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Campbell Soup Co. (CPB)

Q1 2024 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Greetings, ladies and gentlemen, and welcome to the Campbell Soup Company First Quarter Fiscal 2024 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's now my pleasure to introduce your host, Rebecca Gardy, Chief Investor Relations Officer. Please go ahead.

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

Good morning, and welcome to Campbell's First Quarter Fiscal 2024 Earnings Conference Call. I'm Rebecca Gardy, Chief Investor Relations Officer at Campbell. Joining me today are Mark Clouse, Chief Executive Officer; and Carrie Anderson, Chief Financial Officer.

Today's remarks have been pre-recorded. Once we conclude the 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 on 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 make 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 of our presentation or our SEC filings for a list of factors that could cause our actual results to vary materially from those anticipated in the 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 our presentation.

Slide 4 outlines today's agenda. Mark will provide insights into our first quarter performance as well as in-market performance by division. Carrie will then discuss the financial results of the quarter in more detail and outline our guidance for the full fiscal year 2024, which we reaffirmed this morning.

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, everyone, and thank you for joining our first quarter fiscal 2024 earnings call. From Campbell's management team, we hope you enjoyed a happy Thanksgiving with family, friends and of course, some green bean casserole and Pepperidge Farm stuffing.

As you saw in our press release this morning, we reported first quarter results with top line coming in consistent with our expectations. And adjusted EBIT and adjusted EPS coming in slightly ahead as we lapped one of our strongest quarters, with 15% growth across all three key metrics in the prior year. I am pleased with these results as we continue to navigate an evolving and challenging consumer environment.

We also made material progress advancing the key initiatives of our focused strategic plan and continue to build confidence in the next stage of Campbell's growth. I am encouraged by the consistency of our outstanding execution, including strong, sustained performance across our supply chain, numerous successful innovations and marketing programs and more recently, improving share trends. We achieved all this while maintaining our margin and earnings expectations.

Going forward, we anticipate these areas of focus to fuel sequential improvement over the course of the year, generating momentum in terms of revenue, volumes, market share and profit margins, particularly as we head into the second half of fiscal 2024. As a result, we remain confident and are affirming our full year guidance. We believe this building momentum, paired with the pending acquisition of Sovos Brands, will set the stage for accelerated growth and solidify Campbell's position as one of the most dependable names in food.

Turning to slide 7, as expected, organic net sales decreased by 1% to $2.5 billion, following a 15% increase in the prior year, resulting in growth of approximately 7% on a two-year compound annual growth rate basis. Adjusted EBIT and adjusted EPS declined 9% and 11%, respectively, following a 15% increase in both key measures the prior year. Our dollar consumption was down 2% but grew 8% versus two years ago.

In line with expectations we communicated during our fourth quarter earnings call, the consumer landscape remains challenging. However, we have many opportunities within our portfolio to meet these shifting macro consumer trends and have optimized our strategies and plans concentrating on three key areas.

First, we're dedicated to ensuring the affordability of our products and maintaining competitive price gaps within our margin goals. This is particularly important, especially as consumers seek to maximize the value of their spending, stretching their budgets to cover the cost of family meals every day and during the important holiday season.

Second, we are committed to sustaining our marketing and innovation plans. This is critical not only to reinforce the value and differentiation of our products but also to continue to build the long-term equity of our brands on which we've made significant progress in recent years.

Finally, our approach to spending remains disciplined and balanced, focused on high ROI and impactful programs. We are driving productivity and making appropriate trade-offs to fuel this investment, while we protect our margin and earnings objectives, where support has been added, we believe it's both sustainable and profitable. We intend to maintain this focused approach throughout fiscal 2024, and we are confident that we will build momentum as the year progresses and continue to deliver our financial commitments.

We remain confident in this forecasted improvement in trends throughout the year for a number of reasons. It's important to recall that our growth rates in the first half of fiscal 2023 averaged in the mid-teens and subsequently tapered down to mid-single-digit growth in the second half. This approximate 10-point decline in part reflected a slowing in incremental pricing. These more modest comparables post Q2 support our expectations for improving top line and volumes.

In addition, we have a robust pipeline of innovation and marketing programs informed by the current consumer trends to also fuel the improving outlook. So, although the consumer landscape remains dynamic, we are well positioned for improvement and we'll continue to plan contingencies and remain nimble as we navigate the balance of the year.

Turning to our Meals & Beverages division, as planned, we experienced a low to mid-single digit decline in top line and consumption in the first quarter. On a two-year compound annual growth rate basis, organic net sales were up 6%, and dollar consumption was up 1%.

The difference in net sales and consumption growth rates reflect the strength in our foodservice business and unmeasured channels as well as a year ago supply and inventory recovery. Within these results, we find many reasons to remain confident in the trajectory of the business as consumers depend more and more on affordable, stretchable meal solutions, which is at the core of our Meals & Beverages division.

Turning to our Soup portfolio on slide 11, as anticipated, throughout the summer, we experienced decreases in dollar consumption overall. However, within these results, there are pockets of strength. For example, as consumers sought to stretch their food budgets, they turned to the strong value and convenience of the cooking portions of our portfolio. In fact, in our condensed cooking portfolio, we gained dollar share for the fifth consecutive quarter, increasing 1.5 share points in the quarter. Even among younger households, we continue to see long-term potential as household penetration of total condensed cooking soups gained 0.4 points versus the prior year.

In our broth business, we continue to drive relevance among consumers in this dynamic environment as total broth was up 4% behind the strength of our Pacific broth portfolio, which saw dollar consumption grow 16%, well above the category rate. The ready-to-serve and condensed eating businesses experienced more pressure in the quarter as a result of more consumers shifting to more stretchable meals versus single-serve options.

Turning to page 12, as we have begun ramping up planned support in anticipation of the important holiday season, trends have been improving, especially as it relates to share. In fact, over the latest four weeks, including Thanksgiving, we've seen improvement in all segments, driving overall dollar and unit share gains, including a [ph] 0.2 points (00:09:21) improvement in dollar share as well as a [ph] 0.9 points (00:09:22) improvement in unit share for our very important total soup business.

Importantly, we are doing this with modest incremental investment as we are seeing more retailers actively returning to Campbell's brands from private label a year ago. This is providing an outsized benefit while we continue to balance the critical interplay between growing share, volumes and margins in line with our expectations. Although the category remains somewhat under pressure on dollars, it's very encouraging to see improvement in both share and units as we head deeper into our key season.

Turning to our Snacks business, we delivered first quarter organic net sales growth of 1%, consistent with the increase in dollar consumption. Our power brands grew net sales by a solid 5%, following a 21% increase in the prior year, for a 13% growth on a two-year compound annual rate basis. Even with some emerging broader category pressure due to the consumer dynamics that we discussed earlier, our eight power brands have shown remarkable resilience with brands like Goldfish and Lance posting net sales growth of 5% and 15%, respectively.

The strength of our power brands was tempered in the quarter, by lower-margin partner brands and fresh bakery as those businesses are somewhat more vulnerable to private label and consumer trade-down.

On the following slide, we highlighted the continued strength of each of our power brands. Dollar consumption grew 3% versus the prior year and 19% versus two years ago, while five of eight power brands held or gained share in the quarter. Our eight power brands, which now represent approximately two thirds of division net sales, remain a powerful and consistent growth engine even in the current consumer environment.

Turning to slide 15, a prime example of our Snacks power brand growth engine is Goldfish. For the fifth consecutive time, Goldfish has been named team's most preferred snack brand according to Piper Sandler's Taking Stock With Teens, most recently in the fall 2023 survey. This recognition is the result of the remarkable work of our cross-functional teams and expanding the brand to a broader audience and adding manufacturing capacity to meet the incredible demand for this product. We continue to see share strength in the overall portfolio as Goldfish marked its fifth consecutive quarter of holding or gaining dollar share.

One of the keys to our Goldfish success has been a steady drumbeat of innovation. On this front, we're excited to bring to consumers our latest limited time offer for the holiday season. Goldfish Elf Maple Syrup Flavored Grahams in partnership with Warner Bros. Discovery, celebrating the 20th anniversary of its iconic movie Elf. Is there anything better than Maple Syrup Goldfish to spread holiday cheer? And it's perfect for stocking stuffers or snacking all season long.

And there's even more exciting innovation in Goldfish in store this year. Adding to the incredible success of innovations like Goldfish Mega Bites and our run of limited time offers, we are reinventing the category again in a way only Goldfish can with the introduction of Goldfish Crisps, crisps with the way that Goldfish does chips, the best of Goldfish with the best of chips combined into an irresistible light, airy, crispy, fish-shaped baked snack. Launching in three craveable flavors, Goldfish Crisp (sic) [Goldfish Crisps] (00:13:05) will be available at retailers nationwide in January.

On slide 17, I want to highlight the margin momentum that the Snacks division has demonstrated. On a two-year compound annual growth rate basis, we grew Snacks' organic net sales by 8% and operating earnings by 12%, with approximately 130 basis points of margin expansion. Consistent with our long-term margin road map of achieving 17%, we remain confident in fiscal 2024 expectations to finish above 15%. And now, we're adding even more fuel to our Snacks growth and margin journey with our DSD transformation initiative.

This includes three key elements you see on slide 18, two of which were already progressing. First, creating one snacking DSD logistics and warehouse network. This multi-year program will streamline our logistics and warehouse network, eliminate redundancy, simplify our network and improve our technology and capabilities within our warehouses and depots.

Second, modernizing and harmonizing tools and technology used by our critical independent distribution partners. This will enable new capabilities and help enhancing effectiveness and focus. In addition, this will also allow better retailer linkage and alignment to orders while improving in-store insights.

And third, we'll focus on DSD routes. The good news is the vast majority of geographies already have scaled routes. And in combination with the upgrades from the first two elements of our DSD transformation, these will be fully optimized going forward. To help improve geographies, where routes are not operating at full scale, we're piloting a variety of potential solutions with encouraging early results. I'll share more about this third and very important element in our Q2 earnings call.

We're excited to have made so much progress on such a unique and critical part of our business. And in the end, this will result in a strong and differentiated DSD platform to fuel both the growth and margins of the Snacks business.

Before I conclude, let me provide a brief update on the status of our pending acquisition of Sovos Brands. As we announced in October, we received a second request for information from the Federal Trade Commission as part of the agency's review of Campbell's proposed acquisition. We are working hard to complete those requests and are advancing our integration planning.

I continue to be impressed with the strong results the Sovos team is delivering and could not be more excited about completing the acquisition and fueling our next chapter of growth. We expect to complete the deal in the next calendar year. And we'll continue to engage with the FTC on their review with the objective of closing the transaction in mid-2024.

In closing, the first quarter unfolded much as we anticipated, continuing our consistent track record of meeting our commitments. Looking ahead, I'm confident and optimistic about the balance of the year. We will remain vigilant and agile to meet the evolving demands of consumers while continuing to progress our strategic plans.

With that, I'd like to wish all of you and my colleagues across the company, a happy holiday season and thank the entire team at Campbell's, for their ongoing incredible and impactful work.

And now I'll pass it to Carrie.

Carrie L. Anderson

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

Thanks, Mark, and good morning, everyone. I'll begin with an overview of our first quarter results. As Mark indicated, our top line finished as we anticipated and adjusted EBIT and adjusted EPS came in slightly better, primarily due to the timing of adjusted marketing, selling and administrative expenses.

Our organic net sales decline of 1% reflects mid-single digit expected volume declines, a lower contribution from pricing and disciplined levels of promotion activity. Lapping a 15% increase in organic net sales in the prior year, organic net sales grew approximately 7% on a two-year compounded annual growth rate.

Adjusted EBIT decreased 9% to $407 million, reflecting lower adjusted gross profit, a commitment to continued marketing and selling investments and lower benefits from pension and postretirement income, partially offset by lower adjusted administrative expenses.

Adjusted EPS decreased 11% to $0.91, driven primarily by lower adjusted EBIT and slightly higher interest expense, partially offset by a reduction in the weighted average diluted shares outstanding.

Slide 22 summarizes the drivers of our first quarter net sales performance. Excluding the impact of the Emerald nut business divestiture, organic net sales declined 1%. We generated 3 percentage points of growth from net price realization and volume and mix declined 5 percentage points, in line with expectations.

As shown on slide 23, our first quarter adjusted gross profit margin of 32.1% decreased a modest 10 basis points with the year-over-year change in margin driven primarily by unfavorable volume and mix. As shown on the bridge, the combination of net price realization, productivity improvements and cost savings initiatives offset higher cost inflation and other supply chain costs.

Turning to slide 24, we continue to successfully mitigate inflationary headwinds, with core inflation moderating to 2% in the first quarter, driven by attenuation in key inputs such as flour and oil. We expect core inflation to stay within this low-single digit range for the full year, down from the 12% we saw in fiscal 2023.

Net pricing averaged 3% for the quarter, reflecting the contribution from our wave four pricing, our smallest and most focused pricing round. As a reminder, our wave four pricing will be fully lapped at the end of Q2 fiscal 2024.

In addition to pricing, we continue to deploy a range of other levers to mitigate inflation, including supply chain productivity improvements and broader margin-enhancing initiatives, including a focus on discretionary spending across the organization.

These other levers will start to have a greater contribution to margin performance as inflation continues to moderate and volume normalizes, especially as we move into the second half of the fiscal year.

We are pleased with the progress we have made on our cost savings initiatives. Through the first quarter, we have achieved $895 million of total savings under our multi-year cost savings program, inclusive of Snyder-Lance (sic) [Snyder's-Lance] (00:20:00) synergies. We remain on track to deliver savings of $1 billion by the end of fiscal 2025.

Moving on to other operating items, adjusted marketing and selling expenses increased 9%, driven by higher selling expenses, higher advertising and consumer promotion expense, or A&C, which increased 6% compared to the prior year and higher other marketing expenses. On both a reported and adjusted basis, marketing and selling expenses represented approximately 9% of net sales for the quarter.

Adjusted administrative expenses decreased by $5 million due to lower general, administrative costs, partially offset by inflation. We saw some timing favorability in adjusted marketing, selling and other administrative expenses in the quarter, but expect this to be re-phased into Q2 to keep the first half in line with expectations.

As shown on slide 26, adjusted EBIT for the first quarter decreased 9%, primarily due to lower adjusted gross profit, higher adjusted marketing and selling expenses and lower benefits from pension and postretirement income, partially offset by lower adjusted administrative expenses. Overall, our adjusted EBIT margin decreased to 16.2% in the quarter, primarily driven by higher adjusted marketing and selling expenses and changes in pension and postretirement benefit income.

Turning to slide 27, adjusted EPS of $0.91 was down 11%, or $0.11 per share, compared to the prior year. This was primarily driven by the decrease in adjusted EBIT and slightly higher interest expense, partially offset by a reduction in the weighted average diluted shares outstanding. Changes in pension and postretirement benefit income drove an approximate $0.01 impact to adjusted EPS in the quarter.

Turning to the segments, in Meals & Beverage (sic) [Meals & Beverages] (00:21:58), first quarter organic net sales decreased 3%, driven by an approximate 6% volume and mix decline, partially offset by 2% net price realization. Lapping a 15% increase in organic net sales in the prior year, Meals & Beverage (sic) [Meals & Beverages] (00:22:14) organic net sales grew approximately 6% on a two-year compounded annual growth rate.

During the quarter, declines in US retail products were partially offset by an increase in foodservice. Sales of US soup decreased 5%, following an 11% increase in the prior year, primarily due to declines in condensed and ready-to-serve soups, partially offset by an increase in broth.

Segment operating earnings in the quarter for Meals & Beverages decreased 13% to $287 million, largely due to lower gross profit. As expected, first quarter operating margin declined 230 basis points to 20.4%, driven by the lower gross profit margin, which was largely driven by higher cost inflation and other supply chain costs, as well as the unfavorable volume and mix between retail and foodservice, partially offset by supply chain productivity improvements and net price realization.

In Snacks, first quarter organic net sales increased 1% and on a two-year compound annual basis increased 8%. The organic net sales increase reflects net price realization of 5% and unfavorable volume and mix of 4%. Sales of our eight power brands increased 5% in the quarter.

Segment operating earnings in the quarter increased 5% to $161 million, primarily due to higher gross profit, partially offset by higher marketing and selling expenses. Gross profit margin increased due to the impact of net price realization and supply chain productivity improvements, more than offsetting higher cost inflation and other supply chain costs. Overall, within our Snacks division, first quarter operating margins increased year-over-year by 80 basis points to 14.5%.

I'll now turn to cash flow on slide 30. We generated $174 million in operating cash flow in the first quarter and deployed that cash consistent with our capital allocation priorities to maximize long-term shareholder value. We see some great opportunities to reinvest back into the business to drive incremental growth, productivity and enhanced business capabilities. And as such, we stepped up our capital spend in fiscal 2023, and this will now continue into fiscal 2024 after a few years of lower spend levels through 2022.

In Q1, capital expenditures were $143 million, $66 million higher than in the prior year, reflecting our commitment to invest for growth, particularly in capacity for our Snacks division. We also continued our commitment to return cash to our shareholders with $114 million of dividends paid and $28 million of anti-dilutive share repurchases in the quarter.

Our balance sheet continues to be in a strong position with net debt of $4.6 billion and a net debt to adjusted EBITDA leverage ratio of 2.8 times, below our target of 3 times. At the end of the first quarter, the company had approximately $91 million in cash and cash equivalents and approximately $1.85 billion available under its revolving credit facility.

In addition, on October 10, we entered into a $2 billion delayed single draw term loan credit agreement. The proceeds of the loan under this credit agreement can only be used in connection with the acquisition of Sovos Brands. This $2 billion credit facility, along with our current revolving credit facility, will provide ample liquidity and flexibility as we plan for the pending Sovos Brands acquisition.

As you'll see on slide 31, we are reaffirming our full year fiscal 2024 guidance provided on August 31. Organic net sales outlook for the full year remains in an expected range of 0% to 2% and reflects volume declines in the first half of fiscal 2024, with positive volume trends in the second half. Specifically for Q2, we expect net sales to again follow in-market trends with likely modest sequential volume improvement from Q1. However, we still expect volume and mix to be negative compared to the prior year.

Additionally, our net sales performance will reflect lower contribution from pricing as we move through the year and continue our disciplined levels of promotion. Our full year guidance range for net sales is largely reflective of what we see as the potential variability in the speed of volume recovery for the balance of the year.

Full year adjusted EPS guidance remains in the range of $3.09 to $3.15, with an expectation of modest earnings growth and margin progress in fiscal 2024 weighted to the second half, benefiting from a moderating inflationary environment and ongoing productivity improvement benefits. As I mentioned earlier, the expense timing favorability we saw in our Q1 results will be re-phased into Q2.

As a reminder, the sale of our Emerald nuts business, which we divested in May of fiscal 2023, is estimated to reduce net sales by approximately 0.5% and have a $0.01 per share dilutive impact in fiscal 2024. Additionally, the acquisition of Sovos Brands is expected to close in calendar year 2024 and therefore, is not included in our current fiscal 2024 outlook. We will continue to commit to investing in our brands, with marketing and selling expense as a percent of net sales expected at the low end of the targeted 9% to 10% range, with the second quarter having higher sequential spend than Q1. We are increasing our capital expenditure guidance to approximately 5% of net sales as we make additional investments in the business and strategically increase capacity to fuel organic growth.

With the timing shift of the Sovos Brands transaction, we are accelerating certain key growth and infrastructure projects from fiscal 2025 into fiscal 2024. All other guidance assumptions remain unchanged.

Turning to slide 32, we thought it would be helpful to provide some additional insight behind the adjusted gross margin and adjusted EBIT drivers we expect to come to fruition in the second half of fiscal 2024. As shown on the slide and referenced in our guidance, our core inflation outlook for fiscal 2024 is materially improved from the low-double digit levels we averaged in the prior year.

With cost inflation expected to remain in the low-single digit range for the balance of the year, we expect to see a greater net contribution from productivity and cost savings to our bottom line. Other factors that we expect will contribute to improving margin trends in the second half will be more favorable mix as volumes stabilize, especially on profitable businesses like Soup, normalizing year-over-year changes in marketing and selling cost as well as lower pension and postretirement income headwinds.

In closing, first quarter results were largely as expected, and our fundamentals are strong as we head into this important winter season. Our Snacks business continues to progress its margin journey while we continue to invest in the equity of our brands.

Our Meals & Beverages business continues to attract consumers seeking stretchable meals, which is especially important for winning the holiday season, given the current consumer environment. With a clearly defined strategy and a best-in-class supply chain, Campbell's is well positioned to deliver the rest of its fiscal year. From the management team at Campbell's, we want to thank all of our teams for their hard work and wish everyone a wonderful holiday season.

And with that, let me turn it over to the operator for Q&A.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Andrew Lazar from Barclays. Your line is open.

Andrew Lazar
Analyst, Barclays Capital, Inc.

Q

Great. Thanks so much. Good morning, everybody.

Mark A. Clouse
President, Chief Executive Officer & Director, Campbell Soup Co.

A

Hi, Andrew.

Andrew Lazar
Analyst, Barclays Capital, Inc.

Q

Hi, there. Mark, you mentioned an encouraging start to the holiday season. And of course, we don't want to make too much of any given four-week period, but for Campbell, obviously, the recent data is pretty critical. I guess, I was hoping you could dig in a bit more on this data, particularly how you see sort of category dollars progressing to help inform how fiscal 2Q is unfolding? And more important, how you see the rest of the year given the expectation that 2024 is going to be a somewhat back-end loaded year?

Mark A. Clouse
President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. So, yeah, great question, Andrew. And yeah, I think it's always important to see trends over longer periods of time. But of course, for us, Thanksgiving. I think from a barometer as far as the consumer, kind of macro consumer trends, but also for the business is quite important.

And I guess, the headline I'd give you is that the holidays as we had hoped, or especially Thanksgiving, was very resilient. I think consumers, for the most part, as we had anticipated, were very present, and especially in those categories that are most relevant to Thanksgiving. And as you may be aware, we're – outside of the protein, we're in the three biggest, with pretty strong positions in all three, which is broth, condensed soup and stuffing. Those are your top three household penetration categories beyond protein for the holiday. And I would say, in all three of those segments, we saw improvements and significant step-up in share. So, on condensed, we grew dollar share by [ph] 1.1 points, in broth 1.2 points and stuffing 0.2 points (00:31:45).

I will say one of the dynamics that we are also seeing is that the shopping dynamic has evolved a little bit, as you might expect, in a tough economic backdrop. And what I mean by that is one of the dynamics we saw was much later purchases. So, the key week of Thanksgiving was much bigger than the prior week. And historically speaking, those tend to be a bit more balanced. And as part of that, we did see a lot of consumers very actively seeking promotion.

And so, I will say that on the dollar side of the categories, in some cases, although overall improvement in total Thanksgiving categories, if you [ph] tune (00:32:22) them together were positive, you still see some headwinds on dollars. What I will tell you, though, is it's not a function of, what I would call, disproportionate or inconsistent with precedent promotion or spending. And so, I know always when you see a little bit of separation between units and dollars, there's always that question.

What I would tell you is that we did a very good job of executing within the holiday. One of the things I mentioned on the – in the fourth quarter was that a year ago at Thanksgiving, a lot of customers had chosen to go with private label as their lead item. We saw that reverse in a material way this year. And so, Campbell's products were back in the lead position, which was very important for us relative to ensuring that we get off to a good start in the season.

So, although I wouldn't say a comprehensive win across every measure, I think the things that we could control and the things we really needed to see, we were able to see and I think bodes well as we go into the December holiday and Christmas period as we roll through the winter. You'll still see some headwinds on some of the non-Thanksgiving-related products that dampen a little bit the overall category, but nothing that's inconsistent with what we've seen or quite frankly, what we expected.

Andrew Lazar
Analyst, Barclays Capital, Inc.

Q

Right. No, thanks for that. And then just a quick follow-up and it's related to this. Obviously, gross margins came in well above Street forecast. And I think that helps suggest that – or backs up your point around promotional tactics from Campbell maybe are playing out sort of as you'd expected in a somewhat more rational way. I guess, maybe you can discuss what you're seeing there and more importantly, what you're seeing in terms of lifts? Are the lifts around some of the promotional activities sort of consistent with what you've seen historically?

Mark A. Clouse
President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. I'd say better. And I think part of this – now, again, as I suggested, I do think we are getting a bit of a tailwind. And you can see it, right? What you'll notice is a fairly substantial step down in private label in certain of these categories, as you'll see that flip occur between us getting kind of key week. And for those that may not understand exactly what I mean, retailers have a decision to make on who's in their ad, who's on the end cap for the key week.

These are the things that are really important to enhance the return on investment for our promotion and the lifts that you're describing. And this year, opposed to last year, where I think private label might have been a little bit more new, and I think retailers felt like, well, let's just get to a low price and maybe that's what's most important. I think what we continue to believe in what we saw again in this holiday is that when the chips are really down, the Campbell's brands matter, and that is evident in the performance that we saw.

I do think you point out a very good proof point and that is how our margins progressing. And I think the reality is in the first quarter. You did not see any type of material change in investment relative to promotion or trade. Our margins came in very much consistent with where we expected. We continue to do a very, very good job on our productivity and some of our other levers in managing costs.

I think as we go forward, you will see us being very judicious, right? This continued balancing act that we've been talking about for a while of making sure that we're affordable and that the price gaps are managed right when we most need them to be, along with ensuring that the margin and the volumes, all kind of work together to give us this kind of optimal position. Not easy to do and in a dynamic environment, we've got to make sure that we're staying agile. But I would say, so far, I see nothing on the horizon that suggests to me that there's any variation from what we would have planned or expected.

Even though in certain periods of the year, you may see a [ph] sharpened (00:36:33) price point or make sure that we're strongest in a key week. But not outside of the precedence that we've set in the past or within the margin construct that we've laid out.

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

Kenneth Goldman
Analyst, JPMorgan Securities LLC

Q

Hi, thanks so much. Carrie, you mentioned the opportunity to manage discretionary spending maybe a bit more as the year unfolds. I'm just curious is it possible to provide, I guess, some examples of where the biggest opportunities might be within discretionary spending. And I suppose I'm also asking for a bit of help with how you define discretionary as well. Thank you.

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

A

Yea, I would say a lot of that goes back to some of our enterprise-wide cost savings initiatives. So, we have a vast program that we look at opportunities to enhance business capabilities, drive efficiencies in all parts of our organization that are part of our $1 billion cost savings initiatives.

So, it's – I would say it's really across the board not only in our COGS areas in our manufacturing facilities, but also going into the SG&A areas as well. And that's where we're seeing it across the board, some of those cost savings opportunities coming through.

Mark A. Clouse
President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. A lot of that, Ken, I would say, it would be in two big buckets. One is what we would call the non-working bucket. So, that's kind of think of it as production or materials or things that are not necessarily driving immediate impact in the marketplace.

And then secondarily, what I would call the non-people cost within our SG&A, where we're looking at everything. I mean, I think in a world where we want to make sure that every dollar is working as hard as it possibly can in this moment, especially, as I said before, as we kind of wrestle with this balancing act, we want to make sure that we've got every penny possible available to either invest in the right areas and/or help us deliver the earnings.

So, I think those two buckets are where we have been although always vigilant, I would say at a whole different degree of rationalization as we really make sure that we're working as hard as we can to get those dollars to work hard.

Kenneth Goldman
Analyst, JPMorgan Securities LLC

Q

Okay. Thank you for that. And then just a quick follow-up. It's great to see the improving share data within Soup, and thank you for the explanation as to what's going on maybe behind the scenes there.

I'm curious, do you believe your key customers are satisfied with overall category volumes with Soup, right, sort of understanding that the comparison is challenging? You did talk about how maybe you expect shipments and consumption to kind of match in the next few months. So, maybe that answers the question. But just trying to get any kind of sense of how those customers are looking at the category right now in the scheme of affordability and so forth.

Mark A. Clouse
President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. It's a great question. And I do think it's a conversation that we have frequently with our customers. And you've heard me talk about this before, and I'm always a little guarded because it should come with the big caveat that we're not going to do anything to undermine the long-term profitability of these businesses and margins. But I will say it is important for us to ensure that the volume on these businesses continues to be in an appropriate range relative to ensuring that the health of the category and really the health of our overall network continues to sustain.

And so, I think one of the other things you will see, Ken, in the holiday period, not surprising with a little bit of the disparity I shared between the unit share and the dollar share being a greater expansion in units, you will see a better step-up in units from where we've been on Soup. And I think, again, it's coming with the right investment package behind it. But look, I think that's encouraging. And I think, over a period of time, where we are looking for this business not just for the next month or the next event but really for the balance of the year and going forward, I think it continues to support what we believe is true, which is that this category continues to be strong.

And look, just as a context, right, I know we forget this sometimes and there's a lot of reasons why we can go back in these last several years and point to maybe non-normal, one-time elements that affected it. But if I would have told you that the four-year CAGR on the Soup category was going to be around 3% to 4%, we would have all felt really good about that given that it's the greatest growth period the categories had. And so, even though we're experiencing some slowdown in this year, I continue to believe that the underpinnings of this category, especially in the areas that we've identified as the most important growth areas, continue to have a good, solid runway ahead. And I think Thanksgiving just becomes maybe a little bit, as I said, not the complete victory, but another proof point in that story.

Operator: Your next question comes from the line of Robert Moskow from TD Cowen. Your line is open.

Robert Moskow
Analyst, TD Cowen

Q

Hi. Thanks. Mark, last quarter, you did some work to segment out grow versus optimize Soup brands. And I want to know if the grow brands performed any better than optimized in the quarter or were there comparisons at play to kind of change it around. And also maybe a little bit into the tactics you used for grow compared to optimize, how are they different?

Mark A. Clouse
President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. So, an interesting quarter on that front because you had, I would say, some real strength and some challenges in both of the two buckets. So, they were fairly consistent in the quarter, a little bit better, I would say, on share as broth recovered in the optimize, which was a good thing given its significance at the holiday. But the tactics, I think, for both. And again, if I look at this over the last couple years, as I said in the fourth quarter, you do have a pretty dramatic difference where the growth businesses over the last couple years CAGR is about 3% of upside and growing and the optimize businesses are down about the same amount and even a little bit more. More importantly, in the growth areas over the last two years, you're seeing relatively strong shares across most of the key areas like Chunky and the icons on condensed and Pacific.

I think in this particular quarter, what helped the optimize was some of the work and some of the benefit that we saw on broth kind of regaining its footing relative to private label. And I would say that was more of a function of just cycling private label than anything dramatic we did. I will say, as we went into the key weeks, and if you remember what I said on broth, even as an optimize, what's important is that we win those key holiday weeks.

And I think the good news is for a reasonable investment relative to what we expected, we saw that, where broth for the quarter or for the four weeks was up 4% on dollars, and up 1.2 share points in the latest four weeks, which is a great sign, while private label was down pretty significantly.

I think on the growth, Rob, what we're seeing, that's a headwind, right? The, I'd say, condensed cooking, icons, Pacific, all of those are doing extremely well. I will say the pressure on ready-to-serve has been a bit more pronounced in the last quarter. And this is really, we believe, a dynamic of consumers, especially our lower income consumers that are under a lot of pressure that are migrating a bit more to what we would call stretchable meals from single serve.

And so, one of the things that you'll see us doing on Chunky in particular, is really positioning it more through the lens of the protein content and its ability to also stretch in meals to match a little bit where those consumers are going.

But I do think in the quarter, what dampened a little bit of the growth trajectory was that ready-to-serve. I'm not particularly concerned. I think we'll continue to see, as we get into the season, a lot of activity on that business. And all the other areas of growth are doing extremely well.

Robert Moskow
Analyst, TD Cowen

Q

Great. Thank you.

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, 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

Hi, there. So, in terms of inflation as an enabler to gain the margin recovery in the back half, it sounds like you're looking for core commodity inflation to remain roughly stable where you were in the first quarter, the low-single digit rate. But when you show us the margin bridge, there's a big gap there. Like the 2% core inflation rate would suggest far less gross margin compression than the 460 basis points you show with the inflation in other bucket. So, what's going on with the other? And what should we expect going forward?

Mark A. Clouse
President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. So, the other supply chain cost is a variety of variables and maybe Carrie and I can tag team on this one a little bit together. But I'd say there's three things in there that are influencing that margin pressure that we're seeing now. The first is, I would describe some inflation, albeit not core inflation, cost of the supply chain, some of the intrinsic costs within our plant costs have been a headwind and have moved kind of in concert, I would say, with inflation. And so, although we don't categorize it as core inflation, I would say, generally, that's what's behind it.

I think the second is, it's also there is a mix dynamic that is within that cost structure that's related more to SKU mix. And even as we see some of the brand and category mix even through to SKU, we've seen a bit of a headwind there.

And then the third area is, and again, not completely unexpected, that's also where you see absorption and some of the fixed cost leverage that you would experience in a circumstance where volumes might be a little bit down from where they've been, and that's pressure that's there.

So, as you can expect that normalization, whether it be from the mix standpoint, inflation standpoint and/or even the volume standpoint, that's why we do not see those continuing forward. And you will begin to cycle if you were to go back and look at our Q3 and our Q4 from 2023, you would see rather significant contributions from those buckets as well.

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

A

Yeah. I would just add that, think about some of those elements that Mark just talked about, is cost of manufacturing versus cost of sales. There is a timing element that ultimately moves from your balance sheet to your P&L. And it – we're cycling some of those things, as Mark talked about on absorption, as he mentioned.

Jason English
Analyst, Goldman Sachs & Co. LLC

Q

That's helpful, thank you. And Mark, Carrie, another sort of higher-level question on the outlook for snack foods, the notion that snack foods are growth advantaged has come under some pressure recently, supported by the data.

If you look at consumption data, there's been pretty sharp deceleration of volume trends across numerous snack food categories. I'd love to hear you opine on what you believe is driving that deceleration whether or not you think we are sort of pivoting into a period where the growth advantages of snack foods are behind us. And if so or if not, why, what drives that expectation?

Mark A. Clouse
President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. It's a great question, Jason. I think what you're starting to see is a little bit more bifurcation within snacking. So, I do think there are places where we are seeing greater pressure, especially where, I would say, segments are a bit more commoditized.

What's interesting in the first quarter, if you look at our results, you saw power brands, right, which are now about two thirds of our business continuing, I would say, albeit at a slightly lower rate of growth than we may have had in the past, but still certainly a healthy delta versus what I would say the average for total food was, doing fairly well and continuing to perform well and even the underlying vol/mix trends on that business for the quarter, they were essentially flat for the – I think, down just under 1% for the power brands.

But what you are seeing is some of the – a pretty healthy step down on a couple areas, both the partner and the contract brands, that's a little bit more of our catalyst of managed continuing to optimize DSD and I talked about that for the first time in more of a complete way.

And I know a couple questions there that I'll answer in Q2 and give everybody kind of a full picture of margin timing and a few other things that I know we owe to folks. But I think what I would say is, we continue to work actively, although an important part of our business to manage that effectively.

And then some of our non-core snack businesses were weaker in the quarter. And they tended to be segments where you had a little bit more pressure from private label or competition in general. I would point to bread, was a little bit weaker in the quarter and things like microwave popcorn and some other areas that, albeit not power brands, certainly are not insignificant and had a little bit of headwind.

So, I think there's going to be a period here, Jason, where although I would suggest that overall, you may see a little bit of pressure on some of those categories, but we have to remember too, I mean, these snacks businesses, last year at this time, most of these power brands were growing at 20%. And so, even when I put the in-market 3% growth up against that business and combine it over a two-year horizon, you're still talking about strong double-digit growth over the last couple of years. And so, it's always a little hard to get the calibration of what's a trend that's going to sustain and what's kind of the normalization a little bit of the business. So, I still feel very bullish about it. I think we're going to, again, not unlike we're doing in other categories, have to stay very vigilant on what consumers are looking for and making sure that we're positioned well. But I would say, so far, so good relative to how we're seeing that play out.

Operator: Your next question comes from the line of Jim Salera from Stephens. Your line is open.

Jim Salera
Analyst, Stephens, Inc.

Q

Hi guys, good morning. Thanks for taking our question. Mark, I wanted to drill down a little bit on the snacking, particularly Lance and Late July posted, I thought, very impressive share gains. Just offer some color on what's driving the strength of those two brands in particular compared to kind of the broader power brands portfolio.

Mark A. Clouse
President, Chief Executive Officer & Director, Campbell Soup Co.
A

Yeah. There's a lot – those are quite – those are two quite interesting brands because they do both highlight, I think, consumer dynamics that may feel a little bit of tension with one another, but are fueling the categories. We actually see this on Meals & Beverage (sic) [Meals & Beverages] (00:52:54) and on Snacks. So, let me take Late July first. I would say, Late July is a more premium added-value brand. And we are seeing our premium brands doing extremely well. And part of the factor that underpins this is a lot of the decline that we're experiencing actually a significant outsize of contribution is coming from low-income households, which index on snacking only at about 20%, but they represent a much bigger portion of our declines, whereas the premium brands that index higher to the mid and higher income levels have been very stable, if not growing at fast rates.

And so, I think Late July is a well-positioned brand in that added value and elevated space and thus, within those consumer segments remains extremely relevant and the growth rates continue to perform very well.

Lance is interesting because Lance is really a brand that, in our snacking portfolio, does really index high to value. And one of the things that we're seeing is demand for that sandwich cracker segment, and in particular, Lance has been extremely high. And when you think about the price point, the value, even the content, right, protein delivery, the perception of value of food relative to spend, it is a very, very high performing brand and one that is doing very well.

So, you can imagine among the more challenged consumer base, that particular business is just right on target and we've seen demand doing – going up pretty dramatically across that whole portfolio. So, it is a really good example of two very different macro trends that we're experiencing within the businesses, both snacking and Meals & Beverages.

Jim Salera
Analyst, Stephens, Inc.
Q

Great. That's helpful. And then maybe to wrap up on some of the innovations you guys have, if we think about, especially in Goldfish, are these innovations meant to bring new households to the brand? Obviously, Goldfish is a very well-known brand.

Mark A. Clouse
President, Chief Executive Officer & Director, Campbell Soup Co.
A

Yeah.

Jim Salera
Analyst, Stephens, Inc.
Q

Is it meant to kind of expand the buy rate with core Goldfish consumers? Or are you still kind of in search of adding incremental households that maybe don't buy the core products, but would be enticed by an innovation?

Mark A. Clouse
President, Chief Executive Officer & Director, Campbell Soup Co.
A

Yeah. I would say consistent with what our ongoing strategy has been, which is broadening usage of Goldfish to the entire household. We have always been a powerhouse with kids and not surprising, I think, to many of ourselves as our own behavior may indicate is that once it's in the household, more of the family tends to eat it. But we've not necessarily brought offerings that index a little bit more or specifically meet more of the expectations of either teens or even adults in the household. And that strategy over the last couple of years, whether it was Frank's RedHot or OLD BAY or Mega Bites, the innovation has been paramount into driving that. And one of the things that we mentioned in the call today, this is now going on two years of being the number one requested snack among teens. And that's everything, right? That's the brands you think of as being kind of these mega teen snacks and Goldfish has been number one.

And so, when you think about a product like Crisps, where you really are intermingling kind of potato chip behavior with cracker behavior to get this kind of light munchable texture on Goldfish, it's a perfect fit for that. But we also want to make sure that kids target, we continue to meet their expectations as well. So, you love to see a maple-flavored Elf product on Graham as well.

So, I think the goal for us is to continue to be that number one choice for kids while enabling the entire household to be fans of it. So, I would say, I would expect that to be – to manifest itself in both buy rate as you hope that a kid's household is buying couple more packages of some of these other innovations or flankers or that we hold on to households longer. So, as the kids age up, you're actually maintaining Goldfish in that repertoire even if it may be through a Crisp or a Mega Bite as an extension into a longer and older set of kids or households.

Operator: Ladies and gentlemen, we have reached the end of our question-and-answer session. This does conclude today's conference call. Thank you for your participation. You may now disconnect.