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Campbell Soup Co. (CPB)

Q4 2022 Earnings Call

CORPORATE PARTICIPANTS

Rebecca Gardy

Senior Vice President & Chief Investor Relations Officer, Campbell Soup Co.

Mark A. Clouse

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

Mick J. Beekhuizen

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

OTHER PARTICIPANTS

Andrew Lazar

Analyst, Barclays Capital, Inc.

Ken Goldman

Analyst, JPMorgan Securities LLC

Peter T. Galbo

Analyst, Bank of America

Jason English

Analyst, Goldman Sachs & Co. LLC

Robert Moskow

Analyst, Credit Suisse Securities (USA) LLC

MANAGEMENT DISCUSSION SECTION

Operator: Greetings, ladies and gentlemen. And welcome to the Campbell Soup Company Fourth Quarter and Fiscal 2022 Earnings Conference Call. At this time, all participants are in listen-only mode. After today's presentation, there will be an opportunity to ask questions. [Operator Instructions] As a reminder, this conference call is being recorded.

It is now my pleasure to introduce your host, Rebecca Gardy, Chief Investor Relations Officer. You may begin.

Rebecca Gardy

Senior Vice President & Chief Investor Relations Officer, Campbell Soup Co.

Good morning. And welcome to Campbell's fourth quarter full fiscal year 2022 earnings conference call. I am Rebecca Gardy, Chief Investor Relations Officer at Campbell Soup Company. I am joined today by Mark Clouse, Campbell's President and Chief Executive Officer; and Mick Beekhuizen, Campbell's Chief

Financial Officer.

Today's remarks have been prerecorded. Once we conclude our prepared remarks, we will transition to a live webcast Q&A session. The slide deck and today's earnings press release have been posted to the Investor Relations section of our website, campbellsoupcompany.com.

Following the conclusion of the Q&A session, a replay of the webcast will be available at the same location followed by a transcript of the call within 24 hours. On our call today, we will be making forward-looking

statements, which reflect our current expectations. These statements rely on assumptions and estimates, which could be inaccurate and are subject to risk.

Please refer to slide 3 or our SEC filings for a list of factors that could cause our actual results to vary materially from those anticipated in forward-looking statements. Because we use non-GAAP measures, we have provided a reconciliation of each of these measures to the most directly comparable GAAP measure in the appendix of this presentation.

On slide 4, you will see today's agenda. Mark will share his perspective on our fourth quarter and full year performance as well as in-market performance by division. Mick will discuss the financial results of the quarter in more detail and then review our guidance for the full year fiscal 2023.

And with that, I'm pleased to turn the call over to Mark.

Mark A. Clouse

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

Thanks, Rebecca. Good morning, and thank you for joining us today. On behalf of Campbell's leadership, I want to begin by thanking the teams for all their hard work this year. By maintaining focus on the factors we can control, we delivered solid fourth quarter and full year results while advancing our strategic plan to deliver sustainable profitable growth.

The teams executed with excellence across the company. We improved supply chain performance and implemented effective revenue management to counter inflation all while demand for our portfolio of brands remained elevated. Importantly, we did what we said we were going to do. We delivered on the high end of our original full year fiscal 2022 adjusted EPS guidance. We accomplished this despite the volatile environment we're in, and with the momentum we built throughout the year, we're confident in our ability to continue to deliver in fiscal 2023.

Let me start with the fourth quarter. We delivered strong growth across all three key metrics: net sales, adjusted EBIT and adjusted EPS, driven by continued improvement in our supply chain execution, sustained consumer demand and our successful efforts to mitigate inflation.

Organic net sales increased 6% versus the prior year due to net price realization, continued elevated consumer demand and significantly improved supply. Adjusted EBIT and adjusted EPS both returned to growth due to successful inflation mitigation and cost management. For the full year, organic net sales grew 2% and we delivered adjusted EPS of \$2.85. As expected, adjusted EBIT decreased due to challenging inflationary pressures and our commitment to protect critical brand investments.

Our financial results reflect the strong in-market performance of our brands. Fourth quarter consumption was up 8% versus the prior year and up 21% compared to three years ago. For the full year, consumption was up 4% versus the prior year and up 14% versus three years ago. The sustained strength of our portfolio continues to signal great growth potential for the future.

On slide 8, I'd like to talk about a few of the reasons why Campbell's is well positioned for the consumer and economic environment as we head into fiscal 2023. First, our brands are in categories that excel during challenging economic times. Consumers tend to seek out the better value our meals and beverages portfolio delivers while the resiliency of snacking has been consistent in prior economic downturns. Also, we're not solely dependent on pricing to manage inflation.

We've already delivered \$850 million of multiyear cost savings and we're tracking to \$1 billion by fiscal 2025. Our supply chain transformation continues, as well as we address both short-term and longer-term challenges and are performing substantially better than even earlier in the year.

In fact, service levels in the fourth quarter improved by approximately 15 points compared to the first half of fiscal 2022. We've delivered strong innovation with a focus on relevant, differentiated and value-driven platforms. We saw a 2% contribution from innovation in fiscal 2022 and have our most robust pipeline yet for fiscal 2023.

For our US soup business, innovation contributed 3% of net sales in fiscal 2022, demonstrating the opportunity for innovation in this strengthening category. Let me now turn to another strong proof point of our progress, which are the share results for our brands as we emerge from the last three years of the pandemic influence. We're pleased with the fact that share for most of our key brands across our portfolio continue to remain at or above fiscal 2019 levels.

While as we expected in the fourth quarter, we have experienced some select share pressure, this sustained share growth versus pre-pandemic levels is a positive sign that we're emerging with a stronger portfolio of brands as we head into 2023.

Turning to our Meals & Beverage division on slide 10, I continue to be pleased by the performance of our brands. Organic net sales in the division increased 7% versus the prior year, with growth coming across all major meal segments. Consumption grew 8% over the prior year and 22% compared to three years ago, reflecting the underlying health of our portfolio and the strengthening position we've built with new consumers through the pandemic especially with new millennial consumers.

Turning to slide 11. As expected, during tougher economic times, shelf-stable, simple meals grew in importance evidenced by the growth of volume share of total food. The strong value and convenience of categories like pasta sauce and ready-to-serve soup, have driven the segment's outperformance versus both refrigerated and frozen simple meals. This consumer behavior, importantly, among younger households gives us confidence in the continued relevance of our categories heading into fiscal 2023.

Throughout the thoughtful planning and execution of pricing actions in fiscal 2022, we anticipated and appropriately plan for the share pressure we are experiencing from private label, particularly in parts of the portfolio like condensed soup and broth

What is important to remember is the context of the strength of our share positions. Although never happy with share loss in a category where we have a significant share leadership position the strength of the category translates to compelling growth on a very important part of our portfolio.

Further, we've been very focused on which consumers are trading down within soup. And they tend to be our baby boomer consumers, who historically are a bit more sensitive to price gaps and also very likely to trade back over time. The good news is most of our new millennial consumers in soup have been highly brand loyal.

Turning to slide 13. We also are encouraged by our performance on select brands within our soup category that we see as the most imperative to defend our share. Our condensed icons continued to perform well this quarter, with share up 4.1 points and consumption up 29.6% versus the prior year.

On a three-year basis, our condensed icons were up nearly 6 points in dollar share, while also growing units approximately 9%, reflecting our focus on ensuring we are winning on the most strategic parts of our condensed portfolio.

In the ready-to-serve business, Chunky continues to be a star, with dollar share up 1.3 points and consumption up 20.3% versus the prior year. Compared to three years ago, Chunky gained over 2 points of dollar share, increased units nearly 27%, and we've added over 1 million new buyers into the brand.

We are revitalizing the Chunky brand for new generations of consumers, leveraging our 25th season as an NFL sponsor and broadening our relationship with gaming icon, EA Madden, featuring the Campbell's Chunky Stadium.

Innovation will also continue to help fuel our winning soup strategy in fiscal 2023. As consumers trade into shelf-stable meals, like ready-to-serve soup, we're bringing new relevant innovation, targeting better-for-you and flavor profiles that will add variety as frequency in these categories go up.

Building off of the success of our creamy Pacific Foods soups, we're adding to our portfolio of organic ready-to-serve soups and plant-based chilis, which launched in the fourth quarter of fiscal 2022. We're also expanding our new Chunky spicy lineup following the insight that nearly two-thirds of consumers agree that savory foods taste better with spice. Finally, we are providing a full restage of packaging and graphics to continue to fuel the relaunch of our, Well Yes! better-for-you soup line.

Broth is a category where, as expected, private label pressure has been greater. As a result, we continue to further differentiate our Swanson brand. In fiscal 2023, we will be modernizing our packaging and improving our ingredients to drive the taste superiority, quality and value of our Swanson brand.

We will also be launching Swanson Quick Cups, which is a convenient one cup serving of broth, which fits the majority of broth recipe usage occasions. This smaller size offering delivers convenience for smaller households and further delivers value by reducing waste. Through improved quality and a robust lineup of offerings for our consumers, our focus will be on winning this holiday season.

Turning to sauces. We continue to make progress against our goal of building a \$1 billion sauces business. With quick scratch cooking increasing in relevance as consumers continue to eat more at home to save money, we are well positioned to capture market share and growth. In fact, our Prego brand remained the number one share leader in the Italian category for the 39th consecutive month and delivered consumption growth of 12.4% compared to the prior year.

In addition, repeat rates were up 4 points in the quarter compared to three years ago. We are also building on this success by expanding Prego's lineup, as consumers are seeking new elevated flavors and ways to enhance their meals as they cook more at home. Prego's new varieties offer bold and vibrant ingredients to meet the growing need to bring more choices to the in-home Italian sauce experience.

Pace continued to build momentum in the fourth quarter, as we recovered from material shortages that pressured supply earlier in the year, leading directly to share gains in the category. Compared to the prior year quarter, Pace gained 0.4 points of dollar share and grew consumption 14.5%, while repeat rates increased 5.9 points versus three years ago.

Turning to slide 17. As I mentioned earlier, convenience and value are key drivers, especially when paired with the continued strength of quick scratch cooking. In support of these key consumer dynamics, we're fueling that behavior through innovation, with the launch of Campbell's Flavorup concentrated sauces and with the relaunch of Campbell's cooking sauces. Both will expand options and flexibility for dinner variety, especially as consumers look to find ways to incorporate more interesting flavors at home.

For example, with Campbell's FlavorUp!, cooks can control flavor and portions. Plus, given its concentrated form, a home cook can flavor 15 meals in every \$5 package, making it an excellent value that helps stretch consumers' grocery dollars. We will launch this through focused retailer partnerships to methodically build momentum, as we create this new exciting way to cook. We are pleased with our results and our innovation. And we remain poised to deliver our goals of achieving a \$1 billion sauce portfolio.

Turning to our Snacks division on slide 18. The division also had a strong quarter, with organic net sales up 6% over the prior year quarter, driven by our power brands. In-market performance was strong, growing consumption 8% versus prior year and 20% compared to three years ago, fueled also by the performance of our power brands.

We have also now successfully delivered our value capture from the integration. And although we recognize that margins do reflect some of the short-term pressure from inflation and COVID-19, we remain very confident in our plans for further margin expansion in the future. Perhaps even more encouraging is the continued strength of our growing, highly relevant and unique portfolio of power brands.

Taking a closer look at these brands, in-market consumption grew 11% versus the prior year. And on a three-year basis, consumption grew 26%, with double-digit growth across all our power brands versus three years ago. With respect to share, our power brands held dollar share in the quarter versus the prior year, with share gains on Kettle Brand, Cape Cod, Snack Factory pretzel crisps and Pepperidge Farm cookies.

On slide 20, as we indicated last quarter, our improvement in supply chain execution would enable us to invest in our brands through promotional activity in the fourth quarter. We were encouraged to see that our increased support helped drive positive results. We also are continuing to watch unit share very closely on snacking, as we know share of stomach in these categories are very important and provide insight into longer-term growth potential.

The great news is we saw unit share improvement across all our power brands in the fourth quarter versus the third quarter. A particularly competitive segment is total salty snacks, where we were the only major player who grew unit share in the fourth quarter as we've worked hard to keep price and promotion balanced as supply recovered.

Goldfish continues to deliver exceptional results also, driven by relevant innovation and award winning marketing. We continue to shake things up with our limited time-only strategy, building on successful collaborations and flavors with Frank's RedHot and Jalapeño Popper as well as with bold and sweet partnerships with Old Bay and our recently announced Goldfish Dunkin' Pumpkin Spice Grahams.

Since their launch, Frank's RedHot and Jalapeño Popper Goldfish have driven incremental sales of 60% for the Goldfish brand. These two innovations along with Old Bay Seasoned Goldfish were ranked number one in velocity for the cracker category innovations during the launch.

We're engaging consumers in a unique way, coupling our ability to create delicious flavor-driven snacks with strong partnerships and world-class marketing. This is expanding our consumer reach and usage. The latest accolade is that Goldfish was named one of America's Hottest Brands of 2022 by Ad Age.

So in closing, Campbell's enters fiscal year 2023 with strengthened fundamentals, a powerful brand portfolio in advantaged categories, and a proven track record of navigating the continued volatile environment. We remain focused on what we can control, and most importantly, continue to deliver our commitments.

With that, let me turn it over to Mick to discuss our fourth quarter and full year results, and present more details on the fiscal 2023 outlook we provided in our press release this morning.

Mick J. Beekhuizen

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

Thanks, Mark, and good morning, everyone. We are pleased by the strong results we delivered in the fourth quarter in a challenging operating environment. As Mark said earlier, we are proud to have delivered strong full year results, with adjusted EPS at the high end of our original fiscal 2022 guidance range.

This is a testament to the progress our team has made throughout the year in areas such as our supply chain, allowing us to support continued elevated demand levels. Additionally, we have made significant progress regarding inflation mitigation via effective revenue management, continued productivity improvements and cost savings initiatives.

Our cash generation during fiscal 2022 remained strong as well, with cash flow from operations of \$1.2 billion, a 14% increase over prior year. Of which, we returned over \$600 million in fiscal 2022 to our shareholders through dividends and share repurchases.

At the end of my remarks, I'll review our fiscal 2023 guidance. But now, let's first discuss our fourth quarter results in more detail. Turning to slide 25. For the fourth quarter, organic net sales increased 6% as our inflation-driven pricing actions continued to gain traction. Fourth quarter consumption was slightly ahead of our organic net sales performance, driven in part by year-over-year net sales declines in our non-measured channels and due to shipment timing following our July pricing. We now expect inventory replenishment to extend more into Q1.

Adjusted EBIT increased 5% compared to the prior year to \$269 million, primarily due to higher adjusted gross margin, partially offset by higher adjusted administrative expenses and lower adjusted other income.

Our adjusted EBIT margin decreased 20 basis points to 13.5% compared to 13.7% in the prior year. Adjusted EPS from continuing operations increased 8% to \$0.56 per share, driven primarily by the increase in adjusted EBIT and lower net interest expense.

For the full year, organic net sales increased 2% and adjusted EBIT decreased 4% compared to the prior year, resulting in an adjusted EBIT margin decrease of 90 basis points to 15.1%. Our fiscal 2022 adjusted EPS was \$2.85 per share compared to \$2.86 per share in the prior year.

On the next slide, I will break down our net sales performance for the fourth quarter. Net sales in the quarter, both reported and organic, increased 6%, driven by 14 points of inflation-driven pricing. This was partially offset by a 4 points volume and mix headwind and 3 points of increased promotional spending in the quarter, primarily within snacks.

Turning to slide 27. Our fourth quarter adjusted gross margin percentage increased 40 basis points from 30.9% to 31.3%. Net price realization drove an 840 basis point improvement, reflecting the impact of our inflation-driven pricing actions, net of increased promotional spending in the quarter. In addition, our ongoing supply chain productivity program and our cost savings initiatives contributed 150 basis points and 30 basis points to the adjusted gross margin percentage, respectively.

Inflation and other factors had a negative impact of 810 basis points, with the majority of the impact driven by cost inflation as overall input prices on a rate basis increased by approximately 15%, which was relatively consistent with the prior quarter. Lastly, unfavorable volume and mix had a negative impact of 170 basis points in the quarter.

In the fourth quarter, we continued our efforts to mitigate inflation, highlighted on the next page, through a combination of targeted price increases and trade optimization, as well as productivity improvements, primarily in our supply chain, cost saving initiatives and a continued focus on discretionary spending across the organization.

Moving on to other operating items. Adjusted marketing and selling expenses increased \$4 million or 2% and represented approximately 9% of net sales as planned or a 30 basis point decrease compared to last year. The increase in the quarter was driven by higher selling expenses, which were partially offset by lower advertising and consumer promotion expense or A&C.

A&C declined by 3% in the quarter, driven by reductions in our V8 beverage business, where investments were moderated to reflect material availability constraints, offsetting increases in snacks, primarily on Goldfish. Adjusted administrative expenses increased \$14 million or 10% to \$153 million.

The increase in adjusted administrative expenses was driven by higher incentive compensation costs, higher benefits related costs and inflation. As a percentage of fourth quarter net sales, adjusted administrative expenses were 7.7%, a 30 basis point increase compared to last year.

On slide 30, we are providing an adjusted EBIT bridge to summarize the key drivers of performance this quarter. As previously mentioned, adjusted EBIT increased 5% in the quarter, primarily due to an 8% or \$44 million improvement in adjusted gross margin, as volume declines were more than offset by the net rate improvement, resulting in a 40 basis point adjusted EBIT margin contribution.

In addition, higher adjusted administrative and R&D expenses of \$14 million and lower adjusted other income of \$13 million had a negative adjusted EBIT margin impact of 30 basis points and 60 basis points, respectively. Despite adjusted marketing and selling expenses increasing \$4 million versus the prior year, they were lower as a percentage of net sales, and therefore, had a positive impact on our adjusted EBIT margin of 30 basis points. Overall, our adjusted EBIT margin decreased year-over-year by 20 basis points to 13.5%.

The following chart breaks down our adjusted EPS growth between operating performance and below the line items. A \$0.03 impact of higher adjusted EBIT was further benefited by a \$0.01 favorable impact from lower net interest expense. This resulted in adjusted EPS of \$0.56, which was up \$0.04 per share or 8% compared to the prior year.

Turning to slide 32. Our Meals & Beverage division had a strong quarter, with organic net sales increasing 7% versus prior year, driven by increases in US soup and gains in foodservice and Prego pasta sauces. Inflation-driven pricing and sales allowances were partially offset by volume declines and increased promotional spending.

Sales of US soup increased 6% due to gains in ready-to-serve soups and condensed soups, partially offset by declines in broth. Segment operating earnings in the quarter increased 18%. The increase was primarily due to a higher gross margin and lower marketing and selling expenses, partially offset by higher administrative expenses.

Gross margin percentage improved, reflecting the mitigation of ongoing inflation with pricing actions and supply chain productivity improvements. Lower volume and unfavorable mix, as well as higher level of promotional spending, pressured gross margin percentage. Overall, within our Meals & Beverage division, the fourth quarter operating margin increased year-over-year by 160 basis points to 17.2%.

On slide 33, organic net sales in our Snacks division increased 6%, driven by sales of our power brands, which were up 9%. Snacks sales increased due to gains in salty snacks, primarily Kettle Brand, and Cape Cod potato chips, as well as in cookies and crackers, primarily Goldfish crackers. Inflation-driven pricing and sales allowances were partially offset by increased promotional spending and volume declines.

Segment operating earnings in the quarter increased 3%, primarily due to higher gross margin, partially offset by higher marketing and selling expenses and higher administrative expenses. Gross margin percentage was relatively flat, reflecting the mitigation of ongoing inflation with pricing actions, supply chain productivity improvements and cost savings initiatives, partially offset by higher levels of promotional spending, lower volume and unfavorable mix. Overall, the fourth quarter operating margin decreased year-over-year by 40 basis points to 13.4%.

I'll now turn to our cash flow and liquidity. Fiscal 2022 cash flow from operations increased 14% year-over-year to \$1.2 billion, primarily due to changes in working capital, partially offset by lower cash earnings. Cash outflows from investing activities were reflective of the cash outlay for capital expenditures of \$242 million, which was down from \$275 million in the previous year. Cash outflows from financing activities were \$910 million. The majority of which, or \$618 million, represented the return of capital to our shareholders, including \$451 million of dividends paid and \$167 million of share repurchases.

At the end of the fourth quarter, we had approximately \$375 million remaining under the current \$500 million strategic share repurchase program and approximately \$172 million under our \$250 million anti-dilutive share repurchase program. We ended the year with cash and cash equivalents of \$109 million.

Turning to slide 35. As covered in our press release, we are providing financial guidance for the full year fiscal 2023. While we expect the current macro challenges to continue, our portfolio of brands is well positioned to meet consumer demand.

Our previous pricing actions are now fully in place, with expected price elasticities in fiscal 2023 to be slightly above fiscal 2022 levels. We expect positive top line growth for the year in both divisions, partly driven by an increase in our brand investments, supported by an improved supply chain.

Our productivity improvements of approximately 3% and cost savings of approximately \$60 million in fiscal 2023 will continue to play an important role in mitigating inflation, which is expected to be in the low-teens range for the year.

Other assumptions incorporated in our full year guidance includes, interest expense of approximately \$190 million and an adjusted effective tax rate of approximately 24%. We expect pension income to decline year-over-year by approximately \$35 million, representing a headwind of approximately 3% to adjusted EBIT and adjusted EPS growth in fiscal 2023.

All in, we expect net sales, both organic and reported, to be plus 4% to plus 6%, adjusted EBIT of plus 1% to plus 5% and adjusted EPS of flat to plus 4% versus the fiscal 2022 results. We plan to invest in the business with capital expenditures targeted at approximately \$325 million for the year.

Although the midpoint of our guidance reflects modest growth in adjusted EPS, it's important to highlight that without this headwind from pension income, we expect a significant step-up in growth across all key metrics while still accelerating investments to continue to unlock our full potential. This significant step-up in growth is more indicative of the progress of the business.

Overall, we had a strong finish to the year. And we are truly grateful for the continued dedication and commitment by our teams.

And with that, let me turn it over to the operator to begin the Q&A portion of today's earnings call.

QUESTION AND ANSWER SECTION

Operator: [Operator instructions] Your first question comes from the line of Andy Lazar from Barclays Capital. Your line is open.

Andrew Lazar

Analyst, Barclays Capital, Inc.

Q

Great. Good morning, everybody.

Mark A. Clouse

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

A

Hey, Andrew. Morning.

Andrew Lazar

Analyst, Barclays Capital, Inc.

Q

Morning. I guess first off, Mark, you're guiding to a 4% to 6% organic top line gain in fiscal 2023. Maybe you can talk a bit about the key drivers to this in terms of expectations around pricing and promotional spend versus volume expectations. And then I've just got a follow-up.

Mark A. Clouse

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

A

Sure. Yeah. So 4% to 6%, to kind of build it up, anticipates what I would describe on the pricing side as kind of low-teens pricing and then likely a couple hundred or so basis points of promotional spend back. So, think of it as kind of double-digit net pricing impact. So, there's no outsized promotional spend, but there is some reinvestment, as we had anticipated.

Elasticities have continued to be very positive versus historical levels. But as we land fully the wave three pricing that rolled out in [ph] P12 (31:37) of 2022, we've been seeing elasticities in about the 50% range, better on snacking, a little bit of a step-up is anticipated for next year, probably more like 60% of historical elasticities.

And then you've got some tailwinds as we have kind of pushed some of the inventory recovery forward from 2022 to 2023. I'll explain that, I'm sure, in a bit. But – and the step-up in investment that we have. And so collectively, you put those pieces together, you get to the 4% to 6%. I think as you think about the year and where the incrementality of pricing sits as well as where the supply recovery will probably be most prevalent, we're anticipating a stronger first half growth. In particular, Q1, I think will have a positive relationship to consumption, a little bit of a flip of Q4 as we saw a little bit of timing of shipments move into Q1.

Andrew Lazar

Analyst, Barclays Capital, Inc.

Q

Got it. Got it. And that's helpful. Yes. And it's a good segue into the second question, which is really just – I realize there are plenty of moving pieces here to guidance. And maybe a bit more color on expected phasing for the year and any discrete items that we need to keep in mind along these lines. You obviously mentioned the flip in shipments versus consumption expected as you go into Q1. But any other things around phasing that we should be aware of more for modeling purposes and such?

Mark A. Clouse

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

A

Yeah. Sure. So maybe let me give a little bit more color. And Mick, feel free to jump in if I miss something. But on the EBIT side, to kind of give you a little bit of the building blocks there, as Mick said, we continue to expect inflation next year in the low-teens, is what we've positioned it as, with pricing and some of our productivity covering that.

And then the balance of productivity and cost savings are really more than enough to offset the step-up in investment in marketing and selling as well as covering the pension that Mick laid out. So I think the net of that is modest overall EBIT growth, probably a relatively flat gross margin as you think about the – where the building blocks come from. I generally don't like to guide to gross margin, but I think stable is the way I would describe it.

I also think, as you're thinking about our investment and how much and where are we, we've talked a lot about the goal of getting into that 9% to 10% range for marketing and selling. I think you should anticipate for 2023, we'll be on the low end of that range, but a step up from where we were in 2022 as we build that back.

When you think about phasing for the year, I do think it's a little bit of a reverse story from the top line. I think you'll see probably our toughest quarter on inflation in the first quarter as well as a place where I would expect to see investment returning. As you might remember, a year ago, we were in a little bit of a supply-constrained world, and thus then adjusting some of the investments that we had, we'll see that come back.

And then I think the other thing that's important to note is the pension that Mick talked about. Two-thirds of that will be in the first half of the year. And so as you put those things together, the way I would expect is a Q1 where margins will be a little challenged and then kind of stabilizing, normalizing as we go through the year to deliver that relatively overall stable gross margin and modest improvement in EBIT.

I think what's important, just to point this out, but I'm sure it's kind of self-explanatory in the numbers, but the EBIT without the pension [ph] in it (35:30), we're 1% to 5% growth on the base, but without the pension in there, we're 4% to 8%, which would put us very much in line with our long-term guidance, and EPS kind of rolls through to the same kind of dynamic.

So, at the end of the day, I think when you look a little bit past the accounting on the pension, the underlying guide, I think, continues to support the momentum and progress that we've been talking about and describing.

Andrew Lazar

Analyst, Barclays Capital, Inc.

Great. Thanks so much.

Q

Operator: Your next question comes from the line of Ken Goldman from JPMorgan. Your line is open.

Ken Goldman

Analyst, JPMorgan Securities LLC

Hi. Good morning, everybody.

Q

Mark A. Clouse

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

Hi, Ken.

A

Ken Goldman

Analyst, JPMorgan Securities LLC

Hi. Just to tie a bow, I guess, on the conversation about the one-time puts and takes in 1Q. Is there any way for us to sort of estimate or quantify the degree to which shipments are expected to exceed consumption? I understand these dynamics are hard to forecast, but I just kind of want to minimize surprises if we can.

Q

Mark A. Clouse

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

Yeah. Maybe a way to do that, Ken, is to give you a little bit of color on Q4. Because I do think, to some degree, an expectation that net sales would have been perhaps at or favorable to consumption might have been an expectation out there. And I will say that relative to our own modeling, we saw a little bit more of the shipment timing move into Q1. But maybe it will be helpful to bridge Q4 and then I'll tell you kind of what to think about as you get into Q1.

A

So, I think probably the biggest shift, if you will, in the difference between the two, and this was a little bit of a unique dynamic, but I think the right call, which was to roll out our Wave 3 pricing in the last month of 2022. And that was really designed to ensure that we had the pricing fully reflected and in place as we stepped off in fiscal 2023.

However, in a month where you're executing pricing, I do think we saw a little bit slower, especially as it relates to inventory recovery as we executed that. The good news is, as we project in the Q1, that's probably a couple of hundred basis points of difference that I think will move into the Q1 timing. And as we start the year, we see momentum as – in support of that. So, I think that's the first piece.

The other two, as we have continued to prioritize the retail environment, some of the non-measured channels, especially on snacking, it was about 200 basis points of headwind for our snacks business, about 100 basis points overall for the company of decline in unmeasured channels, which is part of that bridge as well.

And then perhaps the final piece, but on a smaller level of contribution, although I feel tremendous about the progress we're making on supply chain, we still have a few businesses where material availability has slowed full supply recovery.

That's primarily Lance, Late July and V8, where each of them have their own kind of material availability challenge that will take us some time into 2023 to fully recover. So, you put that into the mix as well.

So as you think about Q1, imagining that we're a couple of hundred basis points ahead of kind of in-market consumption, I do think the unmeasured channels will stabilize and be more in line as supply fully comes back in line, especially in our snacking businesses.

And so, I think that's probably a good way to kind of think about the dynamics of the movement from Q4 to Q1 and maybe a little bit of explanation on why you might not have seen a little bit more top line, in particular, on the snack business in Q4.

Ken Goldman

Analyst, JPMorgan Securities LLC

Q

Great. Thank you for that. And then, a quick follow-up on promotional spending. Can you maybe elaborate a bit on what drove that sort of sudden increase, I'd say, in the fourth quarter in promo spending and snacking? I guess, how...

Mark A. Clouse

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

A

Sure.

Ken Goldman

Analyst, JPMorgan Securities LLC

Q

... [indiscernible] (39:46) that trend would be? And kind of how you think about – I know you talked about a couple of hundred basis points in 2023. But is there a breakdown by segment? Just very roughly, Mark, that we can kind of model in.

Mark A. Clouse

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

A

Yeah, yeah. No, and I think we tried to kind of allude to that is – as we were moving from Q3 into Q4, that as supply came back in line and given the nature of snacking, it is probably more important to get that balance of promotion right. And it's interesting when you look at snacks in the fourth quarter, although you did see about 400 basis points of step-up in promotional spend, you also saw vol mix that was down only about 3 points, which relative to the total net pricing we took would imply a very low elasticity.

And part of that is the nature of snacking. And so what we want to make sure we're doing perhaps more so in snacking than other categories is really ensuring that we stay competitive as it relates to units, because in the end, that's really what's indicative of the future health of the business. And so I think that balance is what we're striking. I do not think you'll see 400 basis points as a ongoing runway. I do think we – the summer does tend to be a little bit more historically promoted period. And so you saw that.

And given what we were lapping, which was very light on promotion. I think it's a more normalized view of promotion than it might have looked at first glance with 400 basis points. But as I think you get into 2023, I think it will. As I said, 200 basis points, probably a little more distortion to snacking, but generally in that ballpark for the year is a good assumption.

Ken Goldman

Analyst, JPMorgan Securities LLC

Great. Thank you.

Q

Mark A. Clouse

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

Yeah. And by the way, just as closing that out, I mean, that is why you saw, I think, in Q4 the unit share performance that I talked about in the remarks. And the fact that we were growing units in salty snacks, which is perhaps the most fiercely competitive segment of snacking was – in my mind, as I thought about what we were trying to accomplish in the quarter, was a very positive outcome. Okay.

A

Operator: Your next question comes from the line of Peter Galbo from Bank of America. Your line is open.

Peter T. Galbo

Analyst, Bank of America

Hey, guys. Good morning. Thanks for taking the questions.

Q

Mark A. Clouse

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

Sure, Peter.

A

Peter T. Galbo

Analyst, Bank of America

Mark, I guess, just the first question, going back to – circle back on Andrew's question around gross margin and realizing that you've given a little bit of color there. I just – in the context of some of the guidance elements that Mick has given, it would kind of seem that gross margins would actually have to be up to make the EBIT math and the EPS math work versus kind of the flattish and just wanted to make sure that your comment wasn't that they would be flat but could potentially be up on the year.

Q

Mark A. Clouse

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

I think they're going to be relatively stable is what I would say. So I always hate to give precise numbers on gross margin. But I do think what I would expect to see – and remember this too, like when we talk about cost savings and even some of our productivity, that's not all in gross margin. Part of that is below the line. And that contribution, as Mick laid out, the cost savings goal for the year does give us some counter to the increase in marketing and selling spend that we have below. So I think when you put those together, it's helpful. Mick?

A

Mick J. Beekhuizen

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

Yeah. Maybe kind of to be a little bit more precise around the cost savings, think about it as about a third is going to [indiscernible] (43:38) cost of goods. The remainder is below the gross margin line.

A

Peter T. Galbo

Analyst, Bank of America

Got it. Okay.

Q

Mark A. Clouse

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

A

So I think if you did that math, if you roll that math together, I think it will allow for you to have a little bit of kind of offset to where you would see marketing and selling up and the pension recovery with cost savings relative to then a gross margin that I think will be healthy, but generally, probably pretty stable.

Peter T. Galbo

Analyst, Bank of America

Q

Got it. Okay. And then, Mark, just going back to some of your comments from prior calls around soup. I think it's played out kind of as you expected or as you've communicated, maybe more so in broth, that private label has taken more of the share. I guess what we've seen in the Nielsen data is, on the condensed side, realizing that broth is maybe a part of that, private label has taken more share in condensed relative to ready-to-serve. But maybe that's not what you're seeing in your business. So I just wanted to understand if there was a difference between the data that we're seeing and what you're seeing internally.

Mark A. Clouse

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

A

No, no. And that's what we would have expected, right? So, private label in our soup business really is prevalent in two places. It's the condensed business and it's the broth business. And those are the two places where we recognize, we're – we've got to be very, very on top of price gaps and the overall value proposition.

I think the one piece of context that I'll just give to you that I do think is important, and I mentioned it in my comments, in a condensed world where we're 80% of the category, and the category is up double-digits, that is a good thing for us overall. Although, again, I'm never happy nor satisfied with any share loss at all, I do think the overall strength of the segment has been very positive.

I think further to that, we've tried to really carve out the parts of the condensed business that we want to make sure that we're defending in a more perhaps vigorous way. And that's – we describe it as our icons, but that's essentially chicken, noodle, tomato, cream of mushroom, cream of chicken, these are the kind of juggernauts of condensed.

And when we look at those head-to-head versus private label, we're actually winning on share expansion and growth. Where the decline is coming from is on a lot of the flankers, which tend to be a little bit higher priced. There are things like healthy requests and some of the longer tail on flavors.

And so as we go into 2023, what we're really going to be trying to do is maintain that focus on icons, but also providing a little bit more support behind the broader portfolio to try to continue to bring kind of a full solution to bear, if you will, for condensed.

And so, although I expect that pressure to be there, especially in the first half until we kind of cycle where we were when pricing really kind of took hold in the back half, I do feel very good about where we are. And it's very consistent to where we expected to be. And again, if the category can continue to maintain the momentum, I think it bodes well for us longer term as well.

I think broth, as I've always said, it's kind of the toughest, because arguably, it is the most commoditized segment of the soup business. But I will say, I feel the best about our offerings that we've ever had as we roll into 2023. We've got a quality improvement that now tests superior to private label. We've also got packaging constructs that

are unique to us that will bring value and convenience. And so I think we put our best foot forward. And I think this holiday season will be a good initial test of that. And so we're geared up and ready to go there. But I think that category or segment continues perhaps to be one of our most challenging longer term, [ph] but (47:49) I feel very confident that the condensed business, we're very well positioned on.

And then just to round it out, I mean, on ready-to-serve, I feel terrific about where we are there. Shares have been improving. Our Chunky business is really just doing fantastic. Well, yes, continues to plot its course of recovery. I mean Chunky's growing top line share and units. So we've got everything going in the right direction. We've got a terrific pipeline of innovation. We've added Pacific in a material way to ready-to-serve now. And we've got a whole another new lineup of ready-to-serve organic soups and chilis with Pacific.

So I feel really good about that, and I think that's evident in our results. So when I take a step back on soup, I would just say, again, I'm never going to be okay with share loss. But I don't think it's inconsistent with what we expected. I think we've got good action plans against the different pieces. And I do expect us to continue to show progress. And if at the end, the underlying dynamic is continued strong growth in the category, ultimately, that will be a very good thing for us.

.....
Operator: Your next question comes from the line of Jason English from Goldman Sachs. Your line is open.

.....
Jason English

Analyst, Goldman Sachs & Co. LLC

Q

Hey. Good morning, folks. Thanks for slotting me in.

.....
Mark A. Clouse

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

A

Hey, Jason.

.....
Jason English

Analyst, Goldman Sachs & Co. LLC

Q

Two questions. Hey. I'm surprised to hear you measure [ph] on (00:49:19) measured channels as a headwind in snacks. It's been growth accretive for most companies. Can you shed some light on what's going on there? Where are you seeing the weakness and what's driving it?

.....
Mark A. Clouse

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

A

Yeah, yeah. What it is, Jason, is a little bit of decision making between where we steer supply in the short term. So I don't feel at all like it will be a problem in the future at all. But I do think in the fourth quarter, we made some decisions to strengthen our presence in some of the retail channels where we had been weaker on supply and kind of prioritized recovery there.

I think you'll see strong recovery as we go into fiscal 2023. And I don't think you'll see that as a drag on the business at all as we go forward. And yeah, it's a very healthy channel and one we want to be present in going forward or healthy channels that we want to be present in going forward. But in the fourth quarter, it was a little bit of pick your spot. And we decided that we prioritize the retail first.

Jason English

Analyst, Goldman Sachs & Co. LLC

Q

Understood. Thank you. And I'm a little surprised by some of your comments on snacking, the characterization salty snacks is exceptionally promotional or something to that effect, and your highlight on units over value. It very much sounds like you're pivoting to a volume over value strategy, which we as analysts here been conditioned over the years to get very nervous about because it's often led to a path to like value destruction, margin compression, race to the bottom. Maybe you can give us some context, like why we shouldn't be concerned around some of the language you're using and where – what you're choosing to highlight as areas that we should focus on.

Mark A. Clouse

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

A

Yeah. I think the biggest indicator I can give you, Jason, is that we're not talking about anything even remotely broader or deeper than historical levels. And honestly, even with the Q4 example that I gave, we're still not back, and nor do I think we need to go all the way back to historical levels. At the same time, I do think that snacking in general, because of so much of the impulse decision making that's there, the balancing act between the two is perhaps a little bit more important. So this is no shift in strategy.

And again, I continue to be very confident in our ability to drive the margin goals that I know you and I have talked a lot about over the years and continue to see a runway. And even in the quarter, right, where we delivered that kind of investment, although our margins were off of, I think, 30 basis points, it's a really stable margin on the business that I expect to continue to accelerate as we get into 2023.

So I don't think you should have any concern at all about some shift in strategy that's going to result in margin erosion. I do think what you should expect is some recovery of the promotion that has left the segment as we continue to kind of be in a position where we want to stay as competitive as possible.

So, I think where you'll land at the end is less probably promotion than we had historically, but certainly more than what we had last year, because it just was – it was too much. And again, it was because we didn't have supply. And so, I do expect that recovery to come. So yeah, please don't read too much into this. It's really about the recovery.

But I do think in a world where inflation is so dramatic, continuing to calibrate volume and making sure you know where your volumes and your units are is a very important aspect of recognizing are we pricing in the right balance. So, I would tell you that it's probably more about the overarching sustainability of the broader strategy and making sure that we've got that balance right.

Jason English

Analyst, Goldman Sachs & Co. LLC

Q

Helpful context. Thanks a lot. I'll pass it on.

Mark A. Clouse

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

A

Yeah.

Operator: Your next question comes from the line of Robert Moskow from Credit Suisse. Your line is open.

Robert Moskow

Analyst, Credit Suisse Securities (USA) LLC

Q

Hey. Thank you. I noticed in your CapEx guidance, I think it's \$325 million, it's well below the 4% to 5% of sales that you'd talked about at your Investor Day. And I want to know, are there any projects that are getting delayed? And is it correlated to your innovation plans? Because 2% of sales this year contribution from innovation, it just sounds low in historical context. And I know at Investor Day, you talked about increasing that over time. So, can you talk about that?

Mark A. Clouse

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

A

Maybe I'll do innovation first and then we'll back into the capital. But – so, if you remember on Investor Day, we showed a slide that had essentially kind of a historical runway rate of about 1.5%. And then for 2022, we had 2% innovation as our target, which we delivered, and saw momentum even on that as we were kind of exiting the year. As we move forward, we expect that to get back up into the 2% to 3% to 3% to 4% over time. And that is, in our mind, really kind of best in class. And again, you expect there to be a bit more innovation flowing through your snacks business just because of the nature of that category.

But what I felt this year was important in a world where we were wrestling with a lot of external variables was to stay on track to deliver the goal that we laid out in Investor Day was a good step up. And then now, with an even bigger pipeline in the future, we feel great about where we're going and where we're headed in the future. And I think our capital is really built to support that, but also with a good amount of it that's related to continued cost savings and productivity. But Mick, I'll let you give you a little more color on that.

Mick J. Beekhuizen

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

A

No, I agree, Mark. And basically, the way that I would think about, Rob, is that we had – we obviously spent this past year \$242 million. This year, we're targeting \$325 million. Obviously, quite a bit of an increase, but really to your earlier point, to make sure that we support the overall growth of our business while we obviously maintain our assets as well and we support all the innovations.

So we're not stepping back. If anything, I actually feel like we're doing step forward here, and we continue to make sure that we support the growth. And if you look at it from kind of as a percentage of revenues, of course, there's a little more kind of overall top line pricing reflected and all that. So net-net, with 3.5% is – if you look at the mid-range of our net sales guidance and you take – put that \$325 million in perspective, I actually feel pretty good where we are from an overall capital investment perspective.

Robert Moskow

Analyst, Credit Suisse Securities (USA) LLC

Q

Okay. So if I could ask a follow-up. Mark, I think you said that one of the reasons for the inventory reload spilling into 1Q had to do with pricing actions that you took during fourth quarter. And I would have thought that customers would actually buy more inventory after you announced a price increase before the pricing goes through. Why doesn't that dynamic play out?

Mark A. Clouse

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

A

Yeah. It actually did. It just happened much earlier in the quarter. And then in the – normally, what we do on pricing, right, just the way that the nature of executing these, it tends to be at the turn of quarters. And you end up

getting a little bit of an inventory build as you kind of roll out of the quarter and then a little bit slower start as people work through their lower-priced inventory before they replenish. I think the desire to get pricing in place for 2023 led us to push that a little bit more forward.

And I am really glad we did, because in the end, we're in a great position headed into the year. We're at a much stronger and kind of Wave 3 pricing fully behind us is what we wanted. But I will say that where you would normally have perhaps a little more of incentive to build in the final month, you just didn't see that quite as much.

And at the end of the day, I think the good news is, as I said, very consistent with prior circumstances, in this month, we're seeing that bounce back as you would expect. And so I think the good news is that it kind of carries that opportunity a little bit into Q1 and I think that in many aspects will be beneficial.

Robert Moskow

Analyst, Credit Suisse Securities (USA) LLC



Okay. Thank you.

Operator: And ladies and gentlemen, this concludes today's conference call. Thank you for your participation. You may now disconnect.

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