



The Hershey Company

Second Quarter 2025 Earnings Q & A Session

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C O R P O R A T E P A R T I C I P A N T S

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C O N F E R E N C E C A L L P A R T I C I P A N T S

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Max Gumport, *BNP Paribas*

Megan Clapp, *Morgan Stanley*

Peter Galbo, *Bank of America*

James Salera, *Stephens Inc.*

David Palmer, *Evercore ISI*

Robert Moskow, *TD Cowen*

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Leah Jordan, *Goldman Sachs*

David Palmer, *Evercore ISI*

Michael Lavery, *Piper Sandler*

Scott Marks, *Jefferies*

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PRESENTATION

Operator

Greetings and welcome to The Hershey Company Second Quarter 2025 Question-and-Answer Session.

To join the queue, please press star, one on your telephone keypad. At this time, all participants are in a listen-only mode. As a reminder, this conference is being recorded.

I would now like to turn the call over to your host, Anoori Naughton, Vice President of Investor Relations for The Hershey Company. Thank you. You may begin.

Anoori Naughton

Good morning everyone and thank you for joining us today. I hope everyone has had the chance to read our press release and listen to our prerecorded management remarks, both of which are available on our website. In addition, we have posted a transcript of the prerecorded remarks. At the conclusion of today's live Q&A session, we will also post a transcript and audio replay of this call.

Please note that during today's Q&A session, we may make forward-looking statements that are subject to various risks and uncertainties, these statements including 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 we may 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.

Joining me today are Hershey's Chairman and CEO, Michele Buck, and Hershey's Senior Vice President and CFO, Steve Voskuil. Before turning it over, I would personally like to thank you, Michele, for being an inspiring force. Your clear vision and unwavering dedication to excellence have shaped this company and will continue to motivate us for years to come.

With that, let's get started with the first question. Operator?

Operator

Our first question is from Andrew Lazar with Barclays. Please proceed.

Andrew Lazar

Great. Thanks so much. Good morning everybody.

Michele Buck

Good morning.

Steve Voskuil

Good morning.

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Andrew Lazar

Great. Michele, congratulations to you. Best wishes going forward. And congratulations to Kirk as well as he prepares to take the helm in mid-August.

Michele Buck

Thank you.

Andrew Lazar

My question, Michele, is that oftentimes when a new CEO comes in, it can be seen as an opportunity to sort of rebase earnings and margins, to set a company up for the next several years, particularly if it's a situation where there's been, let's say, underinvestment. Kirk will obviously come in, get under the hood and make his own determination, but I guess from where you sit, if we put issues like cocoa and tariffs aside, do you see the underlying health of the business as in need of this sort of a reset? I guess, more importantly, what specifically did you and the Board see in Kirk that made him the right choice?

Michele Buck

Sure. So first of all, I'll reiterate, certainly, as Kirk walks in he'll have the opportunity to form his own opinion. But what I would share is, as you know, Hershey has been a company that has stated our belief in investments in brands and capability over time to consistently ensure that we can drive sustainable growth and we have proven that we consistently do reinvest during periods of change.

As we got hit by some of the record high cocoa prices, early on we stated that our approach was going to be taking a long-term approach to ensure continued category health, and we've done that. We've continued to spend on our brands. We've invested in technology with our new ERP platform and then new AI and tech-enabled capabilities that have driven significant efficiency, whether in the transformation program or other places.

On top of that, we're seeing top line momentum on the business. We have our profit recovery plans well underway and we'll talk more about that today. As I look at the past 18 months where we've faced headwinds, I then also look at the future where I would say I see more opportunity given the fundamentals of cocoa, the direction that they're headed in, and perhaps even with tariffs.

If I put all of that together, I don't see a need to really reset. I think we've been consistently investing and we have momentum on our side.

Andrew Lazar

Thank you for that. Yes, Kirk.

Michele Buck

Kirk and what made him the best candidate, I mean, certainly Kirk has three decades of experience in consumer packaged goods at Pepsi, a leading talent house. He's got very relevant experience in snacking and then also in beverage, which has many corollaries to our business. It's not only an iconic brand business; it's also a pack type business, ubiquitous distribution across channels, so a lot of similarities.

He is also very focused on being consumer-centric, customer-centric and the importance of culture in delivering results. So I think all of that and to his kind of performance orientation will make him be a great person to continue moving forward our ambition to be a leading snacking powerhouse and continue to deliver sustainable growth.

Andrew Lazar

Great. All right. Thank you for that.

Then a quick one, Steve. Just it appears at least as a starting point in '25, you're looking for elasticity of roughly 1:1 on the new pricing that was recently announced. Is this a reasonable expectation for '26 as well? At least at this stage, just given the magnitude of the pricing being taken? How do you assess elasticity when it's certainly a greater amount of pricing than you've typically taken in a situation like this? Thanks so much.

Steven Voskuil

Sure. As you can imagine, our teams have modeled this exhaustively. I'd put up our strategic revenue management team against anyone very, very thoughtful in the way we've approached this. Overall, the elasticities are probably a little bit more favorable than what we've seen in history, but part of that is because of the breadth. There are parts, as we know, parts of our portfolio like seasons that are a little bit less elastic. There are other parts that are more elastic. And so as we set both the pricing assumption and the elasticity assumption, we did that with a very thoughtful, modeled approach. Now, we'll be watching it closely but right now, we feel we've got a good bead on how it will play out for this year and next year.

Andrew Lazar

Great. Thank you.

Operator

Our next question is from Max Gumport with BNP Paribas. Please proceed.

Max Gumport

Hey, thanks for the question, and Michele, congrats as well. I hope you enjoy the retirement.

Michele Buck

Thank you.

Max Gumport

At CAGNY, you observed that if your realized cocoa costs in '26 matched your costs in '24, then you could do \$10 plus in adjusted EPS in '26, and I realize we're nowhere near that situation currently, and we also now need to factor in tariffs as well which were not contemplated in that math. That said, with the announced price increase it does seem like your pricing will very much close the gap to the total COGS inflation that you have seen in recent years in dollar terms, which with regard to EPS might have an equivalent impact as costs falling back to '24 levels. Also, your comment of the price increase and other initiatives supporting 500 basis points or more of gross margin expansion in '26 before considering partial offsets from cocoa cost and tariffs would support that reasoning as well.

I'm hoping you could provide a bit of a finer point on how to read the impact of this pricing for next year and what it might mean for your P&L, specifically, if cocoa futures were to hold at current levels. I realize there's a lot in there but I'm hoping for a bit of an update on that. Thanks so much.

Steven Voskuil

Sure. I can definitely give some perspective.

You're right. When we gave that back at CAGNY, talked about \$10 and \$12 possibilities with assumptions from '25 and '24 carrying forward without inflation. Some things have changed since then, tariffs being the biggest one, right? Tariffs wasn't contemplated at the time of that thinking and that will continue to be something that we have to work to optimize while also working to see if we can get relief, particularly on the cocoa component of that.

But that aside, this pricing move does make a material impact in the right direction of margin recovery for 2026. It does not, by itself, recover all of the cocoa inflation that we have seen up to 2025. So it's a big step in the right direction, but it's not enough to fully compensate for cocoa inflation up to this point.

As we look forward, all of the other levers are going to continue to be important. We talked about in the prepared remarks Smart Complexity. You've seen us take our transformation savings up. We're going to continue to look at all of those levers to extract more cost savings and margin points so that we, over time, do fully recover our margin expectations. But this price increase, while significant, doesn't get us all the way to flat year-over-year.

Now, having said that, some things do feel more optimistic than maybe they did even on our last call. Cocoa has come back some. And like everyone, we're trying to be thoughtful as we execute our hedging program and plan for cocoa next year. It is still inflationary from what we know today, but it's taken a step in the right direction. We'll continue to optimize tariffs. But if we could get relief and either tariffs or cocoa reverts back, either one of those could give us a path to something better than on-algorithm earnings for 2026, which is a little bit different than probably we thought in our last conversation.

Max Gumport

Great. Then just related to the pricing, how should we think about any need for incremental reinvestment next year to support that price increase and keep the consumer coming into your brands and your franchises? (Cross-talking).

Steven Voskuil

Yes, into our pricing assumption—and Michele touched on this already. We always want to make sure that we're investing back in the brands, that we're investing on competitive events with our customers. We've got a big innovation calendar already planned for next year. We've got some big tentpole events around Olympics and the Hershey movie, and so we feel like those will be fully funded. And of course, we'll be agile when we get into it and if we do see pressure in some spots or the elasticities are not what we expected, we can revisit.

Max Gumport

Okay. Thanks very much. I'll leave it there.

Steven Voskuil

Thank you.

Operator

Our next question is from Megan Clapp with Morgan Stanley. Please proceed.

Megan Clapp

Hi. Good morning and congratulations to Michele as well. I wanted to ask about the nonseasonal performance in CMG in the quarter. I think you talked to mid-single-digit growth in the quarter. That's better

than we'd seen previously, and you still have a lot of activations planned for the second half. And I think you were expecting some incremental shelf space alongside some of those plans in the second half. So maybe, A, you could just expand on what you've seen in that nonseasonal portfolio in the second quarter and what's driving the acceleration? And then, B, how you're thinking about second half growth and kind of the puts and takes? Thank you.

Michele Buck

Sure. So first of all, we're feeling very good about what we're seeing on overall chocolate category growth, and there are really three key factors that we think are driving a lot of what we're seeing. First of all, innovation. The consumer has really responded to innovation. As the consumer looks for value, significant innovation makes a difference and delivers value. And there's been a lot of investment in innovation across the category.

Secondly, we do know that our products provide emotional well-being and comfort during stressful times, and we've seen some correlations as we look at studies that are out relative to consumers' mindset and emotional well-being and where we're seeing growth tick up in the category.

We also have had some periods where we were lapping some soft comps and that helped us relative to every day as well. But I think those overall trends tend to be some of the biggest drivers.

Then certainly, we also have seen some nice tick up from how we approached Instant Consumables and some of the choices that we made to really partner with retailers to broaden shelf space and innovation on Instant Consumables. We saw some very strong positive results and growth behind those programs and we think as pricing hits the market that we will only see that growth kind of maintain and become a bit stronger. We feel really good about what we're seeing.

That said, I would say we're not sure that we will see the category stay at the same level of growth that we saw in Q2. Some of the year-on-year comps will get a little bit tougher.

Megan Clapp

Okay. That's super helpful. Thank you.

Then maybe just a follow-up for Steve to the answer to Max's question. I think you said if relief in tariffs or cocoa—if relief in tariffs happen or cocoa reverts back, you could get to better than on-algo for '26. So I guess, is it fair to say at this point you do expect you could deliver on-algo growth versus the updated '25 guide in 2026?

Steven Voskuil

Yes. Based on what we can see today—and again, things like tariffs are rapidly moving—but based on what we can see today, yes, we see on-algorithm earnings growth and top line growth for next year.

Megan Clapp

Awesome, thank you. I'll pass it on.

Operator

Our next question is from Peter Galbo with Bank of America. Please proceed.

Peter Galbo

Hey, good morning Michele and Steve. Thanks for the questions and congrats to Michele as well.

Michele, maybe I wanted to take the tariff discussion in a little bit of a different direction. I think last quarter you started hinting at some conversations that you all had been having as it relates to potential exemption. I think the Commerce Secretary even made some comments yesterday about cocoa potentially getting exemption, or at least in his words. So just curious if you can give us an update there in terms of the discussions that you're having and kind of how you've maybe seen that evolve relative to three months ago?

Michele Buck

Sure. So I would say that we are even more optimistic now. As we've had conversations over the past several months, we have become increasingly comfortable that the government administration understands some of our concerns about the fact that cocoa can only be grown and sourced outside of the U.S. And so we feel good that they really understand that issue broadly, and we have started seeing more commentary more publicly addressing that, like the comments that Secretary Lutnick made just yesterday. We believe that gives us a lot of optimism.

We understand that there are still country negotiations that are underway that have to come to fruition and so the whole cocoa tariff has to be a broader part of that, but we are optimistic relative to the fact that there are now public statements being made about this issue.

Peter Galbo

Great. Thanks for that, Michele. Then if I actually pivot to Halloween, I think in your prepared comments, again, there was a little bit of maybe a pull forward on shipments from Q3 into Q2. Just want to understand that dynamic. But then also, I believe you had pretty optimistic outlook for Halloween, so I just want to understand kind of what's underlying that view as we get into that season. Thanks very much.

Michele Buck

Yes. I wouldn't make too much of those accelerated shipments. We see shifts over the years between when Halloween ships between Q2 and Q3. That's not uncommon. Some years the customers want to set the category a little bit earlier and that's actually a good thing for us. We think we also may be seeing a bit of this mid-summer wean in. There's been a social media trend around Summerween, which is earlier Halloween celebrations, which has really somewhat taken off with certain consumer groups. So we know that some customers are focused on that. As we talk to customers, we feel really good that there are plans in place to deliver another strong Halloween in '25. Retailers are definitely excited to set the bar higher this year and continuing to deliver an exciting season for the customers.

Peter Galbo

Great. Thanks very much.

Operator

Our next question is from Jim Salera with Stephens, Inc. Please proceed.

James Salera

Again, good morning. Thanks for taking our question.

I wanted to shift gears and maybe ask a little bit on the salty snacks piece of the portfolio, because salty as a category has been pressured this year and yet it seems like you guys are seeing strength in both Dot's and SkinnyPop, which I think play in kind of different value propositions, one obviously more better for you, one more indulgent. Can you just speak to what you're seeing there that's allowing you to deliver kind of

above category trends? Then maybe speak to any opportunities to increase multipack distribution because that's something you guys called out in the prepared remarks.

Michele Buck

Yes. So first of all, both Dot's—pretty much our entire portfolio in Salty Snacks does have a permissible and premium halo. Popcorn—clearly, SkinnyPop is pretty obvious. But as you think about pretzels, pretzels are perceived as better for you than many other salty snacks, so even Dot's has a bit of that permissibility halo.

Across those businesses, we just continue to see strong consumer acceptance and momentum. As we bought those businesses, they were relatively nascent, so continue to have upside in driving household penetration, just getting more consumers to be aware of the brands, continued opportunities to gain distribution. And now we've really dialed up the marketing with new packaging on SkinnyPop, our Jennifer Aniston program, exclusive flavors on Dot's like Buffalo that have generated a lot of consumer interest and fit into some important tentpole events around sports and football.

Then price pack architecture has been another opportunity of just continuing to fill out all the sizes and price points. So between flavor innovation, price pack architecture, engaging with the consumer, there just continues to be momentum.

We've also launched some innovation that is kind of between the seams of some of our categories. For example, Reese's Peanut Butter Filled Pretzels, which has recently hit the market, which is a phenomenal product that leverages our sweet and salty together.

Then you hit multipacks, and I'd say that's just another lever of growth. Frankly, multipacks are of significant size in Salty Snacks, and we're really filling out our portfolio there, both in terms of single items as well as leveraging the breadth of our portfolio to deliver. So we're continuing to expand the SKUs in that space and gain more distribution there.

James Salera

Maybe just one more thought on multipacks. Are you able to leverage some of the innovations that you have and kind of package that together in sort of kind of an innovation-centric multipack offering that would highlight some of the different innovations you have across the portfolio and make that a little bit more front and center and maybe allow the consumer to kind of try all your innovations in one package?

Michele Buck

Yes, we certainly can combine across the portfolio. For example, we've done a Reese's one that we put together that included our Reese's Animal Crackers, our Reese's Filled Pretzels. So yes, we're doing a lot of consumer insight work to optimize what are the most compelling combinations across our portfolio. And we've really just gotten some of these multipacks into the market, so this is an area where there's a lot of upside ahead of us.

James Salera

Great. I appreciate the color, Michele. I'll hop back in queue.

Operator

Our next question is from Robert Moskow with TD Cowen. Please proceed.

Robert Moskow

Hi. Thanks and I just want to extend my congratulations to you, Michele, for such a great track record and creating so much value at Hershey over the years. I wish you the best.

Michele Buck

Thank you.

Robert Moskow

You're welcome. I wanted to ask, though, about the Instant Consumables part of the business. I think you say in the press release, or the transcript that everyday chocolate as a category was up 6.7%. Your everyday chocolate is up less than that and I wanted to know how you would gauge your competitiveness in that segment of the market right now. I thought this is the part where you felt like you had more work to do. Are you seeing any improvement?

Then one extra thing. I think you said that you thought that the category growth rate may not be as strong in the back half because of comparisons. Can you be more specific what those comparisons were? I don't recall from last year. Thanks.

Michele Buck

Yes. So I'll start on Instant Consumables. We do feel like we have made progress there and our numbers demonstrate that. In Instant Consumable, we are now gaining share and growing ahead of the category. We feel good about the actions we put in place relative to partnering on our gold standard planograms, which enabled us to expand distribution, get more breadth of our portfolio on the shelves to make the shelves even more productive. We think that, that will continue going forward, so we feel good about the program that we committed to and executed in the first half of the year.

Take-home is where we have seen some pressure. That's where we've had more pressure on the business, particularly from private label and some of the better-for-you and insurgent brands. It's one of the reasons that as we launched Oreo, we're really focusing on take-home because we believe innovation is what's really needed to capture shelf space and to capture the consumers' mind share of the take-home set.

Relative to year-on-year comparisons, the comparisons are particularly tough in Q4, as that's when we really started to ramp up our big innovation for '25, at the end of '24. So that's really what's driving that lap.

Robert Moskow

Okay. Thank you.

Operator

Our next question is from Alexia Howard with Bernstein. Please proceed.

Alexia Howard

Good morning everyone, and congratulations, Michele. Wishing you all the best for your retirement. And welcome to Kirk.

First question, could you talk about the pace of innovation and how it stepped up over the last couple of years? It feels as though you're really firing on all cylinders now and I'm wondering if you're able to quantify exactly how things have stepped up? And are you at the pace that you would like to be after maybe a quieter period during COVID and the global supply chain reductions?

Michele Buck

Yes, so you're absolutely right about that. We have dialed up our innovation. We measure our innovation as a percent of net sales and try and target where we think we need to be to really fully leverage that innovation without overleveraging innovation at the expense of the core, because we know the core is highly profitable and want to make sure we're focused on that. Our levels are up significantly versus 2019.

What we're seeing in the category, frankly, is a little bit more innovation is absolutely necessary in order to compete, particularly for shelf space with some of the insurgent brands and also private label. And innovation is also perceived as value from the consumers who are looking for value.

So I do think that we've done a really nice job of getting to a good stride as we look to '26, and also getting innovations out there that we do think can really play a sustainable role in the category.

If you think about the innovation that we've put forth in Sweets, around Jolly Rancher, Ropes, freeze dried, the Shaq brand, our M&A in Sour Strips, really strategic in terms of hitting new consumers and new occasions. And then also some really big innovation such as the Oreo one that we announced that we think gives us a good blend of news, incrementality and disruption.

Alexia Howard

Great. Thank you. As a follow-up, it seems to me that there may be some incremental headwinds to consumer demand in indulgent snacking as we enter 2026: the GLP-1 pill version coming out, potential SNAP benefit reduction at the individual state level in terms of what SNAP can be spent on and soda and candy maybe coming out of that. How are you thinking about that as a potential impact next year? Obviously, the innovation, the marketing are obviously going to counter that, but is that something that we should be factoring in? Thank you and I'll pass it on.

Michele Buck

Yes. I'd say, first of all, relative to GLP-1s, we continue to see no material impact in '25. Certainly, we are always monitoring very closely, but at this point we're not expecting it to be significant in '26.

We broadly look at the consumer trend as it relates to health and wellness. As you know, there's been, over time, a continuous pressure of consumers being more and more interested in products that have those types of benefits. And as well, we always watch kind of the national conversation around health and how that may evolve and change anything. So we're closely monitoring that to make sure our portfolio has offerings that appeal to all consumers' desires.

As it relates to SNAP, the way that the rollout is slated, we aren't expecting material impact in '26 and '27. Frankly, given the choice of reducing SNAP or removing CMG, we're less concerned with removing CMG, because it does still give the consumer SNAP dollars to fund their groceries, but they can also choose to spend on confection. As we look beyond '27, it is something that we are monitoring to factor into our planning.

Alexia Howard

Great. Thank you very much and wishing you all the best for the future. Thanks, Michele.

Michele Buck

Thank you.

Operator

Our next question is from Leah Jordan with Goldman Sachs. Please proceed.

Leah Jordan

Thank you. Good morning. Just wanted to go back to the pricing discussion, see if you can help us understand the phasing of the pricing actions you're making in the back half and into '26. I guess, ultimately, why does taking this magnitude of pricing make sense now given the assumption for 1% elasticity as it's often just better to keep people in the category versus trying to win them back later?

Michele Buck

I'll start and throw it over to you.

Certainly, I think pricing makes sense as we look at the continuous pressures that we've had from cocoa pricing on our P&L. We are committed to margin recovery and pricing to cover inflation over time, so that is part of our long-term strategy. We've said all along we were going to watch prices and certainly if we could delay taking an increase, do so, but we think that's important.

We also believe we're still delivering, and we know we're still delivering compelling value across our portfolio. Over 75% of our items are under the \$4 price point. And frankly, we're in pretty good shape on that as we look at where we are relative to the other snacking options in the marketplace.

As we think about 2025 in particular, in terms of impact of pricing, if you think about the rest of the year, we have about 40% of our second half orders that aren't impacted by pricing, given the predominance of seasons in the back half. So between seasons and then also the support behind Oreo and the momentum there, we're not going to get as full an impact in the back half.

Steve, I don't know if you want to talk about anything more broadly going forward.

Steven Voskuil

Yes. I would just say that for this year, the impact, about 2 points to the enterprise on the top line, and then obviously, most of that is going to be in the fourth quarter. Then as we look to next year, it's more mid-teens, the impact. About 80% of the profit benefit will happen in '26 with a little bit of flowthrough to '27 on seasons. The first season to be impacted will be Easter '26, so hopefully that gives you some idea of the profile.

Michele Buck

The other thing I would just add is we view pricing as a strategic way to allow us to continue to invest in our brands and to drive the long-term health of the category with new capabilities, etc.

Leah Jordan

That's very helpful. Thank you.

Operator

Our next question is from David Palmer with Evercore ISI. Please proceed.

David Palmer

Great. Thanks. Congrats, Michele. And also congrats to Kirk, and welcome.

A quick follow-up on the pricing. Does that mid-teens pricing, is that inclusive of tariff-related pricing? I'm assuming so. And if so, what happens if we do see that exemption from cocoa in the near term? Does that get adjusted? How should we think about that? And I have a follow-up.

Steven Voskuil

Sure. Yes. Just to be crystal clear, the pricing has nothing to do with tariffs. This is strictly a catch-up on cocoa component. As we said, we're not fully caught up even on the '25 inflation yet.

David Palmer

All right. So are you currently having discussions where you're talking about two different levels if we see—is there a dual-track discussion happening on that through year-end? Because I would imagine there's one window, so how are you thinking about that?

Steven Voskuil

Yes. I think it's too early. This is now in the market. We talked about it earlier. We want to make sure we execute this with excellence, see what the elasticities look like, and then see what happens. We said we have some optimism relative to tariffs going forward, particularly on cocoa, and we'll continue to watch the cocoa markets, but too early to think about that next step.

David Palmer

You mentioned 80% of that would flow through next year in a previous answer. If we just were to back up and just look at that North American confectionery price mix flow-through in '26, what sort of flow-through should we be expecting from that level of pricing in '26?

Steven Voskuil

I think we're going to begin to see mid-teens again overall for U.S. CMG. We'll start from the first quarter, and then obviously as we talked about with Easter being the first season, there will be a pretty quick start with the new pricing next year for that business.

David Palmer

Got it. So we should be expecting double-digit price mix to be flowing through in '26? Starting in '26.

Steven Voskuil

Right, yes.

David Palmer

Yes, yes. Got it. Helpful. Thank you very much.

Steven Voskuil

You bet.

Operator

Our next question is from Michael Lavery with Piper Sandler. Please proceed.

Michael Lavery

Thank you. Good morning and congrats as well, Michele. Just wanted to come back to the color you gave on the 2026 gross margin recovery. Can you give a sense? You've talked about how it reflects the pricing and the cost savings, but can you give a sense of what assumptions that reflects for cocoa and maybe how much you're already covered for 2026 at this point as well?

Steven Voskuil

Sure. Yes, we won't share specifics on coverage for 2026 other than to say our policy hasn't changed. We continue to follow our policy. We still have an expectation, as we talked about, that cocoa is ultimately going to come down, so we're factoring that into our thinking around coverage and the structures that we're using to hedge. But we are still, based on what we see today, seeing inflationary cocoa for '26. And again, part of that's based on some of the hedging benefits that we carried into '25 and off that base into 2026.

Now we'll watch closely what happens with cocoa in the balance of the year and that could move around, but right now, we're expecting it to be inflationary.

Michael Lavery

Okay. That's helpful. Just as far as a follow-up on the tariff mitigation, you mentioned you're not obviously pricing for that yet. You said that you will mitigate your tariff exposure over time if they endure. Is that just pricing or do you have other levers? What do those plans look like?

Steven Voskuil

Yes. Right now, we're focused on what we can do in the supply chain. We've got the benefit of a very agile supply chain. We've invested a lot in agility, automation, a lot of cross-border opportunities, and so we're going to continue to optimize the supply chain part of this. We've done some of that already, but I will say for this year the impact is relatively small. But as we go forward, that's going to be, I'll say, the principal focus until we see what happens with tariffs long term.

Michael Lavery

Would that be just a different country of origin shift? What supply chain flexibility is there to impact the tariffs?

Steven Voskuil

Yes. I mean there are impacts of where we manufacture. We've got capacity here in the U.S. for some things. It's a mix of what we insource/outsource, and what countries that is located in. It's sort of all of those things.

Michael Lavery

Okay, great. Thanks so much.

Steven Voskuil

You bet.

Operator

Our next question is from Scott Marks with Jefferies. Please proceed.

Scott Marks

Hey, good morning. Thanks so much for taking our questions and again, congrats, Michele, on a great, great career. And congrats to Kirk coming in and taking over.

I wanted to ask a little bit about the cocoa supply dynamics. You made some comments in the prepared remarks around some investments in new origins. You made some comments about Ivory Coast seeing an increase in fertilizer usage. So, just wondering, as we think about maybe the go-forward supply, how much recoveries may be expected to come from that West Africa region relative to how much is expected to come from sources outside of the West Africa region?

Steven Voskuil

Sure. As we talked about, I think overall, we feel there are good signs on the cocoa market, some of which we're seeing now and some we expect. You saw data recently that grinds have come down substantially sort of high single digits and could be heading lower. Butter ratios have come down from their peak, suggesting some inventory building there potentially. The current crop, we continue to expect a modest surplus and see next year's main crop looking quite strong. So I'd say all of those feel good at this point.

As we talked about in the prepared remarks, we're seeing more fertilizer use, some better agriculture practices, that it's more profitable to farm cocoa.

Then to your question, I think we're going to continue to see the origins outside of West Africa continue to invest and play a larger role. Of course, we've been pivoting into that space already, as many others have as well and I think those other origins have responded by investing more and kind of picking up some of that mantle of a bigger role.

We also have seen more recently speculators have reduced positions and so forth, so I think we can get to a potential larger surplus without further recovery in West Africa and new origins growing double digits and demand continues to decline. So I think we could see more of a fall in the second half.

Scott Marks

Got it. Appreciate the answer on that.

Then last one for me. Just you made some comments about convenience stores, obviously, traffic still being down, but you were still able to grow parts of your Instant Consumables business there. Just wondering, as you think about maybe the go forward in C-store, what kind of response have you had from convenience retailers in terms of some of your new initiatives and innovations? How are you thinking about the outlook for that space?

Michele Buck

Yes. I mean we've had very strong results from the retailers relative to those new initiatives. As we shared in the script, some of the gold standard planogram has certainly resulted in significant category growth for retailers. We always go to the retailers with programs that we believe will not only grow our own business, but will actually grow their category because that's a win-win for both of us. And we know that we've seen significant high single-digit growth in the categories where we've put those plans into place, so there's a lot of momentum with the programming in place.

On top of the momentum we already have, we have innovation coming in the second half, which should further advance the momentum and growth that we're seeing on the portfolio there. E

ven if there are continued declines in trips, I think what we feel good about is that we've been able to still drive our business and drive conversion despite where trips are.

Scott Marks

Got it. Thanks so much. I'll pass it on.

Operator

Our next question is from Chris Carey with Wells Fargo Securities. Please proceed.

Chris Carey

Hi. Good morning everyone.

Steve Voskuil

Good morning.

Chris Carey

One quick modeling question, then something more strategic. On the modeling dynamic, well, just it has an impact on your model—the tax rate coming up for the year, some evolution of tax credits. Steve, is that a permanent dynamic going forward or is that unique to the year? Just maybe a couple of sound bites on what drove that evolution and how durable it is. Then I have a follow-up.

Steven Voskuil

Sure. Yes, happy to take that one.

The tax has been a challenge. We talked about it in the first quarter call as well and I think as we get to this point in the year, it's been even more of a challenge. It's very hard to say what is—in the tax world, as much as changing right now, what is permanent. So I can talk about what's happening now and how we think about it for '26 a little bit.

But the biggest factors right now are a couple of things. One is, that we've talked about before, our teams are being very creative in areas like cocoa sourcing and procurement. Those drive a great ROI for the company, but there are some tax consequences relative to our overall rate that are a bit dilutive. So that's one factor. And I would think about that as, I don't know that I'd say it's sticky, but it's certainly a piece for this year, and I would imagine we'll see some of that next year.

A second piece—and you mentioned the tax credit strategy. The tax credit strategy is impacted by two things. One is our income is lower and so there are limits on how much tax credit availability we have with that income level. And second, with all the change in the world of tax right now, some of the returns we're seeing on tax credits just aren't up to the standard that we look for when we pick those investments. I would see that as also being sticky. I think in the near term, there's not going to be a big change and that's why you see the dial-down between other income and expense and the tax rate kind of going in the opposite direction. All of those together probably give us a 250 basis point headwind on economic tax rate right now that I would expect to carry forward into 2026.

That's the way I think. Beyond that, it's difficult to say. I mean, this is an area that's still evolving pretty quickly.

Chris Carey

Okay. Very helpful.

Regarding 2026, it's a bit of a multilayered question, so apologies. But you have these great initiatives in place that are going to give you what sounds like a gross 500 basis point benefit to gross margin. When you think about the offsets which would get you in that sort of algorithm earnings growth next year, is there a way to frame how much you're thinking about that, which is tariffs relative to lingering cocoa inflation relative to the pricing that you're taking?

Then just connected to that, one of your peers reported last night and we're seeing some, I guess, impact some months forward of more substantial pricing, which has been taken in Europe, and some of the elasticities, which are starting to emerge. Are you able to leverage those pricing actions in-market and the volume impacts that we're beginning to see from an elasticity standpoint to, I guess, better serve you as you think about your own elasticities ahead of this kind of, like, substantial and appropriate price increase going into next year?

Thanks for the gross margin and the elasticity. I appreciate it.

Steven Voskuil

Sure. Well, maybe helpful on the EPS side, taking the first part of your question and just kind of walk through some of the puts and takes on '26 EPS. And again, kind of starting to say we can see a path now to being on-algorithm and if a few things were to break, potential for more than that.

But if I just step back on EPS, obviously we're going to have pricing coming through next year. We're going to have increased productivity and higher transformation savings; that was one of the things we called out on the call this morning. We'll see some greater scale in our core brands, so this is part of that Smart Complexity initiative that we referenced, being very thoughtful about how we leverage the core and drive the core, and that also leads to some margin accretion. Then we'll continue to press on tariffs relative to the cocoa exemption, and that's sort of out of our control, but continue to lean there.

As we talked about on the last question, tax is going to remain high, so I don't see that being any better next year. I can probably look at that as a push to next year.

Then on the other side, the delta, obviously, we talked about incremental cocoa inflation. Elasticity, we'll see what we're going to see there, but along with those elasticities we'll have some absorption impact into the P&L. That is factored into our outlook in that 500 basis points, but that's something we have to account for. Then tariffs can also be a negative if they would happen to go the other way. Those are the kind of big moving pieces inside the puts and takes.

On the elasticity question, I think right now we want to see how our assumptions in the market play out here. And like I talked about I think in an earlier question, we'll pivot if we need to, if we see something concerning on elasticities. We're investing behind our brands, strong innovation agenda, so everything is in place to make this a success, working closely with our customers, but we'll remain agile as we see this in the market.

Michele Buck

Yes. I mean at the highest level, I think Steve said this before, but we feel good about being on-algorithm for '26, and as we look at the puts and takes in the marketplace, we think that there are multiple paths to us seeing EPS be well into that double-digit range pending what happens with tariffs and cocoa costs, which, of course, are the two biggest factors. That is with current cocoa and tariffs as they are that we achieve that on-algo.

Chris Carey

Thank you very much.

Operator

Thank you. There are no further questions at this time. I would like to turn the conference back over to Ms. Naughton for closing remarks.

Anoori Naughton

Thank you all for joining us this morning and we look forward to connecting over the coming days.

Operator

Thank you. This will conclude today's conference. You may disconnect your lines at this time, and thank you for your participation.