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PRESENTATION

Operator

Good morning, everyone, and welcome to The Hershey Company's First Quarter 2019 Results Conference Call.

My name is Catherine, and I will be your conference operator today. (Operator Instructions) This call is scheduled to end at about 9:30 a.m. (Operator Instructions) Please note this call may be recorded. Thank you.

I would now like to turn the call over to Melissa Poole, Vice President of Investor Relations.

Ms. Poole, you may begin your conference.

Melissa Poole - *The Hershey Company - Senior Director of IR*

Thank you, Catherine. Good morning, everyone. We appreciate you joining us for The Hershey Company's First Quarter 2019 Earnings Conference Call and Webcast.

Michele Buck, President and CEO; and Patricia Little, Senior Vice President and CFO, will provide you with an overview of our results, followed by a Q&A session.

Before we begin, please remember that, during the course of this call, we may make forward-looking statements within the meaning of the federal securities laws. These statements are based on our current expectations and involve risks and uncertainties that could differ materially from actual events than those described in these forward-looking statements contained in our 2018 10-K filed with the SEC and today's press release.

Finally, please note that on today's call 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. Please refer to today's press release for a reconciliation of the non-GAAP financial measures to the most comparable measures prepared in accordance with GAAP.

With that, let me turn the call over to Michele.

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

Thanks, Melissa. Good morning to all of you on the phone and webcast.

Our year has gotten off to a strong start, and we remain on track to deliver our financial commitments for the year. I'd like to thank my colleagues across the Hershey business for their focused and hard work. Many of them listen to this call. And I'm very proud of what we have accomplished and the progress we are making.

Now on to the results.

Net sales increased 2.3% in the first quarter, in line with expectations. The net benefit of acquisitions and divestitures was 90 basis points, and foreign currency exchange was a 50 basis points headwind. Organic constant currency net sales growth of approximately 2% was driven by a longer Easter season and international [work], which was partially offset by our SKU rationalization program. We continued to make good progress against our margin improvement plans, which contributed to gross margin expansion of 80 basis points in the quarter versus the same period in 2018. This was slightly ahead of our expectations, driven by incremental efficiencies from our complexity-reduction efforts. These gross margin gains, along with our solid sales performance, drove quality EPS growth of plus 12.8% in the first quarter. This was above expectations, driven by the stronger-than-anticipated gross margin as well as the timing of investments.

Our key initiatives for this year are progressing well. And we remain confident that our balanced plans will enable us to accelerate our U.S. CMG performance, deliver our acquisition models for Amplify and Pirate Brands and maintain our international business momentum.

Net price realization was up slightly in the quarter in line with expectations. Consistent with previous guidance, we anticipate the net benefit of pricing to build over the course of the year, and current retail pricing trends are reflecting this acceleration. Recall our Easter season, which had a meaningful impact on sales in the first quarter, was not priced. Additionally, promotional timing and mix related to Amplify, Pirate Brands and international resulted in a modest first quarter headwind. Our U.S. business, excluding recent acquisitions, delivered net price realization of 50 basis points in the quarter. As we shared earlier this year, the late Easter is impacting recent retail performance. Per IRI, year-to-date Hershey candy mint and gums retail sales decreased 6% versus overall category decline of 5.4% through April 14. This resulted in a share loss of approximately 20 basis points, in line with our expectations. We expect our retail sales and share performance to improve in the coming weeks as the full Easter season is reported. As is typically the case with a late Easter, we do anticipate some softness in May retail sales as consumers enjoy their Easter candy and make slightly fewer everyday purchases. This is accounted for in our guidance as part of the net incremental impact from the long season.

Preliminary results indicate a strong Easter season for both the category and Hershey. Hershey retail takeaway grew about 15% to 20%, resulting in an anticipated seasonal share gain of approximately 150 basis points. This was driven by a strong focus on our core brands, purposeful innovation and exceptional retail execution.

Reese's and Cadbury are the top 2 brands in the category during the Easter season, with a combined market share of over 25%. This share is greater than the next 6 brands combined. And we had one of the top-selling new items of the season with our Cadbury shimmer eggs innovation, which contributed to even stronger growth and consumer engagement this year.

A special thank you to all of our employees who helped contribute to the success of the season.

Another key initiative for us this year is the renovation of our chocolate-packaged candy bags, which has just begun to execute at select retailers. This transformation not only increases branding and competitiveness but also enables us to secure incremental shelf space in store. Early results are encouraging, and we will remain focused on this transition in the coming months.

Our Reese's Thins innovation is off to a solid start and is generating strong consumer engagement. We are supporting this launch with both paid and earned media as well as merchandising both in store and online. [Current] distribution is building, and we expect sales to continue to accelerate in the coming weeks. We are also excited about our summer Reese's lovers promotion, which ships primarily in the second quarter. Our activation of this plan in and out instant consumable promotion in late March generated the largest amount of earned impressions ever for one of our announcements. Our nearly 4 billion earned impressions were 3x the amount our competition achieved during the same period. This is a tremendous advantage for us that speaks to the power of this brand and our ability to leverage multiple models to effectively and efficiently drive consumer engagement and grow sales.

And this week, after much media speculation, we confirmed that Kit Kat is launching a new product nationwide in December of 2019. Kit Kat Duos Mint + Dark Chocolate is the first permanent Kit Kat flavor in the U.S. in almost a decade. This item will feature a mash-up of 2 iconic flavors, with mint cream on top and dark chocolate on the bottom surrounding the light and crispy wafer. More to come on this later in the year.

And as I've shared before, we're leveraging new media capabilities and models to support our portfolio in more efficient ways. Earned impressions are a key piece of this, along with targeted media and more efficient content production. This is enabling us to support our brands in a more cost-effective manner. In the first quarter of 2019, 12 of our U.S. confection brands that represent approximately 90% of our sales had media support. Our paid consumer impressions for these brands increased double digits, with only a slight increase in spend. We will continue to leverage this model and support the breadth of the portfolio throughout the remainder of the year. We expect dollar investment to accelerate as we move through the year due to the timing of innovations, the lapping of our media efficiency gains from last year as well as incremental investments supported by our gross margin expansion.

Our e-commerce business continues to show strong growth. In the first quarter, our e-commerce net sales grew almost 50%, and our online chocolate share grew 120 basis points at our key customers. We remain focused on [mending search] and having the right content and portfolio for this channel.

Now for an update on our Amplify and Pirate Brands acquisitions. Both are delivering solid growth and are on track to achieve our financial targets. Per IRI, Skinny Pop ready-to-eat popcorn is growing over 11% year-to-date through April 14, resulting in a share gain of over 100 share points -- I'm sorry, 100 basis points. Our focus on improving distribution and shelf placement is resulting in consistent gains in household penetration. We have a new marketing campaign launching in Tier 2 to help continue this strong momentum.

We successfully transitioned selling responsibilities for Pirate Brands to our Amplify team in the first quarter. We remain focused on leveraging the same capabilities we use for Skinny Pop to optimize distribution and shelf placement to drive growth. Recent retail sales growth has slowed slightly due to distribution losses associated with the transition, but we are confident these trends will improve as we assume wholesaling responsibilities.

Now for an update on our international business. Constant currency organic sales grew 3.5% in the first quarter. And we continued to demonstrate disciplined investment, resulting in segment operating income growth of 14.5% versus prior year. In India, our Kisses launch is off to a good start and pacing ahead of all key metrics. Both consumer and customer acceptance have been strong, and we remain optimistic that this platform can be expanded to additional regions in the future. Our Kisses brand is also seeing strength in Mexico behind our Selección Especial gifting platform. Digital advertising, in-store exhibitions and sampling all helped to recruit new consumers to the brand and drive growth at 2x the category level. This is a great example of a differentiated product proposition. This is driving not only a premium price point but at accretive margins.

So we have good momentum across all of our key strategies, with strong financial results in the first quarter. We remain committed to delivering balanced growth today while making key investments in our brands and capabilities to take the business to the next level.

The organizational changes we announced last week will enable us to continue this good progress. I'm excited that Steve Voskuil will be joining Hershey as Senior Vice President and Chief Financial Officer next month. Steve is a seasoned executive with a wide variety of experiences working in CPG both in the U.S. and international markets. And he brings a broad financial management leadership with the right blend of strategic, operational and transformative expertise that will help accelerate Hershey's growth agenda.

Rohit Grover has been promoted to President, international. With more than 20 years of experience working in nearly all of Hershey's international markets, Rohit has a proven track record of transforming businesses and cultures to drive growth and profitability. Most recently, he designed and led the turnarounds of Hershey's China business, including restructuring the portfolio and operating model which has been the largest contributor to our recent international profitability improvements.

Jason Reiman has been promoted to Senior Vice President and Chief Supply Chain Officer. Also a veteran of Hershey for more than 25 years, Jason has operated in senior executive roles leading all aspects of the supply chain, including manufacturing, engineering, supply chain planning and logistics in the U.S. and international, while delivering superior quality, customer service, margin expansion and growth for the business. And finally, given the increasing importance of our digital transformation to our future growth aspirations, Terry O'Day will transition to full-time leadership of our information technology initiatives. He will continue to lead our ERP transformation, which remains on track.

These changes are a testament to Hershey's talent development and succession planning and a great balance of exceptional internal and external seasoned leaders that I am confident will help take our business to the next level. Thank you to Steven Schiller and Patricia for all their contributions to our success over the past several years.

And now we'll turn it over to Patricia, who will provide you with details on our financial results.

Patricia A. Little - *The Hershey Company - Senior VP & CFO*

Thank you, Michele. Good morning, everyone.

First quarter net sales of $2.02 billion increased 2.3% versus the same period last year, including a 90 basis point benefit from acquisitions, partially offset by a 50 basis point headwind from foreign currency translation. Volume and net price realization increased by 1.7 points and 0.2 points, respectively. These results are in line with our expectations.

Adjusted earnings per share diluted were $1.59, an increase of 12.8% versus the same period last year. This was driven by volume growth, gross margin expansion as well as marketing and administrative expense efficiencies and shifts.

By segment, North America net sales increased 3.2% versus the same period last year. The net impact of acquisitions and divestitures was a 1.6-point benefit. This includes 1 additional month of Amplify versus the prior year period, 4 months of Pirate Brands sales as we transitioned financial reporting into Hershey's system and 2 fewer months of Tyrrells sales versus the prior year. Volume was a 1.4-point benefit driven primarily by a longer Easter season. Net price realization was a 0.4-point benefit, and foreign currency exchange was a 20 basis point headwind. All of these results were consistent with expectations.

North America gross margins expanded 60 basis points, driven by favorable commodity; volume; and insourcing of key Easter items, which was a discrete benefit of approximately 20 basis points only in the first quarter. Additionally, we benefited from cost savings from our complexity-reduction efforts, which was slightly ahead of expectations. We continue to expect gross margin expansion to build as we progress through the year as net price realization increases.

North America advertising and related consumer marketing spend increased 1.1% in the quarter. Media and production efficiency gains enabled by new capabilities drove double-digit consumer impression growth, with only modest dollar spend increases. We expect dollar investment to accelerate as we move through the year due to the timing of innovation as well as the lapping of last year's media efficiency gains.

First quarter total International and Other segment net sales decreased 4.9%, including headwinds of 4.6 and 3.5 points from divestitures and foreign currency exchange, respectively. Organic constant currency net sales increased 3.5%. Volume increased 4.3 points, offset partially by net negative price realization of 0.8 points. Organic constant currency net sales in our focus markets Mexico, Brazil, India and China grew 3% versus the first quarter of 2018. This growth was slightly below 2018 levels, driven primarily by inventory volatility in the first quarter of 2018. We expect that year-to-go organic growth will be comparable to full year 2018 levels.

International and Other advertising and related consumer marketing declined 14%, in line with our expectations as we continue to rightsize our investments to drive more profitable growth.

Total Hershey adjusted gross profit increased 4%, resulting in an adjusted gross margin of 45.7%, an increase of 80 basis points versus the first quarter last year. These gains were driven by favorable commodities, volume, efficiencies from our complexity-reduction initiatives as well as margin-for-growth savings from our international [workings].

First quarter adjusted operating profit of $471 million resulted in operating profit margin of 23.3%, an increase of 160 basis points versus the first quarter of 2018. Gross margin gains and continued SG&A discipline drove favorable operating profit results.

Moving down the P&L. Interest expense of $37 million increased $8 million versus Q1 last year, driven by incremental debt associated with recent acquisitions. Full year 2019 interest expense is expected to be in the $150 million to $160 million range, in line with our previously stated guidance.

The adjusted tax rate for the first quarter was 22% versus 24.9% in the year ago period. These gains were driven by tax reform regulation releases, benefits of employee share-based payments and continued use of investment tax credits versus the first quarter of last year. We continue to expect our full year 2019 tax rate to be approximately 17%.

First quarter other expense was $6 million, an increase of $4 million. There is no change to our full year 2019 estimate of approximately $105 million to $115 million. This reflects a higher investment in tax credit as well as additional expense associated with our pension assets due to December 2018's stock market performance relative to our long-term asset return assumptions.

For the first quarter of 2019, weighted average shares outstanding on a diluted basis were approximately 210 million. The company repurchased 150 million of common shares in the first quarter. This completes the October 2017 $100 million authorization, while $410 million remained on the July 2018 $500 million authorization. We also repurchased $49 million of common shares in connection with the exercise of stock options.

Total capital additions, including software, were $93 million in the first quarter. For the full year 2019, we continue to estimate that CapEx will be in the $330 million to $350 million range. As a percent of net sales, this remains slightly higher than our long-term target as we continue to implement our new ERP system and to invest in core capacity.

We continued to return cash to our shareholders with first quarter dividends of $146 million. This was our 357th consecutive quarterly dividend on the common stock.

To summarize this full year. There is no change to our full year reported net sales outlook. We continue to expect net sales to increase 1% to 3%, including approximately 0.5 points net benefit from acquisitions and divestitures. We expect full year FX impact to be negligible based on current exchange rates. Reported net sales growth is expected to be slightly higher in the second half due to the negative impacts of divestitures and FX in the first half. Organic net sales growth is anticipated to be slightly higher in the first half due to the impact of Easter.

Full year reported earnings per share diluted are expected to be in the $5.50 to $5.60 range. There is no change to our full year adjusted earnings per share diluted range of $5.63 to $5.74, an increase of 5% to 7%, last year. Due to the [gaining] of sales growth, gross margin gains and the timing of promotions and investments, we anticipate strongest EPS growth in Q1 and in Q4.

We continue to take a balanced and disciplined approach to building our brands and evolving our business model for the future. We have a strong cash flow and a healthy balance sheet. That gives us flexibility to make the necessary investments to drive long-term shareholder value.

That concludes my financial discussion, but before I turn it over to Michele, I just want to say that working with Michele and all of our Hershey colleagues has been an absolute joy. One of the reasons I feel so upbeat at the end of my Hershey time is the confidence I have in this business and in the team to take the company to the next level. I know Steve will be a great partner to Michele and the rest of the team in delivering against our aspirations and making an already great P&L even stronger.

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

Thanks, Patricia.

I am pleased with our strong start to the year. The actions we are taking to drive core confection momentum, to capture growth via incremental portfolios and regions and to invest in our brands and capabilities will continue to drive this business forward. I believe this dynamic environment and accelerated pace of change creates tremendous opportunities for us to engage with our consumers in new and innovative ways to grow today and into the future. We remain focused on achieving balanced sales and earnings growth to continue delivering peer-leading shareholder returns. We have a portfolio of beloved brands and an amazing team of individuals that are excited and proud to come to work every day. We are pleased with the progress we are making, but we also have a healthy degree of dissatisfaction that drives us to continue pushing to elevate the business to the next level, and we are committed to doing this in a way that is consistent with our values and purpose.

Patricia, Melissa and I are now available to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We'll go ahead and take our first question from Ken Goldman.

Kenneth B. Goldman - *JP Morgan Chase & Co, Research Division - Senior Analyst*

Thanks for everything, Patricia, and best of luck on your next endeavors.

Patricia A. Little - *The Hershey Company - Senior VP & CFO*

Thank you.

Kenneth B. Goldman - *JP Morgan Chase & Co, Research Division - Senior Analyst*

Two for me. Michele, I think your previous guidance suggested that Easter will benefit annual sales by about 50 basis points, which implies about 200 for the first quarter. I didn't hear a number in your prepared remarks. Maybe I just missed it, but is it reasonable for us to think that Easter helped the first quarter by around 200 basis points on the top line?

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

Yes. That is reasonable, the growth in the first quarter definitely driven by Easter and our international business.

Kenneth B. Goldman - *JP Morgan Chase & Co, Research Division - Senior Analyst*

Okay. And then I know you don't give quarterly guidance, but you did just give some cadence, so I wanted to ask a follow-up to that. I guess I'll just ask the question directly. The Street in the -- for the second quarter, is looking for a bit under $1.8 billion in sales, around $350 million in EBIT or operating income. Are these numbers really unreasonable for you given the Easter timing headwind? I just wanted to get a sense of whether the Street is at least modeling this up in sort of a range of what you're thinking.

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

Patricia, do you want to...

Patricia A. Little - *The Hershey Company - Senior VP & CFO*

Ken, I -- again, we don't give quarterly guidance, so I would absolutely not comment on specific numbers that the Street does have in their model. We were just trying to give you some help because with Easter, FX and divestitures we just really want to help you understand the cadence of our sales. Kind of that is impacting first half, second half. And then a little bit about just the rhythm of EPS that we expect. And we don't have anything further to say and certainly no comments on specific numbers that the Street is modeling.

Operator

We will take our next question from Bryan Spillane.

Bryan Douglass Spillane - *BofA Merrill Lynch, Research Division - MD of Equity Research*

Just wanted to ask -- just tying together, I guess, a couple of comments around gross profits and gross margins. And you talked about it maybe building more later in the year, but -- and you also pulled in a little bit of the benefit from insourcing some of the Easter product. So can you give us a sense of, I guess, is like a 60 basis point gross margin expansion as a basis point year-over-year sort of what you would see maybe for the balance of the year or for the full year? Or is this quarter maybe the strongest in terms of gross margin performance? Just trying to get a sense of where gross margins land for the year.

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

So this is Michele. We feel good about the progress we're making on gross margin, and we expect that our full year gross margin expansion will be at or slightly above what we delivered in the first quarter. So as you mentioned, there was the discrete benefit of about 20 basis points, so I think thinking about 60 as kind of the run -- the base run rate is a good way to think about it. Recall that we will get more price realization in the second quarter with our new packaged candy bags. There's also some packaging costs which are limiting the amount of that gross margin, but as we go through the year, we anticipate that, that gross margin will ramp up a bit off of the run rate that you mentioned. Is that helpful?

Bryan Douglass Spillane - *BofA Merrill Lynch, Research Division - MD of Equity Research*

Okay. Great. Yes, that's helpful.

Operator

We will take our next question from Robert Moskow.

Robert Bain Moskow - *Crédit Suisse AG, Research Division - Research Analyst*

That Bryan Spillane is a smart guy. He took my question, but let me try a different one. Can you talk about the market share losses in the first quarter, which was just 20 basis points? And I guess I thought I heard you say that you picked it up in the early phases of Easter, I guess, related to your Easter seasonal activity. Can you talk a little bit more broadly about just candy, mint and gum in general; your innovation plans? Is that enough to get you back into a pattern of share gains overall for the year or for next year? I think most people's perceptions of the innovation pipeline is it's okay, not super; and a lot of concerns about competitive incursion from Mars and Ferrero.

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

Sure. So Rob, our year-to-date share is in line with our expectations. We expected a little bit of a slower start on share due to the timing of some of our innovation and our promotions, but we continue, as you look at the trend that you're seeing in share, with a continuous kind of improvement in trend as we go through the first quarter here. You're going to see that continue. As we get through Easter, we think that you'll see the retail takeaway. The share and the sales kind of true up and line up together. And then obviously, following that, we have some of our biggest programs for the year, including the chocolate-packaged candy reinvention as well as Reese's Thins and the Reese's lovers activations. So we've got a pretty balanced plan with a lot of activation, but from a retail takeaway perspective, more of that begins to hit Q2 and beyond for the year. And we're continuing to drive a balanced approach to driving our business. We feel great about the innovation we have this year with the chocolate-packaged candy packaging effort, which is about $0.5 billion in the portfolio; Reese's Thins and Reese's lovers promotion, our largest brands by far; and then obviously, just announcing a new item within Kit Kat, one of our other core brands. So we believe we do best when we have a really balanced approach where we are winning on multiple levers which include seasons, pricing, innovation, good marketing on the core. And we're going to continue to drive that. And we anticipate that, as much as there is a lot of competitive innovation, we think that overall it'll be in line in total with prior years.

Operator

We will take our next question from Jonathan Feeney's.

Jonathan Patrick Feeney - *Consumer Edge Research, LLC - Senior Analyst of Food & HPC, Director of research and Managing Partner*

Two questions from me. You -- the Easter share you quoted earlier, I think, was 150 basis points. Is that a Easter share on a through-April-14 basis? Or is that what you know about the totality of Easter this year versus the totality of Easter last year, about how you're comparing with some non-Easter weeks in that number, that share number, first of all? And second of all, yes, I know that there's been a lot going on from a takeaway standpoint. What -- I mean what level -- you gave us a year-to-date takeaway number, and clearly, you're way outperforming that. In the 6 days approaching, [I guess, through that], it's not in that takeaway number. What's a good U.S. CMG takeaway number mid-May that would give us the sense that you are on track towards your plan? Like what is that number so I understand that you guys are on track to -- for the next months?

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

So let me start with your question around Easter. The share gain that I quoted is what we anticipate for the full season based on what we know year-to-date and across the business. And that is really looking full Easter this year versus full Easter last year. Relative to takeaway, somewhere in that 1.5% to 2% range on a year-to-date basis, I'd say, will be a good benchmark.

Operator

We will take our next question from Steven Strycula.

Steven A. Strycula - *UBS Investment Bank, Research Division - Director and Equity Research Analyst*

Congrats on a good quarter.

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

Thank you.

Steven A. Strycula - *UBS Investment Bank, Research Division - Director and Equity Research Analyst*

So this Easter shift is really breaking my calculator here. I'm trying to figure a few things out, but Patricia, I was hoping you'd help me out here a little bit as I think about the organic

(technical difficulty)

think about how that flows through the year directionally is the first part of my question.

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

Steve, you broke up a little bit. You -- I'm sorry. You were just asking about what the organic sales were at Easter in the quarter.

Steven A. Strycula - *UBS Investment Bank, Research Division - Director and Equity Research Analyst*

Yes, just what the cadence we should think about throughout the balance of the year. I think it's a little bit noisy because of Easter. And a lot of investors have been asking me this morning just how to think about front half versus back half and 2Q. And then I've got a follow up.

Patricia A. Little - *The Hershey Company - Senior VP & CFO*

Yes. So as we said, we expect that, because of that Easter, we will -- we would expect that on an organic basis it will be higher in the first half than into the second half, just because of the long Easter. Is that what you were getting at?

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

Yes. So I mean the organic growth [would become]...

Steven A. Strycula - *UBS Investment Bank, Research Division - Director and Equity Research Analyst*

Perfect. I can follow up offline...

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

Okay. Yes. Think about it as the organic growth was about 2% in the quarter. I mean we had...

Steven A. Strycula - *UBS Investment Bank, Research Division - Director and Equity Research Analyst*

Okay. (inaudible)? Sure, yes. I think there's some background noise, but so the other fundamental question I had was -- to piggyback off of Rob Moskow's question, is to think about the incrementality of innovation this year relative to prior cycles that you guys have had. How do you think about what you're bringing to market; and how that [compares] against Cookie Layer Crunch, Hershey's Gold? And what's so different about the packaging this year that it should drive better conversion at retail relative to the past?

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

Yes. So I feel really good about our innovation this year. And I will say, if I look historically, I think frequently the best and more sustainable innovation we've had is when we are really focused on either improving our core or staying close to the core with a key, purposeful benefit. So when I think about the chocolate-packaged candy, it gives us a notable improvement in shelf awareness in a category that is a very challenged category to shop. So I think the first benefit starts with that, and then second in terms of the usability of the package at home. So it's really a lift across a very big piece of business that is a very closed-end product improvement benefit. And I think that tends to -- those types of things tend to perform very well for us. Reese's Thins, likewise, it is a variation of a Reese's cup with a new shape. And as we think about our portfolio, one of the interesting things about Reese's is we have all different kinds of cups and different shapes and different ratios of chocolate to peanut butter, and everybody has their favorite. And thins offers a benefit of permissibility and a totally different eating experience on our biggest core brand. So that proximity to the core tends to lead to a more sustainable approach. So where we find some of those innovations, I feel -- I tend to feel the best about those. So I'm pretty bullish on what we have for this year.

Operator

We will take our next question from David Driscoll.

David Christopher Driscoll - *Citigroup Inc, Research Division - MD and Senior Research Analyst*

Patricia, I just wanted to say thank you so much. It's been a pleasure to work with you, and we wish you all the best. On to the -- I want to follow up on some of the questions related to the top line. So just to be super clear: With CMG takeaway down 6% in the Q1, shipment is up 1.6%, excluding M&A. Volume is a big driver there at 1.4 points. Is there any implication to the second quarter? Is there any shipment pull forward into Q1 that would affect Q2 because of those numbers?

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

David, there's not. If you think about the way Easter and the seasons work, especially given the timing this year, you're shipping to season in the quarter before a lot of the takeaway occurs. So there's a little bit of a -- the disconnect between the shipments and the takeaway, but there is no pull forward. It's just the natural flow of how that business works that you're shipping. And then some of the biggest takeaway for the season comes in the couple weeks, those 2 weeks right before the day of the holiday. And so that's really the dynamic. And if you look at past years, you'll see that -- every year, that's the way it works.

Patricia A. Little - *The Hershey Company - Senior VP & CFO*

So again, David, you can just expect that, by the end of April, the share, the takeaway and the sales will all be trued up together.

David Christopher Driscoll - *Citigroup Inc, Research Division - MD and Senior Research Analyst*

Okay. That's really helpful. My last question is just on pricing. You have expectations that pricing is going to increase as the quarters go forward. Has retail acceptance of your pricing plans been -- if it did happen to the fullest extent? Do you have any concerns about the implementation on pricing, whether it's the list price increase or whether it's getting your new packaging on shelf? Because everything on the pricing plan kind of full steam ahead.

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

Yes, everything relative to the pricing is working and coming in exactly as we expected. The retail price points that we're seeing, in terms of the phasing for the year -- remember Easter wasn't priced. So that's a big piece that, as we get later through the year, is really where the pricing impact kicks in. We've looked at price points, retail price points; where we are in our elasticity and conversion model. And that's in line with what we expected as well, so all looking good.

Operator

We'll take our next question from John Baumgartner.

John Joseph Baumgartner - *Wells Fargo Securities, LLC, Research Division - VP and Senior Analyst*

Michele, it sounds as though the momentum around the media impressions is fairly solid, but I guess my question is really more about the conversion on those because, I mean, you've been working through the efficiencies for a while, but the share in chocolate is still down pretty consistently. And I know your brands are always very responsive to traditional media, but maybe digital is showing as less impactful. So I mean, are you seeing any data points that would suggest otherwise? I mean I'm just trying to square the media shift with the market share we see in the Nielsen data.

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

We continue to optimize the right balance across earned and paid impressions; and also, within the paid, what is the optimal level of TV versus digital and getting tighter and tighter on the digital relative to addressable and programmable media that allows us to reach the exact right person. So I feel good about the progress we're making there. We continue to optimize and implement as we learn and go along the way, but we feel good that we are continuing to see strong ROIs on the spends that we have and continuing to optimize based on those.

John Joseph Baumgartner - *Wells Fargo Securities, LLC, Research Division - VP and Senior Analyst*

And do you have a sense kind of where digital is right now as a percent of the total bucket and where, I guess, the long-term target is?

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

So I want to say digital is about 40% of our total media investment. And in terms of the long-term target, I would say we continue to learn as we go, but at this point in time we believe that mainstream media, given our very broad household penetration, will continue to be an important part of our mix given it's pretty efficient media. And within digital and some of the capabilities of old in terms of more capability about -- around programmable, we'll continue to adjust to that, but there's a lot of blurring of the lines in terms of playing across the entire wheel.

Operator

We'll take our next question from Rob Dickerson.

Robert Frederick Dickerson - *Deutsche Bank AG, Research Division - Research Analyst*

Two quick questions. First question was just on kind of organic sales cadence again for the year. I think you just said in the remarks that you'd expect basically organic sales to be a little bit faster in growth terms in the first half versus second half. It sounds like second half rate would get more of the pricing but less than a mix effect from the new innovation or at least the stand-up bags and the thins, so I'm just curious. If there is to be more pricing in the back half of the year, our organic sales will be slower, I'm assuming, kind of back of Easter. I -- are -- does that imply that your models are baking in some material volume elasticity in Q3 and Q4? Or is it more just an Easter effect in Q1 versus what you expect in the back half?

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

No. Our models do bake in that elasticity in the second half. When we take a price increase, that's historically how it works. And the data we have based on history is exactly what we are banking on. It's also what we're seeing year-to-date where prices have hit, but you're absolutely right. In the year we take pricing, you see a big increase in the amount of our revenue that comes from pricing and you take a hit on volume as the conversion of that builds.

Robert Frederick Dickerson - *Deutsche Bank AG, Research Division - Research Analyst*

Okay. Great. And then just in terms of margin, I think you said you'd expect gross margin to build just given partially the pricing benefit as you move through the year. Operating margin was up almost 160 basis points in Q1. Should we also expect the operating margin to build throughout the year? Or I'm assuming, given higher SM&A and brand investment, that operating margin would likely be expanding but at a slower rate relative to gross margin for the remainder of the year. That's all.

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

Yes. I would say no. That should not be your expectations. There can be a lot of noise on a quarterly basis. And no. Well, there should be a build in gross margin. Do not think about operating margin that way.

Operator

We will take our next question from Ken Zaslow.

Kenneth Bryan Zaslow - *BMO Capital Markets Equity Research - MD of Food & Agribusiness Research and Food & Beverage Analyst*

Just have a question on clarity. I think I'm just confused. I think you said in the quarter that your expectation's where you thought it was on both sales and EPS. And then in the last quarter, you said that your [sales] accelerate through the second half. Now I think you -- and your sales growth obviously was 2.3%. Your guidance is 1.3 -- 1% to 3%, but now you're saying that the first and fourth quarter are going to be the highest. What changed? Did nothing changed? And I just don't understand. I'm sorry.

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

So relative to sales, we said our sales was in line with our expectations...

Kenneth Bryan Zaslow - *BMO Capital Markets Equity Research - MD of Food & Agribusiness Research and Food & Beverage Analyst*

All right (inaudible) fourth quarter. It's supposed to build through the year, right?

Patricia A. Little - *The Hershey Company - Senior VP & CFO*

So it might be the confusion between our reported net sales growth, where it's going to be higher in the second half due to divestitures which we talked about. And then the organic piece is higher in the first half due to Easter. And on the EPS side, we just say that -- all right. And then on the EPS, it was higher than we expected, as we said on this call.

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

Q1 was higher than expected.

Patricia A. Little - *The Hershey Company - Senior VP & CFO*

Yes.

Kenneth Bryan Zaslow - *BMO Capital Markets Equity Research - MD of Food & Agribusiness Research and Food & Beverage Analyst*

Okay. And my real question is can you talk about your e-commerce progress? What share do you want to get to? Where are you? How far are you away from what share you're looking to get and get to? And then what is the difference between your digital spending 3, 4 years ago and now? And where do you expect that to get? And I'll leave it there.

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

So I think we want to continue to drive share and gain share in e-commerce. I think the benchmark we would look at is we would want to be at least comparable to our bricks-and-mortar business, but I would say that I also think there's an opportunity with our capabilities for us to have higher share than bricks and mortars. So that's certainly what we are shooting for. And we're pleased that, in each of the past several years, we've continued to gain over 100 basis points of share on our chocolate business in e-commerce. So we want to capture as much share as we can.

Kenneth Bryan Zaslow - *BMO Capital Markets Equity Research - MD of Food & Agribusiness Research and Food & Beverage Analyst*

And then digital spending, what percentage of your spending is on digital? And where do you expect that to go? And I'll leave it there.

Michele Gross Buck - *The Hershey Company - President, CEO & Director*

Well, for total digital advertising, from a media perspective, it's about 40%, if we just look at media. Obviously, there are a lot of other investments in terms of resources, people, all of that.

Operator

There are no further questions at this time. I will turn the call back to our speakers for any additional remarks.

Melissa Poole - *The Hershey Company - Senior Director of IR*

Thank you for joining us this morning. We'll be available throughout the day for any additional questions you may have.

Operator

This does conclude today's program. Thank you for your participation. You may disconnect at any time.