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EDITED TRANSCRIPT

CPB - Q3 2014 Campbell Soup Company Earnings Conference Call

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OVERVIEW:

Co. reported YTD net sales from continuing operations of $6.416b, adjusted earnings from continuing operations of $645m and adjusted EPS from continuing operations of $2.04. 3Q14 net sales from continuing operations were $1.97b, adjusted earnings from continuing operations were $195m and adjusted EPS from continuing operations was $0.62. Expects FY14 sales from continuing operations will grow approx. 3%.

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Campbell's Soup third-quarter 2014 earnings conference call.

(Operator Instructions)

As a reminder, this conference call is being recorded. I'd now like to introduce your host for today's conference, Jennifer Driscoll, Vice President - Investor Relations. Please go ahead.

Jennifer Driscoll - *Campbell Soup Company - VP IR*

Thanks, Kate. Hello, everyone. Welcome to the third-quarter fiscal 2014 earnings call and webcast for Campbell Soup Company. With me here in New Jersey today are Denise Morrison, President and CEO; Anthony DiSilvestro, our new Chief Financial Officer; and Anna Choi, Senior Manager of Investor Relations.

I'm going to comment first on items impacting comparability in the quarter. Denise will follow me with a high-level perspective on our third quarter. Anthony will wrap it up with a more detailed look at the financial and segment results as well as our guidance. After that we'll take your questions.

As usual, we've created slides to accompany our earnings presentation. You will find the slides posted on our website this morning at investor.campbellsoupcompany.com, and on our IR app, which is available through Google or Apple. Please keep in mind that this call is open to the members of the media who are participating in listen-only mode.

Our presentation today includes forward-looking statements which reflect the Company's current expectations about future plans and performance. These forward-looking statements rely on a number of assumptions and estimates which could be inaccurate and are subject to inherent risks. Please refer to slide 3 in the presentation or to the Company's most recent Form 10-K and subsequent SEC filings for a list of the factors that could cause our actual results to vary materially from those anticipated in any forward-looking statement.

Now for those items impacting comparability, our discussion of the third quarter will exclude an $18 million pretax pension settlement charge associated with the US pension plan. In fiscal 2014, we recorded pretax restructuring charges of $14 million to streamline business operations in China. In the first quarter, we recorded pretax restructuring charges and related costs of $23 million to streamline our salaried workforce in North America and our workforce in the Asia-Pacific region, and for previously announced initiatives.

Our discussion of year-to-date results will also exclude restructuring charges, a loss on foreign exchange forward contracts, and a tax expense related to the sale of our European business in the current year. Last year we recorded $21 million of pretax restructuring charges and related costs in the third quarter and $48 million in the second quarter, related to our US supply chain structure and the manufacturing and distribution capabilities in Mexico. In the first quarter of fiscal 2013, we recorded $43 million of restructuring charges and related costs associated with the US supply chain initiatives, and $10 million of transaction costs associated with the Bolthouse acquisition.

Since our presentation includes non-GAAP measures as defined by SEC rules, we've provided a reconciliation of the measures to the most directly comparable GAAP measures as an appendix to the slides accompanying our presentation. These slides, along with our earnings release and selected quarterly financials, also can be found on our website accessible by computer or on your mobile device with the Campbell IR app.

I've got one more thing to plug. We'd like to cordially invite our sell side analysts, and the buy side, to our annual Investor Day at Campbell world headquarters. This year's event will be held in the morning of July 22, a Tuesday, and will feature presentations by Denise Morrison, Anthony DiSilvestro and several other Campbell leaders. We will unveil our innovations for the next year, outline our new beverage strategy, describe plans for soup, and provide a tasty luncheon featuring Campbell products. We hope you'll join us either via webcast or better yet live at our world headquarters here in Camden, New Jersey. RSVPs are required for those attending in person.

With that let me turn it over to Denise.

Denise Morrison - *Campbell Soup Company - President and CEO*

Thank you, Jennifer. And welcome, everyone. Thanks for joining Campbell's earnings call.

Our sales results for the quarter were mixed. Sales in US Simple Meals grew 7%, powered by strong top-line performance in our sauce business. Plum Organics added 4 points to our sales growth in Simple Meals. Bolthouse Farms delivered 6% top-line growth over the prior year.

Biscuit sales in Asia-Pacific grew, driven by double-digit growth in Indonesia. However, we did not grow our US Soup business and experienced sales declines in US beverages, Pepperidge Farm and our business in Australia.

Overall, organic net sales grew 1%, which was 1% below our expectations. And I'm disappointed that we failed to deliver the sales growth that we anticipated in the third quarter. We believe this is in part a reflection of the persistence of an exceptionally challenging consumer environment.

As many others in the industry have noted, consumers are suffering from continuing under-employment, reductions in the SNAP Program and rising home, fuel, and healthcare costs. In combination, these factors are significantly affecting purchasing behavior, pressuring the performance of a number of our key customers, and constraining growth across the industry, particularly in center store categories

Our adjusted EBIT increased 12% in the third quarter, reflecting lower administrative expenses, including lower incentive compensation costs and our cost reduction efforts. This was more than sufficient to offset the impact of a reduced gross margin percentage and deliver positive EBIT performance.

Following our strong results in the second quarter, we reaffirmed our external guidance for the fiscal year, which called for sales growth of 4% to 5%, adjusted EBIT growth of 4% to 6%, and adjusted EPS growth of 2% to 4%. As we communicated at the time, achieving this level of performance was predicated on improving our marketplace performance relative to the first half. Unfortunately, our performance in US Soup did not improve in Q3 and sales at Pepperidge Farm were below expectations.

Consequently, we are lowering our sales guidance for the full year to 3% growth. We are maintaining our previous full-year guidance on earnings. However, we are refining our estimates to the low end of the 4% to 6% range for adjusted EBIT growth, and the low end of the 2% to 4% range for adjusted EPS growth.

Let me offer some perspective on our performance in the quarter. Sales in US Soup were comparable to the strong year-ago quarter when sales increased by 14%. Within Soup, broth sales grew 14%, but condensed soup and RTS soup posted declines.

Within Soup, we have been refining how we optimize all drivers of demand. In the third quarter, we redeployed funds from advertising and consumer promotion to support increased trade promotion activity. We held our promoted price points and increased promotional frequency, extending across a broader customer base. While we executed the programs effectively, the enhanced trade promotion did not yield the anticipated lift in volume.

In addition to a strong promotion plan, we introduced eight new soups in January under an accelerated time frame, including pub-inspired Chunky, Healthy Request, and Latin-inspired condensed soups. On balance, they generated the sales we had anticipated. However, all of this activity did not generate the incremental sales that we had expected.

Overall, dollar consumption in the US Soup category has declined marginally year to date, and our share has remained relatively stable. I can assure you that we are examining the same questions that you are, and we are formulating the most effective responses for next season.

Within Simple Meals, we did have some bright spots. Our broth, condensed cooking soups and sauces grew nicely. The common thread with these products is that consumers are combining them with fresh ingredients to prepare home-cooked meals.

Prego's growth got a significant boost from our expanding line of white sauces and innovation with red distinctive sauces. Campbell's Skillet Sauces and new Slow Cooker Sauces in pouch packaging have now achieved 76% ACV distribution, with 60% of retailers giving this new segment a dedicated section in the store. Sales continue to build as expected for those products.

Our goal remains to increase our competitiveness and profitably grow our core business. I feel that our Simple Meals business remained competitive in the third quarter, despite falling short of our top-line expectations in Soup.

Turning to Global Baking and Snacking, Pepperidge Farm sales were softer than anticipated. Goldfish Crackers achieved modest sales growth of 2%, boosted in part by Goldfish Puffs, which are performing well. Goldfish Crackers grew sales on the back of increased promotions in a very competitive environment, and gained momentum as the quarter progressed.

However, we saw a significant slowdown in the overall cracker category and a decline in our adult savory crackers, which impacted our overall snacks results. We have reformulated and relaunched our adult savory crackers as Pepperidge Farm cracker chips and expect better performance going forward.

Pepperidge Farm cookies had a weaker than expected performance, also wrapping a strong year-ago quarter. Pepperidge Farm bakery grew as we maintained our shelf space and increased sales of sandwich rolls and buns. It is evident that we have held our own despite the reentry of Hostess in the marketplace.

Internationally we continued to deliver double-digit growth in Indonesia. During the quarter, we remained focused on stabilizing our Arnott's Biscuit business in Australia for the long term. The Kelsen acquisition at the start of the fiscal year has given us a growth platform for biscuits in China and Hong Kong. Kelsen is tracking with our expectations.

Turning to our US Beverage business, we said before it wouldn't be a growth engine this year. The shelf-stable beverage category continued to be pressured by competition from a growing array of packaged, fresh and specialty juices.

We were encouraged by the third-quarter performance of our V8 Red 100% vegetable juice, which has now delivered sales growth for four consecutive months. Our V8 energy drinks continued their strong growth trajectory. But V8 V-Fusion and V8 Splash declined.

In single-serve, we continued to make progress in building our new national distributor network for immediate consumption channels. We plan to discuss our new strategy to revitalize US Beverages at Campbell's Investor Day in July.

Bolthouse Farms is on track to deliver the second half growth that we expected. Third-quarter sales of premium refrigerated beverages and salad dressings grew double digits. Bolthouse Farms is launching its spring innovation suite of 47 new products, ranging from new stone fruit and root vegetable juices to delicious Greek yogurt salad dressings. We made a decision this year to make our first investments in Bolthouse Farms advertising, and we're pleased with the market share, volume trends and brand awareness.

Our acquisition of Plum Organics enabled us to enter the fast-growing organic segment of the US baby food category. In the second half, we expected Plum to show improvement with the full product range back in supply, expanding distribution and introducing several new products. It has done so. We continue to believe that Plum is a well-positioned, on-trend brand that is an excellent fit with our $1 billion portfolio of foods that appeal to children.

Before I turn the call over to Anthony, I want to share a few final observations about the third quarter and our strategy. We said in the second quarter that we expected gross margin in the second half to be flat. However, in the third quarter our gross margin was negatively impacted by lower sales volume because our trade spending did not result in the expected sales increases. Finally, our continuing focus on disciplined cost management is making a difference on the bottom line, as we delivered third-quarter earnings growth in a very competitive environment.

To sum up, we are making no excuses for our disappointing sales. We own the results. Our third-quarter sales did not meet our expectations or yours. But our team remains resolutely focused on executing our dual mandate to strengthen our core business and expand into higher-growth spaces.

We have no illusions about the challenges that we're facing in a tough environment. We are not alone in that regard. Which is why we're also focused on driving growth through four bold moves -- delivering breakthrough innovation, building our presence in packaged fresh foods, increasing availability in faster growing channels, and expanding in developing markets.

We believe that we have the right long-term strategy to deliver sustainable, profitable net sales growth and build shareholder value. We continue to reshape Campbell to respond to the seismic shifts in our industry and meet the evolving needs of increasingly diverse consumers. We've come far since our journey began in 2011. And I look forward to sharing more details about the next steps on our strategic path at Campbell's Investor Day on July 22.

Thank you. I look forward to answering your questions in a few minutes. Now I'd like to turn the call over to Anthony DiSilvestro, our new CFO.

Anthony DiSilvestro - *Campbell Soup Company - CFO*

Good morning. And thanks, Denise. Before getting into the details, I wanted to give some perspective on our results and guidance.

As you'll see, the shape of our P&L reflects a shift within our marketing programs. While total marketing, which includes advertising, consumer and trade, is up for both the quarter and the year, we have redeployed funds from A&C to support increased trade promotions. This is reflected on the P&L as a lower gross margin percentage with an offset in lower A&C expense, which we report in our marketing and selling line.

The second item I want to highlight is the significant reduction in our administrative expenses. Because our fiscal 2014 results are below our expectations, we are accruing incentive compensation below targeted levels. Lower pension expense and the savings from our recent restructuring initiatives are also contributing to this decline in administrative costs.

Lastly, we are reducing our guidance for sales growth. As Denise mentioned, in our US Soup business we increased our promotional activity. However, we did not realize the anticipated volume lifts.

Additionally, in Pepperidge Farm, our volumes have been impacted by increased competitive activity in the snacks category. And in response, we have also increased our promotional spending. As a result of these two issues, we are lowering our expectations for full-year sales growth to approximately 3%.

Now I'll review our results. I'll start with our third-quarter results and segment highlights, followed by a brief look at our year-to-date results and then wrap up with our full-year guidance. As Jennifer mentioned, my discussion of results will exclude items impacting comparability.

For the third quarter, we reported net sales from continuing operations of $1.970 billion, comparable to the year-ago quarter. As Denise mentioned, we were disappointed with our sales in the quarter as US Soup and Pepperidge Farm sales were below our expectations.

Our sales results include a 2 point contribution from our Kelsen and Plum Organics acquisitions. Excluding acquisitions and the negative impact of currency, organic net sales increased by 1%, driven by gains in our US Simple Meals and our Bolthouse and Foodservice segments, partly offset by declines in International Simple Meals and beverages and in US Beverages. The organic sales increase was on top of last year's 4% gain.

Adjusted EBIT increased 12% to $310 million. The increase was driven by lower administrative expenses. Lower marketing expenses offset the lower gross margin percentage which reflected higher promotional spending. Adjusted earnings per share were $0.62, a 7% increase versus the prior year, reflecting the EBIT growth, partly offset by a higher tax rate.

The next slide shows the composition of our sales performance. The organic sales increase of 1% reflects 2 points of favorable volume mix and 2 points of growth from higher selling prices, partly offset by 3 points from increased promotional spending. Unfavorable currency had a 2 point impact due to the Australian and Canadian dollars weakening against the US dollar, while acquisitions added 2 points.

The favorable volume mix is driven by our US Simple Meals and our Bolthouse and Foodservice segments. The pricing gains were primarily related to our list price increases on US condensed soup and in our Global Baking and Snacking segment. The promotional spending variance was primarily related to higher rates of spending in Global Baking and Snacking and US Simple Meals.

Our adjusted gross margin percentage declined by 1.8 points to 35.2%. Of the decline, 1.2 points came from the base business, and 60 basis points was the impact of acquisitions. Excluding acquisitions, the decline in gross margin was primarily due to higher promotional spending, increased supply chain cost and cost inflation, partly offset by productivity improvements and higher selling prices.

Our margin performance was below our expectations, reflecting the lower than projected sales lift from promotional spending and increased supply chain costs. In North America, cold weather was a key cost driver as it disrupted the distribution and warehousing network, as well as impacting our plant performance.

The rate increase in cost of goods sold was approximately 4% in the quarter, including about 2 points from inflation and the balance from higher supply chain costs. This increase was partly offset by productivity savings. Looking ahead, inflation and cost of goods sold for the year continues to be estimated at 3% to 4%.

Marketing and selling expenses for the quarter decreased $28 million to $217 million. The decrease was primarily due to lower A&C expenses and the negative impact of currency. Excluding acquisitions, A&C for the quarter fell 19%, and was down 5% year to date, while total marketing including trade spending increased for both periods. Administrative expenses decreased $30 million to $134 million, primarily due to lower incentive compensation costs, lower pension and healthcare expenses, and cost savings from recent restructuring initiatives, partly offset by the impact of acquisitions which added approximately $6 million.

Now let's look at below-the-line items. For the quarter, net interest expense decreased $1 million to $30 million. The adjusted tax rate for the quarter was 30.7%, a 4 point increase versus the prior year.

The prior year benefited from lower taxes on foreign earnings and the favorable settlement of certain state tax matters. Reflecting the higher tax rate, adjusted earnings from continuing operations increased 7% to $195 million.

Third-quarter segment sales results and organic growth rates are shown on the next slide. Our US Simple Meals segment delivered $672 million in sales, including a $24 million contribution from the acquisition of Plum Organics. US Simple Meals organic sales increased by 3%.

Within this segment, US Soup sales were comparable to a strong prior-year quarter that saw soup sales increase by 14%. Consumer take-away in measured channels was down 2% in the quarter. We ended the quarter with inventory levels higher than last year, due to the late holiday timing.

Excluding the impact of the Plum acquisition, US saw organic sales increase by 11%. The increase was driven by gains in Prego pasta sauce, which benefited from the introduction of Prego white sauces, Campbell's dinner sauces and Pace Mexican sauces.

Our Global Baking and Snacking segment delivered $564 million in sales, including a $17 million contribution from Kelsen. Organic sales were comparable to the prior year, with growth in Arnott's offset by declines at Pepperidge Farm. Sales gains at Arnott's were driven by strong growth in Indonesia, partly offset by declines in Australia from savory and sweet varieties.

The sales decline in Pepperidge Farm reflected declines in frozen products and snacks, partly offset by growth in fresh bakery. Within snacks, declines in adult cracker varieties and Pepperidge Farm cookies were partly offset by increases in Goldfish snack crackers.

Our Bolthouse and Foodservice segment posted $358 million in sales, an increase of 4%. Sales rose 6% at Bolthouse Farms, driven by double-digit gains in premium refrigerated beverages and salad dressings. Organic sales in North America Foodservice increased compared to the prior year.

US Beverage sales declined by 4% to $190 million. The decrease in sales was driven by declines in V8 V-Fusion and V8 Splash beverages, partially offset by volume gains in V8 vegetable juice. While sales of V8 V-Fusion declined, our +Energy product has achieved significant growth.

International Simple Meals and Beverages delivered $186 million in sales for the quarter. Organic sales decreased by 7%. Sales declined in Latin America, the Asia-Pacific region, and Canada.

The sales decline in Latin America was primarily due to lower volumes and lower selling prices associated with the implementation of the new business model in Mexico. Sales in the Asia-Pacific region decreased due to declines in Australia and Japan, partially offset by gains in Malaysia. Sales in Canada decreased on declines in beverages, partly offset by gains in both snacks and soup.

Operating earnings for US Simple Meals increased 12% to $175 million. Operating earnings increased primarily due to lower marketing and administrative expenses, partially offset by a lower gross margin percentage.

Operating earnings for Global Baking and Snacking decreased 7% to $68 million, primarily due to Kelsen Group's off-season operating results. Excluding Kelsen, operating earnings decreased slightly as lower earnings in Arnott's and the favorable impact of currency were partly offset by earnings growth in Pepperidge Farm.

Operating earnings for US beverages decreased by 12% to $29 million. The decrease in operating earnings was primarily driven by cost inflation, increased supply chain cost, and higher marketing expenses, partly offset by lower administrative expenses and productivity improvements.

In the International Simple Meals and beverages, operating earnings were $27 million, a decline of 4%. The decrease in operating earnings was primarily due to lower volumes, partly offset by lower administrative and selling expenses. Operating earnings within Bolthouse and Foodservice declined by 15% to $23 million. The decrease in operating earnings was primarily due to cost inflation and increased promotional spending and advertising in Bolthouse Farms, partly offset by higher volumes and lower administrative expenses.

On the next slide, you can see US Soup sales were comparable to the prior-year quarter. Sales of condensed soups decreased 3%, with sales declines in eating varieties partly offset by gains in cooking soups. Lower volumes were partly offset by higher selling prices net of higher promotional spending.

Ready-to-serve soup sales declined 1% with declines in both canned and microwavable varieties. Broth had a strong quarter as sales increased 14%, driven by double-digit volume gains in aseptic varieties.

US Soup sales for the first nine months decreased 1%. The decrease reflects a 4% decline in ready-to-serve soups and a 2% decline in condensed soups, partly offset by an 11% increase in broth.

Let's take a look at US wet soup category performance in the past 52 weeks and our share performance as measured by IRI. For the period ending April 27, 2014, the category as a whole declined 0.6%. Our sales in measured channels declined 1.1%, with weakness in condensed and ready-to-serve soups partly offset by strength in broth. Campbell had nearly a 60% market share, a decrease of 30 basis points in the period. All other branded players collectively had a share of 28%, with private label at 13%.

For the nine months, net sales from continuing operations were $6.416 billion, up 1% from the prior year. These sales results include a 4 point contribution from acquisitions, which consist of Plum Organics, Kelsen acquired on August 8, and one additional week of results from Bolthouse Farms, which closed one week into the first quarter a year ago. Excluding acquisitions, and the negative impact of currency, organic net sales were comparable to the prior year.

Gains in Bolthouse and Foodservice, US Simple Meals, and the Global Baking and Snacking segments were offset by declines in US beverages and in International Simple Meals and Beverages. Adjusted EBIT of $1.022 billion was comparable to the prior year as lower administrative expenses were offset by lower gross margin percentage. Adjusted earnings per share of $2.04 were comparable to a year ago.

For the first nine months, sales grew 1%, with organic sales comparable to the prior year as the impact of higher selling prices was fully offset by higher promotional spending. Acquisitions added 4 points while currency subtracted 2 points.

Our adjusted gross margin percentage declined by 1.8 points to 35.6%. The decline in gross margin was primarily attributable to cost inflation, higher promotional spend, increased supply chain cost, and the impact of acquisitions, including the November 2013 Plum Organics recall, partly offset by productivity improvements and higher selling prices. The increase in cost of goods sold was approximately 4% for the first nine months, partly offset by productivity savings of 3%.

Marketing and selling expenses decreased 1% to $746 million. The decrease was primarily due to lower advertising and consumer promotion expenses, the impact of currency and lower marketing overhead expenses, partly offset by the addition of acquisitions. Administrative expenses decreased $58 million to $424 million, primarily due to lower incentive compensation costs, lower pension and healthcare expenses, and cost savings from recent restructuring initiatives, partly offset by the impact of acquisitions which added approximately $16 million.

For the first nine months, net interest expense decreased $6 million to $89 million. The decrease was primarily due to lower interest rates on our debt portfolio. We expect to finish the year with net interest cost of about $120 million.

The adjusted tax rate for the first nine months was 31.3%, a 50 basis point increase versus the prior year. The prior year benefited from the favorable settlement of certain state tax matters. We continue to expect a tax rate for fiscal 2014 of 31% to 32%.

Adjusted earnings from continuing operations decreased 1% to $645 million. Adjusted earnings per share from continuing operations of $2.04 were comparable to the prior year. Cash flow from operations was $763 million, compared with $864 million in the prior year. The decline was primarily due to lower cash earnings and the taxes paid on the divestiture of the European Simple Meals business, partly offset by lower working capital requirements.

Capital expenditures of $198 million decreased from $205 million a year ago. We are still expecting capital expenditures for the year to be approximately $350 million. Net debt decreased by $113 million to $3.687 billion.

We have revised our full-year guidance for fiscal 2014. We now expect that sales from continuing operations will grow approximately 3% compared with the previous range of 4% to 5%, reflecting the recent shortfall in sales growth from US Soup and Pepperidge Farm. Full-year growth in adjusted EBIT is expected to be at the low end of the previously forecast range of 4% to 6%. And adjusted EPS for the full year is expected to be at the low end of the previously announced guidance of 2% to 4%.

Several items are worth highlighting. Fiscal 2014 comprises 53 weeks, one additional week compared to the prior year. We estimate the extra week will benefit sales growth by about 2%, EBIT growth by approximately 3% and EPS by approximately $0.08. Going the other direction, we expect currency translation will have a 2% negative impact on sales, EBIT, and EPS.

Next, for the full year, we expect incentive compensation costs will be below target levels by approximately $40 million, or $0.08 per share. As you might imagine, this will be a headwind next year, along with the 53rd week.

Two other items we've talked about are the contribution to sales from acquisitions which we continue to project at about $300 million. And in connection with a new business model in Mexico, reported sales in cost of products sold are now expected to be reduced by approximately $30 million.

Thank you. Now I'll turn it back to Jennifer.

Jennifer Driscoll - *Campbell Soup Company - VP IR*

Thanks, Anthony. At this time, Campbell will conduct a Q&A session. We'd like to request that our callers limit themselves to a single question so we can respond to more analysts. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Chris Growe with Stifel.

Chris Growe - *Stifel Nicolaus - Analyst*

Hi, good morning. Let me just ask you first, Denise, in relation to the reduction in revenue growth for the year, it sounds like it was driven by Soup and Pepperidge. So I'm getting that. Is the rationale in the guidance due to the base business or is there any change in your contribution from acquisitions that's occurring as well to bring that revenue guidance down?

Denise Morrison - *Campbell Soup Company - President and CEO*

Chris, to answer your question, there is no change in our expectations on the acquisitions. The reason why we lowered it was because two-thirds of it came from the Soup business and about one-third from Pepperidge Farm.

Chris Growe - *Stifel Nicolaus - Analyst*

Okay. And related to that, in this quarter you had an increase in promotion and you didn't get the response you expected. I'm just curious, is that a comment about the category or a comment about the consumer in terms of them somewhat not responding to the increase in promotional spending? What do you think happened there, is my question?

Denise Morrison - *Campbell Soup Company - President and CEO*

It's a great question. And I have actually looked at the performance of 36 Simple Meals now over the course of time. If you look at the MULO, total refrigerated meals are up 3.3%, shelf stable are up 0.7%, and frozen are down 0.6%.

So what's happening is the refrigerated Simple Meals are experiencing most of the growth. But within shelf stable, there are some categories, like fresh bread and rolls, Italian and Mexican sauces, which are positive, and soup is slightly declining.

If you look at over the last year, the total Simple Meals category is sluggish, up 1.2%, but still positive. So we feel like we're tracking right with the pack here, it's just that the environment is tough.

Chris Growe - *Stifel Nicolaus - Analyst*

Okay. Thank you for the time.

Operator

Robert Moskow with Credit Suisse.

Robert Moskow - *Credit Suisse - Analyst*

Thank you. Denise, we weren't modeling very much growth in Soup in the quarter, merely because the comp was so hard. It was a 14% comp. But it looked like your business plans really did depend on a lot of volume growth on top of what last year was a lot of volume growth.

So, what made you think that in this consumer environment and then in a tight inventory environment at retail -- were the plans that robust that that was possible?

Denise Morrison - *Campbell Soup Company - President and CEO*

We got off to a slow start in the first quarter. We deployed extra promotional activity into the third quarter, beyond what we had last year. And, in addition, we introduced eight new SKUs of soup in January, which was something we don't usually do, but we felt that they were ready and we could use the sales volume to bring us out of the first-quarter slump.

Quite frankly, we were happy that we at least held our own versus the 14%. And over a two-year period we're up high single digit in soup, except that it just wasn't enough to meet the expectations that we needed to bring the quarter in and bring our full year in on our guidance. So that's the best explanation. Anthony, do you want to add?

Anthony DiSilvestro - *Campbell Soup Company - CFO*

Yes, I would just add one point to that which I think is important. On soup, we held our promotional price points. And what we did is we expanded to a broader customer base. So, we went to customers this year that we didn't promote with in the third quarter last year, which gave us some of confidence that we thought we'd get a volume lift.

Robert Moskow - *Credit Suisse - Analyst*

So, more customers got the deals. I got it. Any implications for pricing for next year? I know that some of your commodities are up. Have you announced any pricing for Soup?

Anthony DiSilvestro - *Campbell Soup Company - CFO*

No, we haven't announced any pricing for Soup.

Robert Moskow - *Credit Suisse - Analyst*

Okay. Thank you.

Operator

Eric Katzman with Deutsche Bank.

Eric Katzman - *Deutsche Bank - Analyst*

Good morning, everybody. Denise, I want to focus in on the global snacking and baking area. I looked back, and I had to go back to, I think, 2009 to see a quarterly profit that was this weak between Arnott's and Pepperidge. I know that both of those businesses, especially on the cracker side at Pepperidge, and the core Arnott's business are very profitable.

So I'm really worried that those businesses are starting to roll over at the same time that you've continued to have challenges in other areas. Why shouldn't we be particularly concerned? What do you see as the problem for Pepperidge? And how can we have faith that that business isn't going to be a drag versus competition, maybe better or stronger competition in coming quarters?

Denise Morrison - *Campbell Soup Company - President and CEO*

First, let me address Pepperidge Farm. In Pepperidge Farm, we had positive profits, and the profits are actually pretty robust. The two portions of the business that had sales decline were adult savory crackers and frozen, which are actually a small portion of the business.

In addition, we had a price increase on Goldfish last year. And we found that, given the competitive environment, we had to promote that product more in the third quarter.

We did see lift improving as the quarter went on. So, we do believe that Pepperidge Farm is still a great business, in really good shape.

When it comes to Arnott's, we've been dealing with a very tough retailer environment in Australia. And we have had to invest in that business to stabilize it and return advertising to our core brands, like Tim Tam Shapes and Real Stock. We have had profit hits in Australia. We recognize that.

But we believe that getting that business back to stability is important. It's an important business for us. These are great brands and they have great expansion possibilities, as demonstrated by our double-digit growth in Indonesia. So I hope that answers your question.

Eric Katzman - *Deutsche Bank - Analyst*

I'll pass it on. Thank you.

Operator

Matthew Grainger with Morgan Stanley. Your line is open.

Matthew Grainger - *Morgan Stanley - Analyst*

Hi. Good morning everyone. Denise or Anthony, you're obviously in the midst of integrating a number of acquisitions right now. But given that the M&A environment seems to be heating up a bit, I just wanted to revisit where you see yourself in this process of portfolio transformation, how you'd assess the landscape right now, and how you balance that with addressing some of the base business issues. And do the base business trends having been below your expectations year to date reinforced the urgency of needing to evolve the portfolio faster?

Denise Morrison - *Campbell Soup Company - President and CEO*

We've always held ourselves to a standard since the very beginning of strengthening our core business, while we expand into faster growing spaces. And we will continue to do both of those.

We have been making plans and investments in our core business. And the three acquisitions that we made have been very good for our portfolio. And, yes, we will continue to look for other acquisitions with smart external development that make good strategic sense.

Matthew Grainger - *Morgan Stanley - Analyst*

Okay. Thank you, Denise.

Operator

David Driscoll with Citi.

David Driscoll - *Citigroup - Analyst*

Great. Thank you. Good morning. Anthony, I just want to make sure I heard something right. It's a clarification. On the admin expense line I think you quantified that incentive compensation for the full year was down about $0.08 or $40 million. First off, did I get that right?

Anthony DiSilvestro - *Campbell Soup Company - CFO*

Yes. What I said is our incentive compensation relative to targeted levels is $0.08 favorable.

David Driscoll - *Citigroup - Analyst*

That's what I meant but that was much better said. So, thank you.

And then the big question then is, on 2015, you're saying that that's got to get restored, and so that's something like a 3 percentage point headwind. And then from the 53rd week itself, there's another, I think, 2 percentage point headwind.

So out of the gate with no other information, there's a 5 percentage point headwind against FY15 numbers that we can state is there today. Is that fair and accurate?

Anthony DiSilvestro - *Campbell Soup Company - CFO*

Actually, it's 1 point worse than you stated. At EBIT it's 3 points for each of them. Because, as I said, a 53rd week, it's 2 points at sales and 3 points at EBIT.

Going the other way, we've got a couple things. We're wrapping the Plum Organics recall and we're wrapping a very disruptive winter. We know we have some challenges next year. We're working through our plans now in terms of operating plans for next year to see where we come out.

David Driscoll - *Citigroup - Analyst*

Okay. Thank you for that. It seems the implications are clear on that issue. Thank you.

Operator

Ken Goldman with JPMorgan.

Ken Goldman - *JPMorgan - Analyst*

Hi, guys. One really quick one, then my question. First, how much does 4Q guidance incorporate an expectation of an inventory drawdown? And then my longer question, can you update us on your expectations for the California drought for FY14? I know you won't give specific guidance there but any directional help or thoughts on the situation given how core it is might be useful. Thank you.

Anthony DiSilvestro - *Campbell Soup Company - CFO*

I can take the first, the soup inventory part of that. We did end the quarter about $25 million up versus year ago on soup inventories. It's hard to predict exactly what it's going to come out, as we launch into next year, but our forecast for the fourth quarter does assume the majority of that inventory comes out.

Denise Morrison - *Campbell Soup Company - President and CEO*

Okay. And regarding the drought, we have held our own pretty much during this drought. Our Bolthouse Farms carrot business resides in fields with aquifers, and they've been growing also in Northern California and some other regions to take some of the pressure off.

So, they've been doing well despite the situation. We are expecting some increases in tomato prices as a result of the drought, but that's been incorporated in our planning.

Ken Goldman - *JPMorgan - Analyst*

Thank you.

Operator

David Palmer with RBC Capital Markets.

David Palmer - *RBC Capital Markets - Analyst*

Good morning, guys. If you were to separate your business drivers into the controllables, like your marketing and innovation, and the factors outside your control in FY14, like the consumer environment, weather disruption, and even factors like the competition you're seeing in healthy snacking, do you see the net impact of the uncontrollables in FY14 as perhaps unusual in a way that creates an easy or difficult comparisons as we think about FY15?

Denise Morrison - *Campbell Soup Company - President and CEO*

The only thing that I can say is that the sales were below our expectation by about 1 percentage point. Some of that was controllable in that the promotions didn't get the lifts that we wanted. But then you could argue you that one of the reasons why we didn't get the lifts was because of a harsher environment and a more cautious consumer. So, I'm not sure how to accurately tease that out.

Anthony DiSilvestro - *Campbell Soup Company - CFO*

I think there's a couple things to point out. Obviously, one, we're wrapping the Plum issue. That obviously is a noncontrollable that will go away.

We expect improved performance in Pepperidge Farm. Denise mentioned we've got two parts of that business that are hurting us this year, which are a small portion. That's the adult savory cracker business and the frozen business.

Then I think more fundamentally, and we've talked about the need to improve our performance in US Beverages and in Arnott's which have been a drag on the portfolio this year and we need to turn that around.

David Palmer - *RBC Capital Markets - Analyst*

Thank you very much.

Operator

Alexia Howard with Sanford Bernstein.

Alexia Howard - *Sanford C. Bernstein & Company, Inc. - Analyst*

Good morning, everyone. There was some data around share trends in US Soup, suggesting that over the last year you've been losing out. Who are you losing share to? Is it your chief competitor? Is it other niche brands? It's clearly not private label. And what do you think you might be able to do differently to address that? Thank you.

Anthony DiSilvestro - *Campbell Soup Company - CFO*

If you look at it, there's been some share gains by some of the niche brands. And I think if you look as to why that is, there are some pockets of growth within the category around things like organic and health and wellness attributes. And obviously we're looking at those things.

We've got a pretty robust plan for soup for next year and some exciting things going on. We plan to share that more fully with you at our Investor Day in July.

Denise Morrison - *Campbell Soup Company - President and CEO*

When you look at share of Simple Meals, we definitely are holding our own against other peers in the set. So, even though Simple Meals is only up slightly, we have maintained our share of that.

Alexia Howard - *Sanford C. Bernstein & Company, Inc. - Analyst*

Great. Thank you very much. I'll pass it on.

Operator

Erin Lash with Morningstar.

Erin Lash - *Morningstar - Analyst*

Thank you for taking my question. I wanted some additional detail, or I was hoping you could give me some additional details regarding the new products that you've been bringing to market, and how those are either resonating relative to plan and what potentially you can do differently, if you can address that. I know this is something you're going to talk about at the Analyst Day but any additional insights you might have would be helpful.

Denise Morrison - *Campbell Soup Company - President and CEO*

Okay. I think that we've had some really good performance from our new dinner sauce products. We started building a new platform, which was completely disruptive with our first execution of skillet sauces last year. We added new slow cooker sauces to that. And then next year we're adding new oven sauces. And we've been successful in getting a destination set in the stores to give the consumer a specific place to shop for these sauces.

I think one of the reasons why they're doing well is because obviously they're consumed with meat and fresh food. We're finding a lot of home preparation these days. So those have done very well.

Goldfish Puffs have done really well and are meeting our expectations. Not so well were the Pepperidge Farm cracker chips and Jingos! which is one of the things that we're cycling in that business this year. But we have reformulated the cracker chips and have better expectations for those going forward.

Erin Lash - *Morningstar - Analyst*

What about within Soup specifically?

Denise Morrison - *Campbell Soup Company - President and CEO*

In Soups, most of the innovation has been sustaining innovation. The new pub-inspired Chunky soups are doing really well. The broth is doing phenomenal where we've moved from just chicken, beef and vegetable into more flavorful broths with recipes to go along with that. And then the new eight SKUs that we introduced in January are performing as expected.

Erin Lash - *Morningstar - Analyst*

Great. Thank you. That's helpful.

Operator

Jason English with Goldman Sachs.

Jason English - *Goldman Sachs - Analyst*

Good morning, folks. Thanks for taking the question. Denise, at a high level, you're reallocating money into trade promo, out of marketing. You're not alone. The entire industry has been moving this way over the last few years. And, as we do this, we just see promotional efficacy continue to step lower and lower and lower.

We're not really dealing with expandable consumption categories here. So, at what point do we say enough's enough, quit trying to throw money at this? And is there a path on the horizon to actually get this money back out? Because it's a lot easier to pour money into trade, it's a lot harder to retract it once retailers have their hands on it.

Denise Morrison - *Campbell Soup Company - President and CEO*

We are continuing to work with all of the levers of drivers of demand, which vary by business. We are working, as well, with customers for more trade promotion effectiveness.

And our business leaders need to be flexible to make course corrections along the way, both to capitalize on opportunities or meet competition. And in several of these categories, we have seen a ramp-up of competition. What we've tried to do is increase our frequency, not go into deep discounting.

Jason English - *Goldman Sachs - Analyst*

Okay. Coming back on a couple more tactical themes, Arnott's, it was my view coming into this year that this should be a year of profit recovery as you implement the automation in your manufacturing network in the market. Based on results, it looks like all those savings, and then some, are being plowed back into the market. Is that indeed the case?

Anthony DiSilvestro - *Campbell Soup Company - CFO*

That's primarily the case. But one point I would add. We experienced some delays in achieving those savings. So, we didn't get the full amount of savings in the year. So, that should help us going into next year.

Denise Morrison - *Campbell Soup Company - President and CEO*

I think the other thing I would add is we've completely changed the team in Australia. They have a new plan that they're implementing which is calling for investment, particularly in the power brands. And we believe that's the right thing to do for that business right now.

Jason English - *Goldman Sachs - Analyst*

Makes sense. Last one and I'll pass it on -- encouraging to see North America Foodservice volume return to growth. I know you brought on some new capacity, new technology for you late last year. Has much of that been deployed yet?

Anthony DiSilvestro - *Campbell Soup Company - CFO*

I would say some of it's been be deployed. The major driver of the improvement in North America Foodservice has actually been our traditional up and down the street Foodservice business.

Jason English - *Goldman Sachs - Analyst*

Got it. Okay. Thanks a lot, guys. I'll pass it on.

Operator

Diane Geissler with CLSA.

Diane Geissler - *CLSA Limited - Analyst*

Good morning. I wanted to follow on Eric's questions earlier about the baking. Just more broadly, could you talk a little bit about your viewpoint on snacking?

It seems like Pepperidge Farm is one of those brands where you would think it was strong enough to carry a volume lift. And yet we continue to see a move away from grain-based products due to shifts in the consumer diet. So, could you talk a little bit more broadly about snacking and carbs versus protein and what you're seeing with the consumer base, please? Thank you.

Denise Morrison - *Campbell Soup Company - President and CEO*

There is no question that within snacking, we have seen -- and I'm talking about macro snacking -- we have seen brands in the better-for-you space gaining traction. One of the reasons why we introduced Goldfish Puffs, in addition to attracting teens and tweens into the Goldfish franchise, was that we were able to make that product gluten free. So we are participating in that macro snacking at this point.

I do believe, though, that our cookie business and our Pepperidge Farm cracker business, particularly Goldfish, do have a nice, loyal consumer base. And we'll continue to innovate in that space, as well. Our model is to give consumers choices, depending upon what they're seeking to buy.

Diane Geissler - *CLSA Limited - Analyst*

Okay. All right. Thank you.

Denise Morrison - *Campbell Soup Company - President and CEO*

And our last question will be from Akshay, I think?

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

Yes, thanks for taking the question. One quick one on the financials. Just can you update us on your gross margin expectation now? I know you've come in below what you were projecting at the beginning of the year. Could you just help us with the drivers of that?

It seems like promotional costs and volumes have come in lower than expected. But maybe give us a sense of where the commodity outlook is and if it has changed.

And, more importantly, just on Bolthouse, you did see 6% growth. But my expectation there is that longer term that's an 8% to 10% top line grower and margins should be expanding. Can you help us understand the performance this quarter, especially at the margin level on Bolthouse that came in well below what I was expecting? Thanks.

Anthony DiSilvestro - *Campbell Soup Company - CFO*

I'll make a couple comments on your gross margin, more about where we've been than the outlook for next year. In terms of this year, we expect cost inflation and the rate to go up about 3% to 4%.

Inside of that, ingredients, packaging and energy inflation running about 2% to 3%. And then you need to add 1 point for the supply chain issues that I mentioned earlier.

If you step back and look at the base business or gross margin decline, as I said in my comments, 60 basis points of that is the impact of the acquisition and 1.2 points is the base business. You're right, promotional variance is a significant factor in that in addition to the inflation that I talked about. We've increased our promotional spending in our baking, snacking business and in US Soup.

And we've also increased trade promotion in Bolthouse Farms, which is one of the reasons you're seeing a lower gross margin or lower margin in Bolthouse. Because in addition to the advertising spend to build the brand awareness, the competitiveness in that category has intensified of late and we have increased our trade spending in response. We don't expect that to be an ongoing issue but it did impact the third quarter, both the top line and the bottom line, for Bolthouse.

Denise Morrison - *Campbell Soup Company - President and CEO*

And Bolthouse year to date is up about 7%. And the beverages and salad dressings are up double digits, both in sales and also in consumption. And the carrots are low single digits.

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

Okay, thank you.

Jennifer Driscoll - *Campbell Soup Company - VP IR*

Thanks, everybody, for participating in our third-quarter earnings call and webcast. If you missed any of the call, the replay will be available about two hours after our call concludes. You may call 703-925-2533 for that. Country code plus 1. The replay access code is 1635565.

You have until June 2, 2014 at midnight, at which point we will move our earnings call to the website, investor.campbellsoupcompany.com under News and Events. Just click on Recent Webcasts and Presentations.

If you are a reporter and have questions, please call Carla Burigatto, Director of External Communications, at 856-342-3737. Investors and analysts should call me, Jennifer Driscoll at 856-342-6081.

This concludes today's program. We hope to see you at our Investor Day in July. You may now disconnect.