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The Hershey Company

First Quarter 2022 Question-and-Answer Session Conference

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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

Melissa Poole, *Vice President, Investor Relations*

Michele Buck, *Chairman and Chief Executive Officer*

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

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

Andrew Lazar, *Barclays*

Robert Moskow, *Credit Suisse*

Ken Goldman, *JPMorgan*

Jason English, *Goldman Sachs*

Alexia Howard, *Bernstein*

Bryan Spillane, *Bank of America Merrill Lynch*

Michael Lavery, *Piper Sandler*

Cody Ross, *UBS*

Chris Growe, *Stifle Institutional*

Steve Powers, *Deutsche Bank*

Jonathan Feeney, *Consumer Edge*

John Baumgartner, *Mizuho Securities*

David Palmer, *Evercore ISI*

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

Operator

Greetings, and welcome to The Hershey Company First Quarter 2022 Question & Answer Session Conference.

At this time, all participants are in a listen-only mode. As a reminder, this conference is being recorded.

I'd now like to turn the call over to your host, Ms. Melissa Poole, Vice President of Investor Relations for The Hershey Company. Thank you. Please go ahead.

Melissa Poole

Good morning, everyone. Thank you for joining us today for The Hershey Company's First Quarter 2022 Earnings Q&A Session.

I hope everyone has had the chance to read our press release and listen to our Pre-Recorded Management Presentation, both of which are available on our website. In addition, we have posted a transcript of the pre-recorded 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 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 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.

With that, I will turn it over to the Operator for the first question.

Operator

Ladies and gentlemen, the floor is now open for questions.

The first question is coming from Andrew Lazar of Barclays. Please go ahead.

Andrew, your line is live. Please make sure you're not muted on your end.

Andrew Lazar

Good morning, everybody. Can you hear me?

Operator

Yes, we can hear you.

Andrew Lazar

Great, thank you. I guess first off, by our estimate, it seems like you're raising full year organic sales by essentially the over-delivery in the first quarter; meaning, expectations for the remainder of the year haven't changed. Is that the way you're looking at it, and if so, I guess why is that, given the momentum in the business? I realize you'll start to lap some of the pricing as the year unfolds.

Michele Buck

Hey, Andrew, good morning.

Andrew Lazar

Good morning.

Michele Buck

I'm going to kick it off with a few responses, and ask Steve to jump in, as well.

First of all, I'd say we're really pleased with our first quarter results and the momentum that we see on the business, but it is pretty early in the year still, and as we all know, we continue to see significant volatility in the marketplace, whether it's record inflation, the Ukraine/Russia situation, continued disruption in supply chain. As we dissect the business in the first quarter, clearly, within the first quarter the large majority of our sales were related to stronger elasticities that had been realized in the marketplace, but we do anticipate, as we look further out in the year, that we'll see some moderation on those elasticities, perhaps back to more historic levels, and a lot of that is driven by that reduction in government subsidies and the continued inflation pressure that we think consumers will experience.

There was another component of our Q1 sales beat that was about—or raise, that was about Dot's and our ability to really get our arms around the Dot's business and better understand what we thought it could deliver for the year. We have pretty good visibility into that, so we feel like the number there is pretty good.

Then, lastly, as we look at inventory, we've been really working hard to build inventory, and we did get more inventory out to retail. We made a decision to do that in Q1, to really try and increase on-shelf availability.

So, from a sales perspective, as we look at what we realized versus how we think that will impact the back half of the year, we think the strength in Q1 from sales is much stronger. But, Steve, do you want to comment more about that, and also relative to the cost and profit situation?

Steve Voskuil

Yes, on the top line, I think you hit all the key points. The inventory piece was about a 3-point benefit to the first quarter. That'll come out in the back half. That's one of the unique things, I guess, that drove the first quarter performance. Then, Michele touched on the elasticities. We saw a big benefit in the first quarter. We do expect to see elasticities normalize a bit as we go forward quarter-by-quarter through the year. So, those are probably the two biggest things. So, that's talking a little bit of the outlook on the top line.

Andrew Lazar

Great. Then, I guess the second one would be sort of a similar thought process, but more on the EPS side. Obviously, the first quarter came in some $0.40 higher than the street and you're raising the full year by $0.07. Maybe, can you bridge that gap for us a little bit? Are you trying to be just somewhat conservative in your thought process given, obviously, an increasingly dynamic environment, which makes total sense, or are there some other things that are more discrete that we want to make sure to keep in mind on the profit side? Thank you.

Steve Voskuil

Sure. Yes, the biggest driver for first quarter earnings was that volume, 4.5 points of volume in the quarter that dropped through to earnings. That was the biggest factor. There were some unique pieces, as well. I think we called out a couple in the remarks. One was inventory revaluation, which is sort of an unusual thing, we see it in times of higher inflation, which has the impact of giving a benefit to the P&L and putting more costs on the balance sheet to reflect the cost of goods value there. So, that was 100 basis points to the Confection segment in this quarter, that won't repeat going forward.

As you said, we do expect more year to go inflation. We, in the first quarter, saw a little bit of that incremental inflation, but as we look forward, despite the hedging that we have in place, we're still going to have some incremental exposure, particularly to the commodities impacted by the events in Eastern Ukraine—or Eastern Europe, sorry.

Andrew Lazar

Thank you so much.

Michele Buck

Thanks, Andrew.

Operator

Thank you. The next question is coming from Robert Moskow of Credit Suisse. Please go ahead.

Robert Moskow

Hi. Thanks for the question. There's a lot of detail in the prepared remarks about competitive activity that caused you to lose some market share during Easter, and your capacity constraints that led to that. As we head into Halloween, are you in a position to ramp up sufficiently, so that you can hold your share? The reason I ask is, you know, I remember during the pandemic Halloween was a real tipping point for your distribution with retailers. You gained a lot of goodwill after that. You gained a lot of distribution. Are you in a position so that there's no risk of that reversing?

Michele Buck

Rob, clearly, over the past two years, we have had some nice gains in share, and certainly those have contracted recently given some of the capacity pressure. I think we're up about 50 basis points versus where we were pre-pandemic. Our share versus our next largest competitor, that gap has clearly widened and remains pretty strong, about 200 basis points ahead of pre-pandemic levels. We are doing everything we can, relative to building capacity, investing in new lines, distribution centers, hiring more people, to build our supply as much as possible, and working really closely with retailers, as well, on our plans for Halloween right now. We expect that, as we go through the year, we will continue to have supply challenges, although they will improve as we progress throughout the year, and we're working hard to maximize the opportunity for Halloween.

Robert Moskow

Well, Halloween commitments are probably made pretty early. Can you give us any color as to what you're able to commit to right now?

Michele Buck

We believe that, just as we've seen strengths in the seasons over the past two years, that we will continue to see strengths in the seasons throughout the year. This year, we've seen it in Easter. But, at this point in time, we're not going to give anymore specifics on exactly what those growth numbers are going to be. I guess I would say, overall, what I would say is we're not really seeing any big changes in how our competitors are operating or in their strategies, so, really, it's a focus on us continuing to build supply. Over the past two years, we grew pounds about 7%, versus our competitors in the marketplace, collectively, had a 1% decline in pounds. So, we are just a little tighter on supply and capacity than the environment.

Robert Moskow

Okay, thanks for the question.

Michele Buck

Thank you.

Operator

Thank you. The next question is coming from Ken Goldman of JPMorgan. Please go ahead.

Ken Goldman

Hi, thank you. I wanted to ask about the margins and profitability in Salty Snacks. Steve, you gave a helpful explanation of all of the reasons behind, maybe, what could be considered a little sluggishness versus what people were looking for, but I'm curious, to what extent did it fall below your expectations, if at all, what were the key drivers of that shortfall, if there was one, and how quickly might we see a little bit of a rebound there?

Steve Voskuil

Yes, thanks, Ken. Yes, it was sluggish from our side, as well. Some of the margin degradation, we expected, so the mix piece that we called out, obviously, as we brought Dot's into that portfolio, but we also planned on higher raw materials for the portfolio for the year, but the incremental inflation that we've seen more recently, again, following the events in Eastern Europe, are falling more into the Salty Snacks space, so thinking cooking oil, wheat, and then just a smaller business impact on oil price flowing through the P&L. So, that was, I could say, a surprise piece relative to the raw materials side.

We're also in the process of starting up a new distribution center, that began in the first quarter and will continue through the second quarter, and I'd say the start-up there has been a little bit bumpier than we expected, although we're working our way through it and expect to see improvement as we go through the next quarter.

Then, we did have, also, some higher advertising expense in the first quarter. That will moderate. That was part of the plan to spend more in the first quarter and part to offset some of the elasticity due to price increases there, which I think we've done a good job of, because that business is growing strong double-digits, but we'll see that begin to moderate as we get to the next couple of quarters.

So, if I kind of point to the things that were a bit unusual, I'd say the DC start-up, the incremental inflation, and probably higher advertising spend, that we wouldn't normally see in that business.

Ken Goldman

Thank you, and just a quick follow-up. I know these things are hard to sort of parse out, but is there any way to think about what the gross margin, roughly, might have been in the first quarter if you were to exclude the inventory fill? You may have called it out and I missed it. I'm just curious for an estimate there.

Steve Voskuil

Yes, we didn't go that far in the remarks and sort of back into what it might have been. What I would say is—we talked about this a little bit on the last call, as well—the opportunity here is really to optimize the new snacking division. As we look at even the work we're doing with the distribution center, that's all pointed towards driving network efficiency. We're going to be working through supply chain efficiencies, and of course, eventually, back office efficiencies, as well. We continue to be excited about the opportunity to drop more margin out of that business as we gain scale and get some of those integration points together.

Ken Goldman

Thanks so much.

Steve Voskuil

Thank you.

Operator

Thank you. The next question is coming from Jason English with Goldman Sachs. Please go ahead.

Jason English

Hey, good morning, folks. Thanks for slotting me in.

Michele Buck

Good morning.

Steve Voskuil

Good morning.

Jason English

A couple questions. First, Snack margins, I think you said you had about 500 basis points degradation from mix. I imagine a good chunk of that is coming from the manufacturing asset you picked up. So, a question on that. How much Snack capacity is in that asset? You mentioned in your prepared remarks that you're beginning to lean in and have--and start producing some of your other snack items on that network. How much can you move over and how far can you shrink that 500 bps as you improve asset utilization, presumably, migrate production from outsource providers to insource?

Steve Voskuil

Yes. So, a couple things there. One, inside that mix is also the amortization, the incremental amortization of the deal, so not all of it is capacity-related. That's going to be around for a while, obviously. As we look at combining supply chains, we—those assets are pretty well utilized. They were a little bit a less utilized in the first quarter than they will be for the balance of the year, but we continue to see opportunities to continue to leverage those assets to get to world-class manufacturing assets. That's one of the reasons we're able to bring our Pirate's Booty asset into that mix as early as we did, and the plan is to see more of that sort of consolidated manufacturing. We'd expect to see some mitigation of that mix impact as we continue to leverage those assets and drive more volume through that system.

Jason English

Got it, and back to the comments on market share attributed to capacity constraints. I just pulled your brand level data just to get a snapshot of which are brands are holding you back a bit, and it's brands like Kit Kat, Reese's Pieces, Twizzlers. Those don't seem like the types of brands you'd be capacity constrained on. Are they, or where are the capacity constraints?

Michele Buck

Our biggest capacity constraint is really on Reese, and some of our assorted bags, but primarily Reese. As you know, Reese is our biggest brand by far, it's a couple billion dollars in size, and when it is growing double-digits, as it has been, and has had such a track record of strong growth, that is—that's where some of the—you know, the biggest rub and the biggest dollar opportunity that we're focused on. Then, some of our other take-home brands. Obviously, given the strength of consumers now consuming at-home, there's a lot of pressure on some of the brands in terms of how they show up in take-home, and that's spread across a number of different brands.

Jason English

Got it. Okay, thanks. I'll pass it on.

Operator

Thank you. The next question is coming from Alexia Howard of Bernstein. Please go ahead.

Alexia Howard

Good morning, everyone.

Michele Buck

Good morning.

Steve Voskuil

Good morning.

Alexia Howard

Okay. So, a couple of questions here. The Dot's Pretzels acquisition, obviously, incredibly strong growth year-on-year, that you reported in the remarks. Could you talk about the distribution opportunity? Where is the ACV at the moment, where could it get to? Is this something that—I guess, how large is the opportunity? We'll start there.

Michele Buck

We are continuing to build distribution on Dot's. Clearly, as we were acquiring the brand, the distribution remained skewed to kind of the West Coast, the middle of the country, and we've had a big focus on trying to close the distribution gap on the East Coast, in particular, and then to also fill in in some of the key retailers and classes of trades throughout. So, it's been a constant build. We had a lot of distribution growth in Q1. I believe that we're in the mid-70s right now on distribution, so there remains some upside, that we're experiencing now and we continue to drive through the back part of the year. We continue to gain household penetration as a result of that, as more consumers find out about the brand. Household awareness of the brand continues to be low and we see that as a key opportunity, as well.

Alexia Howard

Great, and then can I ask about—on a different topic—on the c-store dynamics. There have been concerns in the past that when gasoline prices spike, that that leads to fewer trips and, therefore, that hits your c-store sales. Can you talk about what you're seeing in that segment and whether that's the case this time around, or if you're seeing something different? Thank you, and I'll pass it on.

Michele Buck

We have seen some changes in consumer behavior within convenience stores as gas prices have risen, but what we're seeing is that many consumers seem to be trying to manage the higher price by not fully filling their tanks. So, they're making more trips, but just not filling it full. To date, they have not really reduced their non-gas purchases in a meaningful way and we haven't seen an impact. Our business remains quite strong in convenience stores, so we haven't really seen an impact on our business, though we do expect that these trends will continue to evolve as we see some of those pressures we talked about earlier, relative to reduction in government subsidies and the continued persistence of inflation, and the impact on consumers.

Alexia Howard

Great, thank you very much. I'll pass it on.

Michele Buck

Thanks.

Operator

Thank you. The next question is coming from Bryan Spillane with Bank of America. Please go ahead.

Bryan Spillane

Thanks, Operator. Good morning, everyone.

Michele Buck

Good morning.

Steve Voskuil

Good morning.

Bryan Spillane

I had just one question and it's around inflation and gross margins. Can you just help a little bit with—based on the incremental inflation you saw in the first quarter, you've widened—your expectation for gross margins change. As we're kind of looking at this kind of moving even past the fiscal year, what will you be able to do to begin to mitigate or offset that margin pressure? Is it going to be as some of this new capacity comes on, there's more efficiencies? Is pricing potentially a lever in the mix? Just really trying to understand, as we move forward, are you going to be able to mitigate that margin pressure?

Steve Voskuil

Yes, it's really all of those, Bryan. We're certainly going to look at all our usual levers, driving productivity and efficiency from a manufacturing standpoint, and we will see more of that as we get more scale and more assets coming online, so that'll be a factor. But, pricing is always part of our strategy, we look at it all the time. We're very sensitive to both the consumer and what's happening from an input cost standpoint, and we'll continue to look at that as we think about our plans for next year.

Bryan Spillane

Okay, but as it stands now, you haven't contemplated or you haven't—embedded in the guidance isn't any incremental pricing actions or other actions to offset that inflation, you're just absorbing the inflation right now.

Steve Voskuil

That's right, but what's in the outlook right now is the pricing that we've already announced that's flowing through the P&L for the year.

Bryan Spillane

Okay, perfect. All right, thank you.

Operator

Thank you. The next question is coming from Michael Lavery of Piper Sandler. Please go ahead.

Michael Lavery

Thank you. Good morning.

Michele Buck

Good morning.

Steve Voskuil

Good morning.

Michael Lavery

I know that gas price increases is a factor that may make it a little bit harder to tease this out, or really recognize it, but can you talk about mobility and just some of the consumer patterns you're seeing there as things are reopening more, consumers are getting out more? How does that impact some of your, obviously, higher margin instant consumable products? Are you seeing any shifts or anything that's notable in terms of the mix of what they're buying and where?

Michele Buck

Yes, we definitely are seeing consumer mobility has returned, is strong. It's interesting. It's certainly dialed up versus what it was before, and at the same time we're still seeing a lot of interest in some of the at-home behaviors, where people haven't totally returned to some things, like restaurants and some activities, frankly, not as much because of COVID, a little bit more because of some of the price pressure of inflation. We are seeing some consumers try to consolidate trips, but we haven't really seen a meaningful impact to our total trips, and we've been looking across each class of trade. I'd say food is strong, has accelerated. C-store, I mentioned before, quite strong, which is a key indicator of mobility. But, really, across most classes of trade dollar, mass, food and c-store, the trends remain quite strong.

Michael Lavery

Okay, that's helpful, and just on International, those margins were better than expected and very strong. That segment has some pretty significant seasonality. But, can you just help us understand some of what's driving that and how to think about the rest of the year? Is it likely to keep up some of those gains, or what's the right way to frame how that plays out over the course of the year?

Steve Voskuil

Yes, the business has done really well. All of core markets had double-digit top line growth, so that was a good starting point. Then, we're still seeing through the first quarter the last bits of some of the restructuring that we did in China, so that's giving a little bit of an incremental benefit to the first quarter. That, I would say, is probably not going to be a year-over-year component going forward. But, I would also commend the International Team for looking at the whole P&L and managing their cost structure and executing a smart pricing strategy, as well.

Michael Lavery

Okay, great. Thanks so much.

Operator

Thank you. The next question is coming from Cody Ross of UBS. Please go ahead.

Cody Ross

Hey, good morning, everyone, and thank you for taking our question. You just noted that you don't plan on taking additional pricing the rest of the year. However, most companies that have already reported this season discussed taking additional pricing. Why is that?

Michele Buck

We remain very confident in our pricing strategy and our ability to get price realization. As Steve mentioned, what you're seeing in our P&L right now is the pricing that we announced last year flowing through into the business. We all know that this remains a volatile environment. The cost side has continued to evolve, especially with continued supply chain pressure, and also the Ukraine/Russia situation. As always, we will continue to look at every lever at our disposal, as we always do, to make the best decisions for the business.

Cody Ross

Got you. Then, you noted the Russian/Ukrainian war is affecting supply availability. Are there any commodities you can call out that you're having difficulty securing, and do you expect to have any issues securing supply for the balance of the year? Thank you.

Steve Voskuil

Yes, at this stage, taking the last part first, we don't foresee a challenge in availability for the balance of this year. Where we've kind of seen the most pressure is in the cooking oil space, a lot of that sourced out of Eastern Europe, but our business is resilient and we've got other sources and other solutions that we're working through to ensure that we'll be able to satisfy consumer needs, even if we face some more pressure next year on that commodity.

Operator

Thank you. We'll move on to the next question, which is coming from Chris Growe of Stifel. Please go ahead.

Chris Growe

Hi, good morning.

Michele Buck

Good morning.

Steve Voskuil

Good morning.

Chris Growe

Good morning. I just had a question for you, just to follow up on the fact you were able to rebuild some inventory this quarter. It sounds like you're going to have some more in the second quarter now and it's more heavily favored towards the first half. Before, we had thought about that happening in the second half. Do you continue to build inventory in the second half? I guess what I'm ultimately getting to is when can you start—when will you be at a point where you can start to market and promote more normally, like you had historically?

Steve Voskuil

Yes, we're going to continue to build inventory. We're going to see—you should see sequential improvement. More for this year pulled into the first half. But, we want to continue to build inventory, as Michele said earlier, and we've got a lot of capacity coming online. The first quarter was our highest production quarter ever, and as we get more capacity coming online, we expect to see that build and be able to catch up both on our own internal inventory and trade and retail inventory.

Chris Growe

Then, can marketing start more aggressively this year, or is this more like next year?

Steve Voskuil

We're going to make sure that we're fully participating in seasons, just as we talked about earlier with Halloween, and make sure that we're getting all of our product out of our inventory and onto the shelves as quickly as we can, so that we can continue to support the brands, and we'll see more of that support pick up as we get to the back half of the year.

Chris Growe

Okay, and just one final question on the gross margin. You have a little more aggressive decline, because of the increase in costs you expect now for the year. Is that any differently weighted by quarter, is Q2 any worse, or Q3? It caused me to have to bring my estimates down for the remainder of the year for the gross margin, given how strong it was here in the first quarter. I just want to get a sense of how that plays out across the rest of the year. Is it just the timing of inflation that will dictate sort of the quarterly progression in the gross margin?

Steve Voskuil

Yes, I'd say it's mostly that. As we look at our plan, we probably see the most pressure in quarter two, but then begins to improve because the laps get a little bit easier. So, if I had to pick a quarter, I'd probably say quarter two would be the worst.

Chris Growe

Okay. Thanks so much for your time.

Operator

Thank you. The next question is coming from Steve Powers of Deutsche Bank. Please go ahead.

Steve Powers

Great, thank you. Two questions, actually. The first one, just to build on the gross margin theme, the prepared remarks suggests—you had to call out the 120 to 140 basis points of contraction, but then equate that with gross profit dollars increasing mid-single-digits. My math may be wrong, but I think, given your top line, that that seems a pretty conservative combination of top line and gross margin, so just wanted to get some color on that mid-single-digit dollar profit growth line in the prepared remarks.

Then, secondly, you call out seeing some impact in certain consumer goods categories from the inflation that we're all seeing and from the declining government assistance that's occurring. I was hoping you could just give a little bit more color as to what specifically you're seeing and how you're monitoring that going forward. Thank you.

Steve Voskuil

Sure. On the first part of that question, there's no intentional conservatism between what we are seeing on the top and what we're seeing on the gross margin line, and so it should tie, but, technically, we should see about 7% gross profit growth, kind of mid- to high-single-digit range growth, and I think that math will work, but happy to take that on the side if you want to go into more detail.

Steve Powers

Yes, mid to high makes sense. It's just the language in the text, actually, it just says "mid". So, thank you for clarifying.

Steve Voskuil

Yes.

Michele Buck

On your other question, we are constantly looking at a couple things relative to the strength of retail takeaway in other CPG categories, as well as our own, and also how much market share is going to private label, as that has typically also been a predictor of the consumer. We're fortunate in our category not to have significant private label, but certainly in other categories where that's present, we do look at that, as well.

Steve Powers

Okay, very good. Thank you for that, appreciate it.

Operator

Thank you. The next question is coming from Jonathan Feeney of Consumer Edge. Please go ahead.

Jonathan Feeney

Hey, good morning. Thanks. A question and maybe a follow-up all in one. The question is—you guided us on the magnitude of this retailer inventory replenishment for the full year, but has that grown significantly with the better than expected experience in the first quarter, not only in your brands, but across the category, through elasticity? I can't imagine retailers and your competitors thought the uptake to this magnitude of pricing would be that good, but maybe I'm wrong about that. So, that's my first question.

Then, how does Easter play into that? Because, you called out in your prepared remarks that people were buying more everyday products because of the shortages of Easter product, and that certainly seems to be borne out in the data. I wondered, doesn't that add to the retailer inventory need going forward and maybe augment the opportunity to fill to greater levels throughout the year and not just what you had talked about and maybe pulling it forward from your prior guidance on inventory fill? Thanks.

Steve Voskuil

Taking the last bit first, yes, Easter will—the Easter sell-through was high, we saw more everyday takeaway, and that will put more pressure on retailer and trade inventory, so that will happen. As we look at the full year, though, we still—actually, we're not seeing a fundamental shift in what we had planned relative to being able to restock. As we said earlier, we got a benefit in the first quarter, we pushed more out. The elasticity has put, for the full year, a bit more volume through, and so that's true, but also we expect to see additional production pick up as we go through the year to help compensate that to some degree. I think net/net, it's not a big change in total, but, to your point, the sell-through on Easter is going to put a little bit more pressure on some trade inventory.

Jonathan Feeney

Thanks.

Operator

Thank you. The next question is coming from John Baumgartner of Mizuho Securities. Please go ahead.

John Baumgartner

Good morning, and thanks for the question.

Michele Buck

Good morning.

Steve Voskuil

Good morning.

John Baumgartner

Michele, one standout over the past two years has been your increases in share of distribution points, whether it be chocolate or non-chocolate candy, and I can appreciate the capacity constraints right now sort of work against that, but putting that aside, how are you thinking about the resources to sustain and grow as capacity improves? I mean, just given all the upheavals over the past two years, whether it's more promotion, more in-store salesforce hours, more advertising investments, where or how do you see those levers of engagement requiring change in a post-COVID world?

Michele Buck

You know, boy, I'd say my first answer to that question is the resources to sustain and grow are in supply chain, building capacity to really be able to drive against the very strong demand. So, probably, first and foremost, I think that's the focus. I believe we have the retail resources that we need from a sales perspective, our sales organization. From a marketing capability, I wouldn't say it's maybe as much about people. We've continued to invest in capability with a new media partner, better targeting capabilities. Certainly, that helps us to really maximize consumer demand. Then, maintaining the strong relationships that we have with retailers and just continuing to evolve the total bundle of investment we have to drive against demand with our retailers and our consumers. But, right now, I think we're focused, really, on supply chain, hiring more people and manufacturing facilities, engineers to execute the capacity work. That's really where the focus is.

John Baumgartner

I guess, just sticking with that, on supply chain, you've done a lot of work there, adding manufacturing lines, fulfillment center and so on. I guess "weak link" is probably too strong of a term, but where do you think the supply chain still needs more work right now, whether it's modernization, automation? Just outside physical increases on capacity, what sort of is kind of the next phase of, I guess, evolution there?

Michele Buck

Well, clearly, as we are executing this capacity and looking at the future, automation, yes, is a big lever across the business. We still have opportunities in some of our manufacturing facilities for what we call single point of automation, say, an automated case packer, or whatever the basic automation is, and then we kind of go to the connectivity of all the different parts of our system talking to each other, and across our entire business, not just supply chain, we continue to look at opportunities where technology can allow us to operate more efficiently, give us better insight, etc.

Then, certainly, as we look at our Salty business, now that we are gaining more scale and have many more businesses in that portfolio, as Steve mentioned earlier, we're doing a lot of work on just optimizing the overall supply chain network and what that looks like, and that's more efficient distribution, it is more efficient manufacturing, really, across the board, and that's somewhat of a transformation.

John Baumgartner

Okay, thanks, Michele.

Michele Buck

Yes.

Operator

Thank you. The next question is coming from David Palmer of Evercore ISI. Please go ahead.

David Palmer

Thanks. Just a quick question about scanner data. It looks like Hershey's behind some of the competitors in pricing, although we don't always see a perfect lens into what actual list pricing is. Do you think that Hershey's behind the competition when it comes to list price increases lately, or are we just seeing some noise in there?

Michele Buck

Yes, I don't believe we are behind. This is a category where it tends to be line-priced. It's really noise related to Easter and just the mix of items that vary across different competitors during the Easter timeframe. I think, as we go forward, you'll see that really, you know, even out.

David Palmer

Then, just a question on advertising and promotions, those were down lately. It's sort of understandable given the capacity constraints, but what's your outlook for advertising spend, and then maybe you can layer on top of that your general philosophy and what you're thinking there? One thought is that you might layer in, as your capacity increases, some more advertising, but some of the industry are talking about digital marketing becoming more expensive and maybe lower ROI. So, just any thoughts on that would be helpful.

Michele Buck

Okay. We are big believers in advertising. I think we've talked a lot about our model is—we are pleased to have some of the strongest gross margins in the industry and we believe in the model, and then using some of those funds to reinvest in our brand and be one of the highest investors in the industry. It's a highly responsive category, with a strong impulsive nature, as well. As you look to the rest of the year, we believe we will be up mid- to high-single-digits, and we will continue to invest as we expand capacity wherever we can, because we're big believers. Media efficiencies have really helped us to control the dollar cost, because, as a result of a new partnership, and also new capabilities, we've gotten more efficiencies in our media.

I think, from a philosophy perspective, relative to your question about digital, we have not seen declines in lift and return, and I don't know if they're being offset because we've built capabilities, new capabilities to better target, and so we're actually seeing a stronger targeting capability and, thus, better efficiency.

David Palmer

Thank you.

Operator

Thank you. At this time, I'd like to turn the call back over to Ms. Poole for closing comment.

Melissa Poole

Thank you for joining us this morning. I will be available throughout the day and tomorrow for any follow-up questions you may have. Thank you for your time this morning.

Operator

Ladies and gentlemen, thank you for your participation. This concludes today's event, you may disconnect your lines or log off the webcast at this time, and enjoy the rest of your day.