth has been a category – and again, this is not necessarily a good thing/bad thing, but just truth, that the category of broth has been growing at a disproportionate rate to soup.

So fourth quarter was a perfect example of this kind of, let's call it, complexity of the dynamics where you had more of a category dilemma on soup and really more of a share challenge on broth. When you put them together in a quarter, you draw the conclusion that everything has both problems. And what we were trying to do was to really provide a perspective that says, okay, 70% of our portfolio, which is really our condensed icons are cooking condensed, Chunky, Homestyle, Pacific, that core part of our business, the first point to take away is that it's 70% of our soup category.

And that business, over the last three years, has been extremely healthy, it's ability to grow. Certainly, we're facing some category dynamics right now due to the drivers I talked about initially, but that category as a whole has been very, very healthy. And if you go back and you plotted versus where we started this journey from, it is significantly ahead of where we were. That complete transformation of Chunky, both from a pricing strategy as well as a consumer dynamic, how we've protected condensed, the fueling of the growth of Pacific, we feel very, very good about it.

Now, having said that, that 30% of the business is not insignificant, and what that represents is the flankers on our condensed business where I think Healthy Request, think kids' brands, think flavor number 15 or 20, Well Yes! and some of our flankers on RTS and our Swanson broth business. And as we look at those, there's probably going to be a different answer for each of them. I do feel like first on Swanson, which is where we are experiencing almost entire share pressure we're seeing right now, the first point I would make is that, that is a business that, in fact, over the last three years we gained a lot of share for whatever reason, private label was a little bit slower back to the party there and we did accumulate some share. But nonetheless, even on a three year horizon, we're still, not to the extent we see right now, but we are still down on share.

And that really is a category where we've got to make sure our blocking and tackling and kind of tactical elements are right. Price gap is right, good promotion display, in particular during the holidays. One of the things we're feeling good about as we go into Thanksgiving and Christmas is, a year ago, private label was kind of the new shiny object for a lot of retailers and so they chose to go key week and really try to drive traffic with private label and it really didn't work. And so the good news is, Swanson, that is the time of year where consumers are not as willing perhaps to compromise with lower prices. It gives us a chance to kind of get back into that key week, which is so important for us.

But that one's going to be a little bit more of a strategy around ensuring value is right. Make sure that we've got the right execution behind it. It's not where the growth is really going to come from, but I don't expect it to be a leaky bucket into the future either. I think on the flankers, both for condensed and for ready to serve, I think it's going to be a combination of reframing some of those to be more clear on their value drive, while also probably rationalize some of it. I think there are some flanker number 40 or 50 on the list. I think we've got enough innovation and enough of a storyline on that 70% that we can create a story for retailers to redeploy the real estate on shelf to make room for the space that we have. And so, as you imagine a future dynamic, I would expect that 30% to shrink a bit more, stabilize, and then use that 70% and continue to grow.

And so, more to come on that. I think as we move forward, we'll try to give investors a better, let's call it, set of breadcrumbs to follow to see that strategy fully evolve. But it is – if you look at all categories in Nielsen and IRI, I would tell you there is no category that has a more disparate number of items that are used in different occasions, different price points that are shifting into one total soup category than that. So, look, I think what I'm trying to do is just make sure that the strategy we're actually executing is more obvious and more trackable for investors.

Robert Moskow

Analyst, Cowen & Co. LLC

Q

Okay. I hate to keep poking on the weaker parts of the portfolio.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

That's all right. That's okay.

Robert Moskow

Analyst, Cowen & Co. LLC

Q

But V8 has been a – I'm sorry, I hope you weren't groaning there.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

No. I was breathing.

Robert Moskow

Analyst, Cowen & Co. LLC

Q

Okay. Good. It's been challenged and for years and years I think investors would sometimes question whether beverage belongs in the Campbell portfolio. And especially now that you've made a big acquisition in a category where – in pasta sauce, where – and even in frozen meals where it looks like you have some real strong tailwinds and runway.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Runway. Yeah.

Robert Moskow

Analyst, Cowen & Co. LLC

Q

What do you think the future is for V8, and why does it belong or what are the pros and cons?

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Right. Well, I think V8 is one of those that I would tell you it's a pretty unique animal in the world of beverage. One of the reasons why – this will probably seem fairly obvious, but one of the reasons that it fits is because it has a very, very common ingredient base to a large part of our portfolio, especially as it relates to V8 Red, which is the vegetable juice. And again, not unlike a little bit of the story we just went through, V8 is a little bit of a story that is told through the different sub-segments of the category. If you look at kind of in a continuum of good to challenged, years and years ago we launched V8 Splash, which was designed to be kind of a marginally better for you version of a kid's juice. And I think over time, really the point of difference or the separation for Splash has become far less.

And so, we've got to really decide whether or not Splash – we're going to do that and we can have it stand on its own two feet or not. But when I look at the balance, which is the V8 Red, I'm not sure that's going to be a growth engine but I do think it has consistently been a fairly stable business. It does drive a lot of synergy and benefits from the fact that our access to tomatoes, our ability to process, really serves that business quite well.

And then you have V8 Energy, which has been extremely successful. And so the goal in mind here is really, let's drive V8 Energy. I think you're going to see even in this year continued expansion of that platform, both from a distribution and geographic footprint. V8 Red, we're going to continue to do really what we have been doing, which is kind of the OG of plant based beverages as we affectionately refer to it as, but use it in this context of really being this opportunity to bring – for those that are focused on more plant based diets or looking for servings of vegetables, it is still arguably one of the most effective ways of bringing that into your diet.

And then Splash, I think, not unlike the flanker discussion we just had on soup, we need to once and for all kind of figure out what that strategy is going to look like and where that goes going forward. As far as the long term view of its relevancy in the category, I think for now it's certainly not creating a distraction or a problem for us. I do agree with your point of view that says, all right, as you get bigger with core items, does that provide a little less emphasis? I think we run it in a pretty efficient but focused way. And so I don't see it as a necessarily a problem, but I think we do have some work to do on it.

And part of what I'm – I just was having this conversation a couple of weeks ago with some investors is, I mean, truth be told, during COVID and kind of through the last couple of years, some of these category or portfolio dynamics where we've got to kind of roll up our sleeves and get a few of these things better positioned for the future just really didn't make the hierarchy a priority in a world where we were dealing with a lot of other variables that we felt were bigger priorities for the business.

And that, honestly, that triage of items I still think were the right priorities to focus on. But now that we're in a world where we're feeling a little bit more normality in the environment, this is a great moment for us to kind of complete the mission on a few of these categories that still have some work to do.

But I don't see any of them as being dramatic undertows to the business, but more opportunity to reshape so that – you could imagine a world, Rob, where we're sitting in the back half and let's assume for the moment that we've got the consumer landscape right, we execute the acquisition of Sovos, we could be in an ideal position to be able to come back to investors with a vision of this transformed Meals & Beverage portfolio that raises all this kind of residual concern of, can I grow, can this contribute, can this be a positive energy in the business, while filling in a few more of the blanks on Snacks, which has terrific momentum on top and bottom.

And I think, really, for the first time position Campbell's as truly a more differentiated, growth driven storyline and maybe shake off a little bit of the legacy of this kind of questions that we've needed to answer. So I'm excited about coming into that window where we can tell this kind of next chapter with really tangible pieces of evidence and distinct actions that I'm hoping will be a real catalyst for the company and the stock for – on that stake as well.

Robert Moskow

Analyst, Cowen & Co. LLC

Q

Sovos certainly adds a lot to the story, and I'm going to get to that in a short time. Let me ask a different question, though, and then we'll also get into Snacks. But one of the debates I hear in the space is that, I guess, doubts that the industry has really changed four years after the pandemic, that there hasn't been any real difference in competitive advantages or how these big food companies have evolved or how consumers have changed. And I want to know if you could highlight maybe some of the key capabilities that your company has developed, especially in the past four years, how you've capitalized on technological advancements and marketing and selling, digitization of the supply chain. Kind of feeding you what I want to hear, but maybe you could talk a little bit about that.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. Well, I mean, normally, I'm pretty diplomatic in my digestion of the challenge, but honestly this one, I would tell you I just think is dead wrong. I mean I think the amount of transformation that has occurred over these last four years is probably one of the most profound step changes certainly at Campbell's, but I think for many parts of our industry that we've probably experienced over the last 20 or 30 years. I mean, it really I think out of necessity for us, right, which is I think was a gift as I felt like we were a little further behind the pack, if you will, when we

walked into the pandemic. And that was probably a good catalyst for us not to be able to kind of relax and wait for the world to calm down because you did end up waiting four years if you took that strategy.

But I think there's a lot of meaningful changes. And for us, I'll use Campbell's as the example. But our supply chain is completely transformed from where it was. And whether that is the technology or the integration of the supply chain into the commercial operations with everything from forecasting to how we're laying out the network for the future, how we operate in our manufacturing facilities, how we motivate, develop and train the folks that are on the line and get them prepared for this next generation of work has been profound.

And I think for us, it's been one of the things that really has given us where I would have said a liability. I actually think because we had to chase that faster, it gave us some distinct advantages. We're cycling through kind of that recovery and, yeah, maybe there is getting it back to a normal level you'll see it more. But I think in the back half of the year, as you watch our cost structure or our margin agenda and you see those pieces coming to fruition, already some on snacking, but even on Meals & Beverages across the board, I feel great about it. I also think – I mean, we've integrated now Snyder's-Lance, Pacific, our portfolio has been completely transformed.

I mean, set aside Sovos for a minute, we've kind of offloaded the majority of the businesses that we felt were not core to us even with the latest sale of Emerald. Thus, we really have just kind of completely embraced this concept of one geography, two divisions and 13 categories. And I think focus is just incredibly powerful in this moment because it allows us to better mass our resources, capital, human, you name it, against that. And you go back four years, five years, we were a little bit all over the map, as you know. And I think that's been a big mission for us as well.

I think on the marketing side, again, it's interesting, COVID, as tragic as that period was, it forced you to learn a few things. I look at two brands in our portfolio that are just completely different today than they were four years ago. One's Goldfish and the other one is Chunky soup, right? You had a Goldfish business that was really a kids brand. And when moms stop taking kids to soccer practice, all of a sudden we were like, uh-oh, it's in the house, but not – how do we get this thing stimulated and driving?

And the team just did an amazing job using what I would call more disruptive technology on marketing to really age up the target. And really smart innovation like Frank's RedHot or Old Bay, Dunkin, all great tools for us, but really changed completely the trajectory of that brand. And we did that really through these last four years. And I'd like to think we would have done that anyway, but the catalyst of being in that moment put real pressure on us to think differently.

And Chunky is a little bit of the opposite, which was, this thing was being foot-balled, if you will, \$0.99, 10-for-10. It was low price, viewed as cheap food. And we completely reframed it with a younger audience to be protein driven, affordable, quick and great tasting, where Chunky soup of all things, on Madden football and gaming as a platform. I was a little skeptical, but honestly, just really hit it out of the park.

So I do think the difference between where some of our brands are today in their relevance and readiness as we kind of come out of this long tunnel, I would tell you, I feel great about where we are. And look, I think you can see that in the fact that now, we used to all kind of tout this 50%, 60% of our marketing and more contemporary digital and social. We're well over 80% now that's in vehicles that are really designed to be very surgical in nature, high ROI and efficiency. We learned a lot about e-commerce and how to convert marketing into purchase, skills that we really didn't have necessarily a long time ago.

And I guess I just would finish the consumer story with for us, right, we have another generation of consumers that know how to cook, and I don't know if that would've happened had they not been backed into the kitchen and had to kind of survive and learn their way forward. But regardless of that fact, we've got a platform now where you see businesses like our condensed cooking soups with a younger millennial household where the growth has come from that's continuing even in this tough environment to grow share is to me, pretty, pretty powerful.

And, look, I think – I feel great about the leaders we've put in place and how we're positioned. So I would say I really feel like this is a different company today. And, look, step back for a second, all the growth at the time was happening in small disruptive brands five, six years ago. A lot of the news or innovation was coming out of these smaller kind of platforms. I just don't think – I think we've retooled. I think you see more innovation coming from the companies now as we needed to, right?

We needed to react and needed to pivot. And I always said, look, it's not an easy overnight turn, but I think these several years have allowed us to get ourselves better postured for the future.

So, I mean, I can't speak on behalf of every company, but I would certainly say from our vantage point, I feel like we're in a really different and better position today than we were. It doesn't make it any easier, by the way. But as far as where we are, I think, well ahead of where we were.

Robert Moskow

Analyst, Cowen & Co. LLC

Q

Okay. And maybe my follow up to that, actually for Carrie, too, is in prior years when companies realized they needed to reinvest for growth, it came with a backward step in profitability and margins because you had to pay for it. And Campbell went through many, many phases of that over the years. But this one seems a little different. And it seems like there's reinvestment and profit growth at the same time. Is that a function of just better tools and more refined marketing capabilities? Is it just because there's a lot of productivity? Maybe for both of you on that.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. Why don't we start with Carrie? Yeah.

Carrie L. Anderson

Executive Vice President & Chief Financial Officer, Campbell Soup Co.

A

Yeah. I'll start. Yeah. And then Mark can add in. But I would say that the good news is that you're starting to see some of the normalization of the macro environment, right? So the trends on inflation are going in the right direction. By no means are we in a deflationary environment yet, but at least we're seeing that those headwinds moderate more. So that's going to allow for some of that margin expansion then to happen. As we talked about for our guidance, some modest levels of margin expansion and earnings growth is what we expect for fiscal 2024.

Good news is that you see that in the Snacks business. So Snacks business saw 14.4% operating margins, 130 basis points improvement from fiscal 2022 in our fiscal 2023 results for Snacks. And there, I think we're seeing that benefit of some of those great productivity improvements. But I think a lot of it is just getting to a much more healthier macro environment as our supply chain, as Mark indicated, has now moved to a strength and we start to lean in more into some of our productivity initiatives, and they start to get to the bottom line, right?

So for Snacks, particularly we've talked about a margin growth – a margin roadmap that ultimately continues to see progression there. We talked about fiscal 2024 margins for Snacks being north of 15%. We feel really good

about that. Again, in light of the fact that we're seeing some of those macro tailwinds – or headwinds subside and allows that productivity to get to the bottom line. In addition for Snacks in particular, we're working on a lot of unique network optimization opportunities, particularly in our warehouses, in our hubs, in our depots, optimizing those, working on our portfolio mix within Snacks. Mark mentioned the Emerald divestiture is one piece of that, but we're also making concerted efforts around where we can grow our own brands and tapering off lower margin, contract manufacturing and partner brands. We're going to be taking advantage of that as well.

Mark, anything else you want to add there?

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. I mean, look, I don't want this to sound like disparagement of other people's strategies, but I will say one of the things that we've been very disciplined on throughout is, when we were feeling pressure on margin, we resisted the temptation to cut all the marketing and equity spend. And I've been there, done that. And inevitably, the reason that dynamic, Rob, you're describing has happened historically is because, yeah, it feels great to be touting big margin enhancements for a quarter or two and then you're like, well, I've got to add it back.

And so I think what we've tried to do throughout is kind of use our guardrails of kind of 9% to 10% of net sales for marketing and selling and try to keep ourselves within that envelope. We may make move a little bit from one to the other, depending on the dynamic, but we did not let that be a temptation that we took. And so therefore, as we start to see the recovery that Carrie just described, you're not going to have that traditional offset of, well, we got to put all the money back into promotion, into equity because we had taken it all out when we were feeling a little pressure.

And as your bridge – like, even last quarter, 100 basis points of the margin hit was really equity investment. And I was quite frankly happy to do that because I feel like this is the moment where we do not want to back off as we kind of come out of this cloud or this turbulent time. I want our core equities to be strong and really be able to be better positioned, if you will, to take it on. And look, I don't think that is the same playbook that was used by everybody in the industry, and I think if you needed or felt you needed to cut that, it's probably coming back.

Robert Moskow

Analyst, Cowen & Co. LLC

Q

Okay. Got it. Can you delve a little bit more, Carrie or Mark, into the building blocks to get to, I think, 17% margins in Snacks over time? You mentioned network optimization being a big part of it, warehouses, hubs and depots. I personally always get a little bit confused as to how many warehouses, hubs and depots do you have? What are you trying to do with them?

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Thousands of them, Rob.

Robert Moskow

Analyst, Cowen & Co. LLC

Q

Many of them are Snyder's. Trying to get my head around thousands. I don't quite get it. So maybe a little more framework around that.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. Look, I think Carrie and I can kind of tackle this together, but let me give you a little bit of a view of how the business operates today. That might help you kind of have a foundation then that we can make a transition off of. So today, as you know, we've got plants that were Snyder's-Lance plants. We have plants that were Pepperidge Farm plants. And that's kind of where we began the journey, right?

So you had, I think in total 16 – 14 or 16 different plants or different manufacturing platforms that we were operating around the country. And then, we had three – or have three DSD networks. So you have a fresh bakery, a Snyder's-Lance and a Pepperidge Farm. Each of those DSD networks had their own depots and hubs. And essentially, a depot and a hub are both warehouses, they're just different sized warehouses.

And so, what happens is you start to consolidate volume for each of our three networks, and then the last stop is a hub or a depot where that's a truck pulls up to a depot and loads up their truck, takes off to the store. And so, if you imagine, like, that's probably 900 plus of those around the country, I think. And then, in different geographies, they get a little more spread out, but there's three of the same thing almost everywhere you are.

Robert Moskow

Analyst, Cowen & Co. LLC

Q

And you own all those depots, is that right?

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Almost all of them. Yeah. So our strategy, right – so I'll just do kind of DSD manufacturing and then I'll let Carrie talk a little bit about other variables in that bridge. But essentially, what the first step was, was to create some synergy starting upstream, right? So the way you want to do it is start to create consolidation as close to the plant as possible and then begin to roll that all the way through, all the way to the truck, right, is the goal in mind.

And I would tell you what we've done is, we've begun to consolidate manufacturing. So we now have plants that are producing both Snyder's and Pepperidge on the same footprint. Charlotte is a great example of kind of our first mega plant. That enabled us to close Columbus, Georgia. So our ability to begin to shrink that manufacturing footprint is one of the first kind of productivity areas that we had.

Then, the next thing we did was consolidate mixing centers. So these are where it's coming out and then going off to depots and hubs from. We've now consolidated those. So both Snyder's-Lance and Pepperidge Farm are running through those. Fresh bakery is a little different because you don't have time. That really goes right to the depot. So everything we've done so far generally has been around salty and cookie, cracker. Bakeries, really, just been kind of self-contained.

Now, when we get to the hubs and the depots, those are what we're going after now. And so, the idea is to consolidate those and begin to create savings by taking down two of your three, consolidate it into one, and invest in technology and capability. Because I'd argue, many of these are still like guys with a clipboard walking through. So to automate it to move them faster, to get them through all the way through.

The next step, right – and that's really what you're beginning to see now, right? That savings is what the kind of next chapter is, if you will, of productivity. And then, the final one that I get asked a lot about is DSD. And we will

talk – we now know what we're going to do there, and we'll talk more about that in the next Investor Day, which probably March-ish timeframe.

But what I'd tell you in kind of two-second version of this is, we have a large part of the country, primarily the East Coast, where the size of the businesses are so big, there's no need to consolidate, right? There's more than enough scale to drive both trucks around, go to salty, go to cookie, cracker. Then there's a big chunk in the middle of the country, and as you go West, where we've been using partner brands and other scale builders to try to support two DSDs. Those, we've been piloting and testing opportunities to bring them together, because, arguably, one thing that's kind of unique is we'd be one of the few with DSD going to both salty and cookie and cracker in the store.

I will say that those have gone extremely well, probably better than we had expected, and that that's going to open up an interesting opportunity to think about that, how do we take that information and go. Now, we'll always probably still have a few places, Pacific Northwest, some other parts of the country where there may be a little bit more to learn to figure out the most efficient, but we do those first two steps, right? We get the hubs and the depot consolidated and we figure out how to deal with this kind of mid to west of the country.

I mean, those are big step changes. And the good news is, these are not like multibillion dollar – I know a lot of concern about we're going to take it all captive and bring it back in and go to Mondelēz's model or FRITOS' model. No. I think an independent distributor model can work. We just had to figure out how to best configure it. So that's really it. I know I maybe took more of the time Carrie for you but there's a lot to believe and a lot of wood to chop there to get to that 17%.

Robert Moskow

Analyst, Cowen & Co. LLC

Q

That's great. And I'm going to slip in one last question on Sovos because I got it from the crowd here. Can you outline what your target IRR is for the Sovos acquisition and the cost of capital that you assumed?

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. So, we'll talk a little more once we obviously get past closing. But we have a pretty hard and fast rules for accretion and IRR. We want double-digit IRRs on anything we're investing. So you can safely assume we're well into that range. And as we've said, accretive in year two. Those are two big hurdle rates that we have to get over for us to feel good about any M&A we do. And you're just not going to see us reach or overpay for something that we don't see the returns. Doesn't mean we won't pay a high multiple, but the economics of it, we want.

Carrie, why don't you talk a little bit about cost of capital?

Carrie L. Anderson

Executive Vice President & Chief Financial Officer, Campbell Soup Co.

A

Yeah. I mean, cost – I mean, it's certainly, as we think about IRR, again, it is definitely above our cost of capital here. And I think again, as we think about what we used in the financial model, I think we were conservative in assuming what the cost of debt would look like there. So, as Mark indicated, it's met our hurdles for IRR, it's met our hurdles exceeding our cost of capital and accretive by year two.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

And we did – so, if you look at the environment today, it's not like – because of how we made the assumptions, we knew there was volatility in the market, so we were fairly conservative. So where we are today, we still feel very good about the model and the economics that were put in place.

Carrie L. Anderson

Executive Vice President & Chief Financial Officer, Campbell Soup Co.

A

That's right.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

We'll obviously be taking action to make sure that we can hedge and appropriately put those protections around it, but I think wisely planned it with a little bit of volatility in the world.

Robert Moskow

Analyst, Cowen & Co. LLC

Great. Okay. Well, I'm going stop us there and thank you both again for joining us today. And everyone's got other meetings to go to. So, Mark, Carrie, thanks again and look forward to talking to you again soon.

Carrie L. Anderson

Executive Vice President & Chief Financial Officer, Campbell Soup Co.

Thanks, Rob.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

Yeah. Thanks, Rob. Congratulations on your new gig, man, by the way.

Robert Moskow

Analyst, Cowen & Co. LLC

Well, thanks. It's great on the other side.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

All right. We'll see you later. Okay. Bye.

Disclaimer

The information herein is based on sources we believe to be reliable but is not guaranteed by us and does not purport to be a complete or error-free statement or summary of the available data. As such, we do not warrant, endorse or guarantee the completeness, accuracy, integrity, or timeliness of the information. You must evaluate, and bear all risks associated with, the use of any information provided hereunder, including any reliance on the accuracy, completeness, safety or usefulness of such information. This information is not intended to be used as the primary basis of investment decisions. It should not be construed as advice designed to meet the particular investment needs of any investor. This report is published solely for information purposes, and is not to be construed as financial or other advice or as an offer to sell or the solicitation of an offer to buy any security in any state where such an offer or solicitation would be illegal. Any information expressed herein on this date is subject to change without notice. Any opinions or assertions contained in this information do not represent the opinions or beliefs of FactSet CallStreet, LLC. FactSet CallStreet, LLC, or one or more of its employees, including the writer of this report, may have a position in any of the securities discussed herein.

THE INFORMATION PROVIDED TO YOU HEREUNDER IS PROVIDED "AS IS," AND TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, FactSet CallStreet, LLC AND ITS LICENSORS, BUSINESS ASSOCIATES AND SUPPLIERS DISCLAIM ALL WARRANTIES WITH RESPECT TO THE SAME, EXPRESS, IMPLIED AND STATUTORY, INCLUDING WITHOUT LIMITATION ANY IMPLIED WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, ACCURACY, COMPLETENESS, AND NON-INFRINGEMENT. TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, NEITHER FACTSET CALLSTREET, LLC NOR ITS OFFICERS, MEMBERS, DIRECTORS, PARTNERS, AFFILIATES, BUSINESS ASSOCIATES, LICENSORS OR SUPPLIERS WILL BE LIABLE FOR ANY INDIRECT, INCIDENTAL, SPECIAL, CONSEQUENTIAL OR PUNITIVE DAMAGES, INCLUDING WITHOUT LIMITATION DAMAGES FOR LOST PROFITS OR REVENUES, GOODWILL, WORK STOPPAGE, SECURITY BREACHES, VIRUSES, COMPUTER FAILURE OR MALFUNCTION, USE, DATA OR OTHER INTANGIBLE LOSSES OR COMMERCIAL DAMAGES, EVEN IF ANY OF SUCH PARTIES IS ADVISED OF THE POSSIBILITY OF SUCH LOSSES, ARISING UNDER OR IN CONNECTION WITH THE INFORMATION PROVIDED HEREIN OR ANY OTHER SUBJECT MATTER HEREOF.

The contents and appearance of this report are Copyrighted FactSet CallStreet, LLC 2023 CallStreet and FactSet CallStreet, LLC are trademarks and service marks of FactSet CallStreet, LLC. All other trademarks mentioned are trademarks of their respective companies. All rights reserved.