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The Hershey Company

Third Quarter 2023 Earnings Results
Prepared Remarks

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CORPORATE PARTICIPANTS

Melissa Poole, *Vice President, Investor Relations*

Michele Buck, *Chief Executive Officer and Chairman*

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

PRESENTATION

Melissa Poole

Good morning everyone and welcome to the pre-recorded discussion of The Hershey Company's Third Quarter 2023 Earnings Results.

My name is Melissa Poole and I'm the Vice President of Investor Relations at Hershey. 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 October 26. 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 Melissa, and good morning everyone.

We remain on track to deliver our full year sales and earnings commitments after delivering strong seasonal sell in and successfully implementing our new Salty Snacks ERP system in early October. Halloween is well underway and the shelves are full to meet consumer demand these last few important days. We continued to support our brands with double digit increases in media during the quarter and we plan to continue this in Q4 to drive unit conversion on both our seasonal and everyday items.

As we finish the year, our teams are focused on building momentum to position us well for 2024. Our retail teams are delivering best-in-class seasonal merchandising to secure strong sell-through, while our sales teams are partnering with retailers to begin shipping our 2024 innovation for Q1 execution.

We have a robust pipeline of innovations for 2024 and we couldn't be more excited to kick things off with our Reese's Caramel launch. Our recent technology and capacity investments in our largest brand will enable us to bring the top category flavors together in a unique way that only Reese can deliver. Product testing indicates strong trial and repeat interest, and our customers are excited to partner with us to bring it to life in stores with incremental merchandising.

As we look to 2024, we are closely monitoring recent consumer trends to inform our strategies and company priorities.

As many of you know, sector growth has slowed as pricing moderates and consumers across income cohorts are increasingly focusing on value. Many are cutting back on discretionary purchases, looking for deals, shopping at discount channels, and buying smaller sizes. We have also seen more category and brand switching, with deflationary perimeter categories and more satiating foods outperforming.

Hershey has a strong distribution across classes of trade, including presence in channels where consumers are increasing trips such as dollar, club and discount stores. We are increasing focus on these channels and partnering with retailers to capitalize on the incrementality of snacks and confection in baskets. We are also leaning into our brands that deliver on consumers' need for value and satiation including Dot's Pretzels, ONE and Fulfill nutrition bars, PayDay bars and our sweets portfolio.

With more stable supply chain performance and increased capacity, our teams are evaluating price pack architecture opportunities to ensure we have the right offerings and price points to meet consumers' changing needs. And we are looking to optimize our investments in trade and media to ensure we have the right mix of each along with the right price points, in store execution and brand equity, to drive profitable growth.

Now let me provide a few details on each of our segments.

Within North America Confectionery, everyday chocolate sales growth slowed in the third quarter as elasticity increased, as expected. We continue to plan for more historical price elasticity in Q4 and 2024.

The category has also been impacted by distribution and merchandising reductions at a key retailer over the past several months. Given Hershey's high share of merchandising and strong gains over the past several years, we have been disproportionately impacted by this change. We are actively partnering to develop solutions that enable our retailers to meet their goals while also capitalizing on the incrementality and expandable nature of our high-margin category to optimize results in 2024.

As we exit the year, we expect confection retail trends to improve as consumers prioritize seasonal traditions and in-store seasonal merchandising levels remain comparable to prior year.

Hershey Halloween retail sales to date are up slightly versus prior year and we are outperforming the category. Consumers have returned to purchasing their trick or treat candy closer to Halloween after supply chain and availability concerns spurred earlier purchases last year. With Halloween next Tuesday, we still have several important selling days to go, and our teams are hard at work ensuring consumers have all their favorite treats to buy for this important holiday. This includes our amazing retail team members and a record number of corporate and other non-retail employee volunteers helping set up merchandising displays and filling store shelves. Thank you to all of our employees who work so hard every day to help create and be a part of these special moments of goodness.

Shifting to our everyday non-chocolate portfolio, Hershey Sweets retail sales grew nearly 9% in the quarter as category trends remain favorable and strong innovation is helping us secure incremental distribution. Hershey gum and mint products grew nearly 12% as the category continues to rebound from lower mobility. Hershey growth is outpacing the category due to improved supply chain performance versus the prior year period. We expect both Sweets and Refreshment to continue to perform well in the fourth quarter.

Within our North America Salty Snacks segment, our teams did an excellent job building inventory in the quarter to prepare for our October ERP transition and a fantastic job with implementation. The new system is now up and running and we are successfully taking and shipping orders.

Dot's Pretzels had a terrific quarter, driven by strong category growth and share gains in both measured and non-measured channels. After a successful test over the past several months, Dot's secured permanent distribution in a club retailer helping drive overall retail sales growth of 36% in the quarter.

While the pretzel category is performing well, the ready-to-eat popcorn and puffs categories slowed considerably in the third quarter as back to school multi-pack purchases were muted and consumers shifted to more filling salty snacks. SkinnyPop and Pirate's Booty were both impacted by these category trends. We expect Q4 Salty Snacks consumption trends to be comparable to Q3, with an additional net sales headwind related to the planned inventory drawdown associated with the ERP implementation.

Within our International segment, growth decelerated across markets reflecting heightened competitive activity and a moderation in category growth. Results were also impacted by our choice to exit a lower-margin beverage product in Mexico earlier this year, as well as timing of shipments in India and Brazil that shifted into the fourth quarter. Our teams remain focused on distribution expansion across markets and executing on seasonal orders to drive growth. We expect Q4 trends to be slightly better given shipment timing in India and Brazil, a new marketing activation in Australia, an innovation launch in Europe, and an easier year-ago comparison.

Before I turn it over to Steve, let me briefly touch on a few critical enterprise priorities. Our supply chain capacity initiatives remain on track for this year and our incremental capacity has enabled us to meet customer seasonal demand, improve our service levels and lean into productivity initiatives. We have a few projects already underway to complete in '24, but will then return to more historical levels of capital spending as utilization reaches our targeted level.

After successful ERP implementations in Mexico last year and Salty this month, our teams are beginning to shift focus to our U.S. transition next spring. Our teams have already put in a tremendous amount of effort to prepare for this transition. With our cross-functional expertise and lessons learned from Mexico and Salty, we believe we are well positioned to successfully deliver this important milestone next year in our largest market.

Steve, let me now turn it over to you for more perspective on our financial results and outlook.

Steve Voskuil

Thank you Michele, and good morning everyone.

In the third quarter, we delivered 11.1% net sales growth and 19.8% adjusted earnings per share growth, a reflection of our team's ability to adapt and execute in an evolving consumer environment.

Our North America Confectionery segment delivered organic, constant currency sales growth of 10.1%. Price realization contributed 11 points of growth to the quarter. We will begin to lap 2022 price increases in the fourth quarter, and therefore, expect pricing to moderate slightly and be a high-single-digit benefit versus a year ago.

Volume was a 1% headwind in the segment, slightly better than expected due to the timing of seasonal shipments from Q4. Overall, seasonal growth contributed nearly half of segment growth in the quarter, along with strong growth in non-measured channels which helped offset everyday declines driven by price elasticity.

Our North America Salty Snacks segment organic constant currency sales growth of 25.5% reflects an approximate 16-point benefit from planned inventory increases ahead of our ERP implementation. The base business grew mid-single digits, aided by new Dot's distribution in the club channel. We continue to expect fourth quarter organic sales to decline low double digits as we ship below consumption as we emerge from the ERP transition and execute fewer promotional programs.

Organic constant currency sales for our International segment declined 1.2%. This partly reflects planned items, such as the discontinuation of a dairy beverage product line in Mexico and a later holiday season in India, in addition to heightened competitive activity in several key markets as category growth moderated. We expect sequential volume improvement in the fourth quarter, driven by strong Diwali and Ramadan shipments, as well as incremental activations and innovation in targeted markets, which should more than offset a 4-point headwind from the exit of the Mexico beverage product line.

For the full year, our overall net sales outlook of around 8% is unchanged. In the fourth quarter, we expect everyday elasticities to be in line with historical levels, and shipments to lag consumption due to the seasonal timing we discussed earlier, as well as normalization of inventory levels.

Moving down the P&L, adjusted gross margin increased 240 basis points in the third quarter as pricing and productivity gains more than offset inflation and higher manufacturing and overhead costs. This was slightly ahead of our expectations due to fixed cost leverage, timing of productivity and sourcing mix, as well as favorable manufacturing and logistics costs. We now expect full-year gross margin expansion at the high end of our previously communicated range of 80 to 90 basis points.

Advertising and related consumer marketing increased 20% in the third quarter, with investment up double-digits across segments. Adjusted operating expenses, excluding advertising and related consumer marketing spend, increased 8.1%, driven by compensation and benefits inflation, as well as incremental capability and technology investments. Looking to the fourth quarter, we expect advertising spend to grow double-digits as we continue our strong support for sell-through of seasonal items and begin to reactivate our Salty Snacks brands coming out of our ERP transition. We expect non-advertising SG&A spend to increase low-single-digits, reflecting a small increase in technology and capability investments.

The adjusted tax rate for the third quarter was 20.4%, an increase of 450 basis points versus the year-ago period. This increase was primarily driven by fewer renewable energy tax credits in the quarter versus the prior year. While our net overall tax outlook is relatively unchanged, we now anticipate a full year adjusted tax rate of approximately 15%, and Other expense to be in the $225 million to $230 million range. Remember that Other expense primarily reflects the write-down of the renewable energy investments that qualify for tax credit.

Given our visibility into seasonal shipments, incremental distribution, and inventory and inflation headwinds in Q4, our full-year outlook for adjusted earnings per share growth remains at 11% to 12%, consistent with our prior outlook.

Capital additions, including software, were $218 million in Q3, supporting our previously discussed capacity expansion projects and ERP implementations. Our full-year capital spending outlook is unchanged. As

Michele mentioned, the second half of 2023 represents a high watermark for capital spending as several capacity projects near completion.

We remain committed to our capital allocation priorities, including reinvestment for growth, dividends, and share repurchases. In the quarter, dividends paid to shareholders totaled $238 million, an increase of 14.8% versus the prior year period. The Company did not repurchase any shares in the third quarter against our May 2021 $500 million authorization and $370 million remains.

As the operating environment continues to evolve, I am confident that our teams and our business will continue to respond with agility and excellence to deliver another year of differentiated results.

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

Michele Buck

Thanks, Steve.

The environment remains very dynamic. We are focused on identifying and responding to these changes to ensure we have the right portfolio, the right strategies and the right talent to meet the changing needs of our consumers for many years to come. We will continue to invest in our brands and our capabilities to drive sustainable long-term growth, while at the same time having a relentless focus on prioritization and efficiencies to get the most out of our resources.

We have iconic brands in great categories, strong margins, and financial flexibility to invest for the future. We thank you for your continued support and interest in the Company.

I invite you to listen to our live question and answer webcast which will begin today at 8:30 a.m. Eastern Time and will be available at thehersheycompany.com. Thank you.