



Conagra Brands

Q1 FY25 Earnings Call

October 2, 2024

CORPORATE PARTICIPANTS

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Sean Connolly – *President and Chief Executive Officer*

David Marberger – *Chief Financial Officer*

PRESENTATION

Melissa Napier

Good morning. Thank you for listening to our prepared remarks for Conagra Brand's first quarter earnings. At 9:30 eastern time this morning, we will hold a separate live question and answer session on today's results, which you can access via webcast on our Investor Relations website. Our press release, presentation materials, and a transcript of these prepared remarks are also available there.

I'm joined this morning by Sean Connolly, our CEO, and Dave Marberger, our CFO. We will be making some forward-looking statements today. And while we are making those statements in good faith based on current information, we do not have any guarantee about the results we will achieve. Descriptions of our risk factors are included in our filings with the SEC.

We will also be discussing some non-GAAP financial measures. Please see the earnings release and the slides for GAAP to non-GAAP reconciliations and information on our comparability items, which can be found in the Investor Relations section of our website.

I'll now turn the call over to Sean.

Sean Connolly

Thanks, Melissa. Thank you all for joining our first quarter fiscal 25 earnings call. Before we begin, I'd like to extend our sympathies to everyone affected by Hurricane Helene. We are

supporting World Kitchen, American Red Cross, and Feeding America, and will continue to monitor the situation to determine how we can further help those in need.

Now let's get started on slide four. Q1 marked another quarter of progress in many areas, and I'm proud of the way our team executed within a dynamic environment. We took the actions we told you we would take, and by and large we got the results we expected to get. We told you last quarter that Q1 would have plenty of noise in it, and it did.

Beyond the anomalies we planned for, we had one out-of-plan dynamic to contend with. Today, we will endeavor to unpack the quarter and provide a clear understanding of the underlying state of our business, which is encouraging. In fact, the most important thing for you to take away from our call today is that we remain on track to achieve our fiscal 25 goals.

We had clear priorities for Q1 and delivered on all of them. We continued to drive meaningful volume improvement in our domestic retail business, including year-over-year growth in our strategic frozen and snack domains. Our share improvement stands out - not just in the absolute, but among peers, as we drove strong share performance across the majority of the portfolio.

Continuing to drive our value-over-volume strategy in Foodservice helped us sustain our margins at pre-COVID levels, despite channel softness. We continued to advance our supply chain productivity initiatives, which remain on track to deliver \$1 billion of cost savings by the end of fiscal 25.

And finally, we were excited to resume our portfolio reshaping initiatives with the acquisition of FATTY Smoked Meat Sticks, which expanded our leading position in the high growth, high margin meat sticks product category, as well as the divestiture of our Indian joint venture, ATFL.

Our team delivered on these priorities despite an out-of-plan dynamic that pressured performance during the quarter, namely a manufacturing disruption that required us to pause production at our Hebrew National hot dog plant in the middle of grilling season.

While we were able to fully resume plant operations, the temporary manufacturing pause resulted in lost sales. Revenue for the Hebrew National brand was down 47% in Q1. We estimate that this equated to a 60 basis point reduction in total volume and a 90 basis point reduction in total organic net sales during the first quarter. The loss was particularly apparent within Refrigerated and Frozen, where we estimated that it accounted for a 150 basis point reduction in volume and a 210 basis point reduction in organic net sales for the segment. We estimate that the majority of the impact of this disruption will be isolated to the first quarter.

Taking all of this into account, our results for the quarter were in-line or above our internal plan for most metrics except organic net sales, which was impacted by the temporary manufacturing disruption I just discussed. I'm pleased with our team's continued execution against our key priorities, which has strengthened the underlying momentum of our business. As a result, we remain on track to deliver our fiscal 25 guidance.

Let's take a closer look at each of our priorities, beginning with our volume progress on slide five. As you can see, our proven playbook and strategic investments have generated continuous volume recovery in our domestic retail business over the past year. In fact, domestic retail volume performance in Q1 exceeded our expectations, and our volume recovery would have been higher but for the temporary impact of Hebrew National.

Importantly, as you can see on slide six, we delivered year-over-year volume growth across both our strategic domains, frozen and snacks. We've focused our investments to maximize consumer engagement within these domains, and their return to growth demonstrates that our plan is working.

Slide seven shows the volume trends in our staples domain. Excluding the temporary disruption in hot dogs, the rest of our staples domain also delivered sequential volume improvement during the quarter. And don't forget, Q1 staples volume was impacted by the elasticity effect of last year's price increase on our tomatoes platform.

Since we wrapped those pricing actions as we exited Q1, this impact will wane going forward. And to give you a sense of the magnitude, staples consumption in Q1 ex-tomatoes and hot dogs would also have been positive. So overall, while we anticipate the consumer environment will remain a challenge in fiscal 25, our proven ability to navigate through it gives us confidence that we will continue to drive volume across our business.

Even more impressive than the strength of our volume improvement is our share performance, seen here on slide eight. Achieving four consecutive quarters of share progress is a solid achievement in any period, but to do so amid today's challenging consumer environment underscores the strength of our strategy and the resiliency of our portfolio. In Q1, approximately 71% of our portfolio held or gained volume share, and the vast majority of that was share gains.

And as you can see on slide nine, our share performance is far ahead of our near-in peer set. Only one of our closest peers has more than half of their portfolio holding or gaining share, and we are outperforming them by a solid margin.

If you zoom in on our strategic frozen and snacks domains, shown here on slide 10, the share performance is even stronger. 93% of our frozen and snack brands held or gained volume share during the quarter. This slide demonstrates the continual improvement of our share performance over the past year, highlighting the effectiveness of our enhanced investments to drive consumer engagement.

Importantly, we continue to deliver volume progress and strong share gains while achieving the expected ROI. Slide 11 demonstrates how the industry merchandising environment remains rational.

There are two key metrics to consider when evaluating the state of merchandising - the share of volume sold on promotion and the average depth of promotion. In both key metrics, Conagra and our near-in peer set are promoting slightly less today than we did in the most comparable pre-pandemic period. Said differently, the overall promotional environment is roughly consistent with historic norms.

And when you double click on each of these metrics, you'll find that Conagra is actually less promotional than our closest peers. Both today and in the pre-pandemic period, Conagra sells a lower percentage of our volume on promotion. And when we do have targeted promotions, our average discount is also less.

The takeaway is clear. We continue to operate in a rational merchandising environment. Conagra remains less reliant on promotions to drive volume, and we continue to maintain a disciplined approach to prioritize the long-term health of our brands.

Now let's dive into each of our domains. Starting with frozen on slide 12, our Q1 volume sales outpaced both edible and relevant frozen categories, led by our strong volume share performance in single-serve meals and share increases in vegetables and multi-serve meals.

Slide 13 takes a closer look at single-serve meals, our largest frozen category. Conagra now represents a majority of all industry volume in this \$6.5 billion dollar category, a tremendous achievement in this dynamic and competitive environment. Our investments have enabled us to drive steady share improvement in this category throughout fiscal 24, and we built upon that success during the first quarter of fiscal 25.

Frozen vegetables is another category that contributed to our improved share performance during the quarter. Recall that Birds Eye was the focus of our value-over-volume approach as we pulled back activity on the commodity vegetable space while building our business and innovation pipeline in the premium value-added space. As you can see on slide 14, our efforts are paying off. Our frozen vegetables business remains stable and positive.

Moving to snacks on slide 15, we continue to considerably outpace the total snacking category, largely due to our advantaged portfolio. Our brands span on-trend, permissible snacking subspaces like meat snacks, popcorn, and seeds as consumers opt for low-carb, protein and fiber-rich snacks offered by Slim Jim, Duke's, David, Angie's BOOMCHICKAPOP, and more. Permissible snacking is growing much faster than the overall snacking category, and our portfolio of well-known brands is benefiting.

During the first quarter, we took another step to build upon this strength by welcoming The FATTY to the Conagra family. Slide 16 highlights some of the key points that make this acquisition so attractive.

Conagra is a leader in the meat snacks category with significant scale. But within meat snacks, Conagra is the leader in meat sticks, a high-margin business that is growing faster than all other snacking categories, as demand for more convenient, healthy, and affordable experiences continues to attract new buyers.

FATTY Smoked Meat Sticks joins consumer favorites Slim Jim and Duke's to form a trifecta smokehouse, which will allow us to capitalize on high growth, protein-focused snacking behaviors. The addition of a premium brand like The FATTY furthers Conagra's position of strength as we focus on growing our snacking business across advantaged categories.

Turning to our Foodservice business on slide 17, it's no secret that COVID posed an unprecedented challenge for the entire foodservice industry, and our Foodservice segment was no exception. Over the last five years, we've been laser focused on building a better business and returning margins to pre-COVID levels.

As a result of our efforts, over the past few years we grew organic net sales and adjusted operating profit. And this past year, we were able to restore Foodservice margins to their fiscal 19 levels. During Q1, we sustained that margin as we continued to execute our value-over-volume strategy.

Our margin recovery has also been supported by our efficient and effective supply chain, highlighted here on slide 18. We expect to drive approximately \$350 million in savings during

fiscal 25 through multiple productivity initiatives. Further, Q1 service levels remained at the strong pre-COVID level of 97%.

We also continued to deliver improvements in free cash flow, reducing our cash conversion cycle by seven days relative to the prior period. As a result of these efforts, we remain on track to deliver \$1 billion of cost savings by the end of fiscal 25. Our productivity initiatives remain a key tool in our strategic playbook, as the savings we realize help fuel our brand-building investments and portfolio reshaping efforts.

Turning to slide 19, we were excited to resume our historical practice of active portfolio reshaping with both inbound and outbound activities. Consumer tastes and habits are constantly changing, and we continuously evaluate opportunities to reshape our portfolio to position the company for further growth and margin expansion, whether that be through investments in innovation and brand modernization, M&A, or value-accretive divestitures or spins.

Portfolio reshaping is in our DNA, and Conagra has taken substantial actions over the past decade to transform our portfolio. However, in recent years, we've been more single-mindedly focused on debt paydown. Now, given the progress we've made on debt and cash flow as well as other market dynamics, we are in a strong position to resume active portfolio reshaping and, importantly, still meet our long-term 3.0x net leverage target through a combination of bolt-on acquisitions and divestitures of low growth businesses.

In Q1, we advanced these efforts through the acquisition of The FATTY and the divestiture of our majority stake in Indian subsidiary Agro Tech Foods Limited. Looking ahead, we will continue to assess opportunities to reshape our portfolio for faster growth and stronger margins.

As discussed at the top of the call, our execution across each of our priorities in Q1 has reinforced our confidence in the underlying strength of our brands, people, and strategy. With that, I'm pleased to reaffirm our fiscal 25 guidance.

I'll now pass the call over to Dave to discuss our financials in more detail.

Dave Marberger

Thanks, Sean, and good morning, everyone. Slide 22 shows our financial results for key metrics in the quarter. Sean provided a good overview of how our business performed in Q1, highlighting our continued volume improvements in domestic retail, share gains, and strong productivity. To most effectively unpack our Q1 results, I'll move to our segment performance on the next slide.

Slide 23 shows the composition of organic net sales by segment and also highlights the estimated impact of the Hebrew National manufacturing disruption on total company sales. Total organic net sales excluding Hebrew would have been down 2.6%, or 90 basis points better than the minus 3.5% we delivered.

In Grocery and Snacks, we delivered organic net sales of approximately \$1.2 billion, a decline of 1.9% versus last year's first quarter, primarily from lower volumes. Price/mix decreased slightly, a result of investments in selected brands, partially offset by a price increase taken in the prior year on our tomato business.

Our Refrigerated and Frozen segment delivered approximately \$1.1 billion in net sales, a decline of 5.7% from prior year. Volume and price/mix were both impacted by the temporary manufacturing disruption in Hebrew National. Excluding Hebrew, we estimate that Refrigerated and Frozen net sales in the quarter would have been down 3.6%. Volume for the quarter would have increased 1.6%, and price/mix would have been down 5.2%.

Refrigerated and Frozen price/mix was impacted by pass-through pricing reductions in certain brands that were experiencing deflation, primarily in our spreads business, and increased trade merchandising investments, particularly in our frozen business. We also experienced a shift in the mix of product sold, which was a headwind to price/mix in the quarter.

Our International segment delivered an organic net sales increase of 3% over prior year, driven primarily by another strong double-digit quarter in our Global Exports business.

Finally, our Foodservice business performance continued to be impacted by the lower margin business we exited that was first called out in our Q3 fiscal 24 call, along with ongoing softness in restaurant traffic. As Sean discussed, our Foodservice business is larger and more profitable than it was at the start of the pandemic and remains an important contributor to the Conagra business portfolio.

Slide 24 shows our net sales bridge. I've already unpacked the quarter's volume and price/mix dynamics for you. The remaining elements are foreign exchange, which negatively impacted net sales by 40 basis points, largely driven by the US Dollar to Mexican Peso exchange rates, and 10 basis points of favorable impact from the acquisition of FATTY Smoked Meat Sticks.

The components of our Q1 adjusted operating margin bridge are shown on slide 25. Adjusted operating margin declined 244 basis points over prior year to 14.2%. In addition to the price/mix and trade merchandising investments I've already discussed, we also saw year-over-year cost of goods sold inflation of 3.3%, primarily from proteins, sweeteners, and warehousing costs. SG&A was higher due to wrapping lower incentive compensation a year ago, and foreign exchange was a headwind.

Productivity improvements, which approximated 3.6% of cost of goods sold, helped fund our trade investments in the quarter. This productivity was partially offset by the impact of the Hebrew National disruption. We don't expect these unfavorable costs to continue going forward.

Slide 26 details our adjusted operating profit and adjusted operating margin performance by segment for Q1. All segments reported a decline from prior year in adjusted operating profit and adjusted operating margin, and all segments were impacted by the same dynamics, primarily lower organic net sales, which included increased merchandising investment, higher cost of goods sold inflation, and unfavorable operating leverage, partially offset by favorable productivity.

Additionally, Refrigerated and Frozen adjusted operating profit was impacted by approximately \$10 million from the manufacturing disruptions in Hebrew National, and our International segment saw an outsized negative impact from unfavorable foreign exchange rates.

The adjusted EPS bridge for Q1 fiscal 25 is shown on slide 27. Adjusted EPS was \$0.53 in the current quarter compared to \$0.66 a year ago due to a decline in adjusted operating profit, unfavorable FX rates, and lower equity earnings from Ardent Mills. Pension and adjusted taxes contributed \$0.01 of EPS in the quarter. Our Ardent Mills joint venture continued to perform well

in its core flour business but delivered lower commodity revenue in Q1 compared to last year due to lower market volatility.

Key balance sheet and cash flow metrics are shown on slide 28. Conagra generated \$269 million in net cash flows from operating activities in Q1. The decline from prior year was driven primarily by lower operating profit and changes in seasonal working capital that we expected. Capital expenditures were \$133 million, dividends paid were \$167 million, and we resumed share repurchases of \$64 million to offset dilution from our share-based equity incentive compensation plans.

Our Q1 fiscal 25 ending net debt reduction from prior year reflects debt paydowns during fiscal 24, and includes funding the Q1 acquisitions of both the FATTY Smoked Meat Sticks business as well as the manufacturing operations of an existing co-manufacturer of our cooking spray products. Net leverage at the end the quarter was 3.6x and was in line with our expectations, as we remain on track to finish the fiscal year around 3.2x.

In addition to the acquisitions in Q1, we also closed on the sale of our ATFL business in India. The net of those three transactions resulted in additional cash uses of approximately \$154 million. We remain focused on reducing our net leverage and continuing to generate strong free cash flow.

As Sean said, we are reaffirming our full year fiscal 25 guidance as shown on slide 29. I will provide some more color on the next slide.

As we stated last quarter when initially providing our full year fiscal 25 guidance, we expect sequential volume recovery each quarter, and we expect adjusted operating margin improvement to be greater in the second half. For Q2, we expect improvement in volume, top-line, and margin compared to Q1.

We do expect our fiscal 25 merchandising investment to be at the highest level in Q2. Also, we are now forecasting full year fiscal 25 inflation of approximately 3.2% of total cost of goods sold. That is up from approximately 3% originally projected for the year.

We are seeing inflationary pressure primarily in the areas of proteins and sweeteners. While we are seeing deflation in select areas such as edible fats and oils, the net impact is a 20 basis point increase in the annual overall inflation estimate.

We don't expect any material impact on fiscal 25 margin or adjusted EPS from our first quarter M&A transactions, but we expect a decrease in overall reported net sales of approximately \$30 million for the remainder of the fiscal year.

Our year-end net leverage target of approximately 3.2x assumes expected favorability in free cash flow resulting from improved working capital, lower expected capital expenditures, and lower estimated cash taxes from a favorable tax settlement. And finally, we expect full year adjusted gross margin to be relatively flat versus fiscal 24.

That concludes our prepared remarks for today's call. Thank you for your interest in Conagra Brands.