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The Hershey Company

Third Quarter 2024 Earnings Results
Prepared Remarks

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CORPORATE PARTICIPANTS

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Michele Buck, *Chief Executive Officer and Chairman*

Steve Voskuil, *Senior Vice President and Chief Financial Officer*

PRESENTATION

Anoori Naughton

Good morning everyone and welcome to the pre-recorded discussion of The Hershey Company's Third Quarter 2024 Earnings Results. I'm Anoori Naughton, Senior Director of Investor Relations. Joining me today are Hershey's Chairman and CEO Michele Buck, and Hershey's Senior Vice President and CFO Steve Voskuil.

In addition to these remarks, we will host an analyst Q&A-only session at 8:30 a.m. Eastern on the morning of November 7. A replay of this webcast and our subsequent Q&A session will be available on the Investor Relations section of our website, along with their corresponding transcripts.

During the course of today's discussion, Management will make forward-looking statements that are subject to various risks and uncertainties. These statements include expectations and assumptions regarding the Company's future operations and financial performance. Actual results could differ materially from those projected. The Company undertakes no obligation to update these statements based on subsequent events. A detailed listing of such risks and uncertainties can be found in today's press release and the Company's SEC filings.

Finally, please note that during today's discussion we will refer to certain non-GAAP financial measures that we believe will provide useful information for investors. The presentation of this information is not intended to be considered in isolation or as a substitute for the financial information presented in accordance with GAAP. Reconciliations to the GAAP results are included in this morning's press release.

It is now my pleasure to introduce our Chairman and CEO, Michele Buck.

Michele Buck

Thank you, Anoori. Good morning, everyone and thank you for joining us today.

The operating environment year-to-date has been challenging with historically high cocoa prices and a stretched consumer continuing to impact our results.

Before I address those items further, I want to first emphasize that regardless of the external environment, the foundation of our business remains intact, as do the fundamental reasons for Hershey's success. We have a diversified portfolio of resilient brands in growing categories, the right strategy in place, and winning commercial capabilities like ubiquitous distribution, a strong in-house retail sales force, category management leadership, and supply chain scale and agility.

Consumers across the income spectrum are making budgetary trade-offs and shopping differently this year, however, our data shows consumers continue to want to participate in snacking occasions.

Confection products are part of the most memorable moments in our consumers' lives, like birthdays, celebrations, and seasonal occasions. For more than a decade, chocolate has consistently ranked the #2 Most Eaten snack, which means it is also an integral part of consumers' everyday lives. The chocolate category has grown at a 4% CAGR since 2009, with positive growth every year for more than two decades. This is an incredibly resilient category that remains healthy in '24, with everyday candy, mint, and gum consumption up over 2% year-to-date and continuing to outpace broader snacking in Q3.

While our categories remain relevant to consumers, our performance this quarter was impacted by both industry-wide and Hershey-specific challenges.

Relative to sector-wide headwinds, total snacking consumption softened to +0.1% in the quarter from +0.9% in Q2, as consumers continue to seek value, budget for meals, and prioritize satiety. This has pressured trips to convenience and drug stores, where we over index. Those trips dipped further year-over-year in Q3. The broader evolution of shopping preferences is shifting trips into channels like club, dollar, and online, where our categories are less developed. Lastly, we saw a continuation of customers managing inventory more tightly, impacting our outlook for both North America Confectionery and North America Salty Snacks.

Relative to Hershey specific challenges, in the third quarter we experienced increased pressure across all our segments.

First, similar to other categories, we continue to see increased competition in confection. In the U.S., we have lost share to smaller players and private label, particularly in take home chocolate where we had gained significant share of shelf through the pandemic. In our key international markets we've seen an increase in activity from large global manufactures.

Second, we experienced executional issues with our plans in both Confectionery and Salty Snacks. For example, Olympics' promotional programming fell short of our expectations as it competed for attention and resources with Back to School. In North America Salty Snacks, we experienced replenishment delays as we executed planned route-to-market changes. As a result of these pressures, we are sharpening our seasonal planning and occasions strategies to respond.

We feel good that the second-half growth plans we discussed last quarter are gaining momentum, though we continue to strive to accelerate our pace of execution.

- Last quarter we said consumption trends would improve as we lapped the onset of merchandizing reductions at a key retailer and as we added new items in Fall resets. Our everyday candy, mint, and gum business with that retailer increased 2.3% in the latest twelve weeks, and we are gaining 23 basis points of share the latest four week period. Excluding the convenience channel, our total everyday candy, mint, and gum business has also returned to growth in the last month.

- We continue to have bigger, more impactful innovation. Reese's Caramel is the #1 Innovation in the category this year and Reese's Lava is off to a strong start and outperforming expectations. In fact, Reese's held share in Q3 despite outsized convenience and drug channel and programming pressures.

- We prioritized the acceleration of our Sweets portfolio and shared the additions of Shaq-a-licious Gummies and Jolly Rancher Ropes that are intended to accelerate our sweets growth into 2025 and beyond. Our Sweets consumption accelerated from 5% in August, to 9% in September, and

23% in October to date, with share gains progressing from flat, to up 30 basis points, to up 130 basis points over those time periods, respectively.

- We anticipated we would deliver on our Halloween expectations, and overall seasonal participation remained solid as we expected. Our shipments and seasonal sell through are in-line with our low-single-digit growth outlook, and we gained share for the fifth consecutive season.

- Finally, we have delivered on our plan to address SkinnyPop declines and expect the brand to return to growth in the fourth quarter. Consumption has inflected from down (1)% in the last 12 weeks to +8% growth in the latest four weeks, resulting in a 260 basis points share gain in ready-to-eat popcorn. And we've seen Dot's sustain strong momentum, up +31% in Q3 and nearing a milestone of $500 million at retail in the last 52 weeks.

Given our fundamentals and momentum in key areas, we remain confident in our long-term strategy.

As we go forward, we know it will continue to be a challenging environment, but we are focused on controlling what we can in Q4 and 2025 to drive category growth and improve our market shares across our business in Confectionery, Salty Snacks, and International. We are taking near-term and longer-term actions to position ourselves competitively for today and into the future.

On North American Confectionery, we are pleased to welcome Mike Del Pozzo to lead the U.S. Confection business. Mike brings significant food and beverage as well as transformation expertise from PepsiCo. In his first several weeks, he has been engaging with customers and distributors, spending time in market with our retail sales team, and listening to our employees with a focus on improving agility and speed. There are a few priorities where he will focus.

Our first priority is reigniting chocolate. For instant consumables we intend to expand implementation of our Gold Standard planogram to improve productivity and findability, and margin accretive growth for retailers. Trade and media investment is being redeployed to efficiently support Variety brands like Almond Joy, Mounds, PayDay, Cadbury, and Rolo, which have stronger velocities and brand equities than many new items, and drive value for consumers and customers. In take home chocolate, we will deliver value through promotional optimization and compelling price pack architecture. And we are confident we will continue to win merchandising share in faster growing, value-oriented retailers.

We also continue to be relentless in accelerating our sweets growth. We are expanding our recent innovation launches nationally, while rolling out new flavors and forms like Jolly Rancher Freeze Dried.

Finally, we plan to continue delivering share-winning seasons, by leveraging scale partnerships like Harry Potter, and delivering best in class seasonal execution.

In North America Salty Snacks, we have seen continued growth, demonstrating the strength of our diversified portfolio. We intend to maintain and grow our share leadership through exciting partnerships, including a new celebrity brand ambassador, and innovative package designs for SkinnyPop. We have plans to continue to accelerate household penetration through investment in media and scaled promotions, while leveraging our Retail sales team to enhance our in-store execution.

In International we are investing for growth in our focus and new growth markets. We are accelerating the growth of our Power brands - Hershey's, Pelon, and Kisses - in Mexico through targeted investments. We expect to deliver accretive global innovation, focusing on both core and new markets like LATAM, the UK and Australia, and we are optimizing our go-to-market strategy to engage more consumers in key growth markets like India.

In addition to our portfolio action plans, we are also continuing to transform our business for long-term sustainable growth. In the third quarter, we executed the next phase of our operating model to better align our organization and our capabilities, and drive more efficient growth.

- This includes evolving our marketing organization to have a stronger portfolio focus and better address evolving consumer needs.

- We are continuing to integrate our supply chain across Confectionery and Salty Snacks to unlock efficiency and scale, leveraging our new ERP platform.

- And lastly, we are rebuilding our technology group and advancing capabilities in data science and technology to enable deeper consumer and category insights.

Based on the current consumer and channel pressures we now anticipate sales growth to be approximately flat, down from our prior guidance of approximately 2% growth, and adjusted EPS to be down by mid-single-digits from our prior guidance of down slightly.

As we look ahead, we are confident in our ability to deliver on-algorithm top-line growth for 2025 as we end 2024 with improved momentum and stronger plans. Cocoa fundamentals are improving, and we believe there will be a global supply surplus in 2025 driven both by a recovery in West Africa and significant production growth in the rest of the world. Despite that, cocoa prices have remained high. Earnings, as expected, will be impacted by this historically high cocoa inflation, in addition to mix headwinds, and a few one-time benefits in 2024 that won't repeat. Steve will cover these topics in more detail.

In closing, we are managing this business for the long-term. Our team is taking action to control the variables we're able to control, and we are carefully monitoring those we cannot. We are addressing consumer and customer evolution, while also making organizational changes needed to ensure the long-term competitive health of our business.

With that, let me turn it over to Steve to provide more details on our financial results and outlook.

Steve Voskuil

Thank you Michele, and good morning everyone.

Third quarter reported net sales declined 1.4%, as approximately 2 points of price realization was more than offset by volume declines. As Michele noted, we fell short of our expectations due to softer consumption trends across our segments, incremental retailer inventory contraction and seasonal shipment delays, in addition to the planned lap of inventory increases ahead of last year's ERP implementation in the North America Salty Snacks segment.

Our North America Confectionery segment delivered organic, constant currency net sales growth of 0.9%. Price realization contributed approximately 2 points of growth in the quarter. Volume was impacted by retailer inventory management efforts across both seasonal and everyday confection. While we saw a greater-than-planned increase in everyday retailer inventory, seasonal shifts continued as Halloween shipments that moved from Q2 into Q3 were partially offset by Holiday deliveries shifting from Q3 into Q4.

The net impact of these inventory items was a 1 point benefit to volume in Q3. Excluding these items, the base business declined slightly, driven by weaker than planned consumer trends, higher competition, and softer than planned summer promotional effectiveness.

The North America Salty Snacks segment net sales decline of 15.5% reflected an approximate 13 point headwind from lapping the planned inventory build ahead of the ERP implementation in Q4 of last year, as well as a mid-single-digit headwind from retailers reducing inventory levels. Excluding these items, the base business net sales increased low-single digits reflecting continued strength in Dot's Pretzels, partially offset by the planned shift of a SkinnyPop promotion into Q4, higher levels of competitive investment, and order timing shifts into Q4 due to the planned route to market changes. As Michele mentioned, we're pleased that SkinnyPop has returned to growth in recent weeks behind media, distribution, and merchandising increases, and we continue to expect growth in Q4. We also expect strong growth from Dot's, albeit moderating against last year's club distribution gains, as our new flavor, Parmesan Garlic, expands distribution.

Our International segment reported a net sales decline of 3.9%. Organic, constant currency net sales were approximately flat, as about 1 point of price realization was offset by volume declines in Brazil and Mexico.

Based on our third quarter performance, we are revising our total company net sales outlook to flat year-over-year. Our reduced outlook reflects our Q3 performance, sustained consumer, competitive, and channel pressures into Q4, as well as lower than planned year-end retailer inventory levels in both confection and salty snacks. As Michele discussed, we are taking actions to improve base business performance across all three segments. In the fourth quarter, we have good visibility on mid-single-digit sales growth from confection Holiday shipments, two extra shipping days, and the lap of planned inventory drawdown following the Q4 2023 ERP implementation in Salty Snacks.

Adjusted gross margin of 40.3% was below expectations reflecting volume deleverage from lower-than-expected shipments and unfavorable mix. We now expect full year adjusted gross margin to decline approximately 250 basis points year-over-year, reflecting our reduced volume outlook and sustained channel and product mix headwinds, along with previously anticipated cocoa and sugar inflation, which more than offset net price realization and supply chain productivity.

Advertising and related consumer marketing decreased approximately 1% in the third quarter as higher investment in our North America Salty Snacks and International segments was more than offset by efficiencies in consumer marketing related expenses in North America Confectionery. Adjusted operating expenses, excluding advertising and related consumer marketing spend, declined approximately 14% due to reduced compensation and benefit costs and decreased capability and technology investments versus the prior-year period.

Our "Triple A" initiative remains on track to deliver at least $100 million in savings this year, primarily within division and corporate expenses, and will continue to build in Q4 relative to Q3.

The adjusted tax rate for the quarter was 15.2%, a decrease of 5.2 points versus the year-ago period, due to higher levels of renewable tax credits in the current period and adjustments to tax reserves in the prior year period. We now expect a full year adjusted tax rate of approximately 11%, which is lower than our previous outlook, driven by increased visibility into renewable energy projects to be completed this year. As a result, other expense is now estimated to be between $260 million and $270 million. The net effect of both adjustments leaves our overall tax impact relatively unchanged.

Interest expense of $44 million in the third quarter was in line with expectations and we now expect full year expense of around $170 million.

Capital additions, including software, were $128 million in the quarter, supporting our previously discussed capacity expansion projects. We now expect full year capital investments of $575 million to $600 million based on improved visibility to on-going projects.

We remain committed to our capital allocation priorities, including reinvestment for growth, dividends, and share repurchases. In the third quarter, dividends paid to shareholders totaled $270 million, an increase of 13.7% versus the prior year period. The Company did not repurchase any shares in the third quarter against our December 2023 $500 million authorization, with $470 million remaining.

Adjusted earnings per share declined 10% in the quarter, as lower sales and gross margins were only partially offset by reduced SG&A related to lower compensation and benefit costs. Our full year adjusted EPS is now expected to be down mid-single digits, driven by the reduction in our top-line and gross margin outlook.

Before we wrap this morning, I want to address the cocoa market and touch on 2025.

We are pleased to see cocoa fundamentals improving, with multiple data sources indicating a global supply surplus in 2025. The crop outlook in West Africa is positive, and cocoa arrivals in Ivory Coast ports are up 27% compared to this time last year. Moreover, production outside of Ivory Coast and Ghana now accounts for nearly half of global supply and is growing, driven by record high prices.

However, low liquidity on the exchange is contributing to sustained high prices, and normalization may occur gradually as cocoa production builds and origin sales continue in earnest. We have robust processes in place to ensure continuity of supply and good visibility into our costs. However, remember that we were well covered for 2024 when we provided our full year outlook in February, and cocoa prices remain significantly above those and prior year levels.

Regarding 2025, as Michele said, we anticipate an on algorithm top-line growth, driven by strong plans, the benefit of a longer Easter, the flow through of previously announced pricing and price pack architecture, and fewer headwinds than we experienced in 2024. However, historically high cocoa costs, other commodity and supply chain inflation, unfavorable mix, and elasticity more in line with historical rates, will more than offset our pricing, productivity, and cost savings initiatives. While we have flexible hedging structures that would allow us to participate in downside cocoa cost normalization, based on what we know today, we expect higher levels of cost of goods sold inflation throughout 2025 than we experienced in 2024. Additionally, bear in mind that earnings in 2024 included a historically low economic tax rate and reduced incentive compensation, which are not expected to repeat in 2025. As usual, we will provide a detailed full year 2025 outlook with our Q4 earnings.

Despite another year of expected commodity-driven earnings pressure in 2025, we will continue to invest to drive top line growth, market share, and innovation that delights consumers. We remain confident in our ability to support peer leading margins through efficiencies and cost savings programs over time.

With that, I will turn it back to Michele for closing remarks.

Michele Buck

Thanks Steve.

We remain confident in the strength of our categories, brands, people, and strategy to deliver long-term top and bottom-line success. We are continuing to invest to secure our competitive positioning and build our next platforms for future growth in 2025 and beyond.