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The Hershey Company

Third Quarter 2020 Earnings Q&A Session

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Ken Goldman, *JPMorgan*

Robert Moskow, *Credit Suisse*

David Palmer, *Evercore ISI*

Chris Growe, *Stifel Nicolaus*

Jason English, *Goldman Sachs*

David Driscoll, *DD Research*

Steve Powers, *Deutsche Bank Securities*

Nik Modi, *RBC Capital Markets*

Michael Lavery, *Piper Sandler*

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Jonathan Feeney, *Consumer Edge Research, LLC*

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PRESENTATION

Operator

Greetings, and welcome to The Hershey Company Third Quarter 2020 Question and Answer Session.

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. You may begin.

Melissa Poole

Thank you. Good morning, everyone. Thank you for joining us today for The Hershey Company's Third Quarter 2020 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, including expectations and assumptions related to the impact of the COVID-19 pandemic. Actual results could differ materially from those projected as a result of the COVID-19 pandemic, as well as other factors. 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

Thank you. If you'd like to ask a question, please press star, one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star, two if you'd like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star keys. To allow for as many questions as possible, we ask that you each keep to one question and one follow-up.

Our first question comes from the line of Andrew Lazar with Barclays. Please proceed with your question.

Andrew Lazar

Great, thanks so much. Good morning, everybody.

Michele Buck

Good morning, Andrew.

Steven Voskuil

Good morning.

Andrew Lazar

Hi. I'm curious—for the past several years, Michele, the majority, if not all, of the Company's organic sales growth has come, really, from pricing as opposed to volume or consumption growth, and much of this is obviously due to the success of the Company's new pricing model and the associated volume elasticity that comes with it. I guess, that said, as you look forward into '21, and beyond, I'm curious if there is a sort of focus internally on maybe regaining some better balance between the two drivers, and if so, would you expect to see some of that maybe develop more fully next year? Thanks so much.

Michele Buck

Yes, Andrew, absolutely. I think we've shared before that we do view pricing as an important part of our growth algorithm, but we are very focused and would like to drive to greater balance between price and volume. We have good visibility into Q4 and 2021, and we do expect volume trends to improve. Part of that will be us lapping some of our pricing elasticity from last year, and also a continuation of some of the strong share gains that we've seen to date, that will carry into the first part of next year. I think you can definitely count on seeing volumes being a more important part of the algorithm next year, and we feel good that the calendar of programming we have, the innovation, the media is really going to help drive some of that.

Andrew Lazar

Great. Great, thanks very much.

Michele Buck

Thank you.

Operator

Thank you. Our next question comes from the line of Ken Goldman with JPMorgan. Please proceed with your question.

Ken Goldman

Hi, and thank you. Along the same lines of 2021, if I can, Michele, you pulled back a little bit on advertising this quarter. It's been a little up and down this year, for understandable reasons. I'm just curious what your thoughts are, in general, on what the Company's plan is for advertising and marketing, in general, as you get into what, hopefully, will be a more normal year in 2021.

Michele Buck

Sure. We definitely believe in investing in our brands. That is a critical piece of our growth model on the business. Clearly, as we mentioned to you, we had pulled back on some spend in areas where we just thought, given the pandemic, it didn't make sense, for example, in refreshment, where we knew consumer usage was down significantly, but as we looked at 2021, and as we've started to see the momentum that we're seeing, and some of the recovery, we definitely plan on taking our investment levels to where we would like them to be and more in line with where they have been historically. So, you'll see us really leaning in to drive the consumer and to leverage some of the behaviors that we're seeing.

Ken Goldman

Thank you, and then, for a follow-up, you didn't do any share repurchases this quarter. I think that's the first time in two years, and the last time was right before you bought Pirate's Booty. I want to ask if the lack of repo is an indication of a pending deal, of course, but I am curious how you would describe the current environment for potential transactions. I guess, particularly, are targets maybe more willing to sell because they can do so off a higher sales number than usual, or are they more hesitant because they, I guess, kind of want to ride this demand wave as long as they can.

Michele Buck

Steve, do you want to take that one?

Steven Voskuil

Yes, I'd be happy to. So, first, just on the share repurchase, I'll just echo what you said, don't read anything into that. I would say for this year, we have taken a little bit more cautious approach to liquidity, in general, you know, going back to the beginning of the year and the COVID phase, just taking a little bit more cautious approach. We will be revisiting that as we look at next year, and I would say, in general, our capital allocation priorities haven't changed.

With respect to M&A specifically, it's probably more the latter. I think people are still—the ones that are the most interesting are riding the wave and they still have valuation expectations that look like they did pre-COVID, if not higher, but I would say we're continuing to have an active funnel, continue to look at a number of opportunities, and will continue to update the market as appropriate.

Ken Goldman

Great. Thank you both.

Operator

Thank you. Our next question comes from the line of Robert Moskow with Credit Suisse. Please proceed with your question.

Robert Moskow

Hi, thank you. I think the recovery expected in 2021 in international and other is—you have a 2% headwind this year in 2020, but can you give us a little bit of color as to the condition of your business in Mexico and India and China? Is it easy to assume that things can go back to normal or has the pandemic impaired your commercial capabilities at all, or the retailers' desire to merchandise confectionary products in those markets?

Michele Buck

Yes. So, first of all, I'd start by saying certainly there's a lot of uncertainty and volatility with the pandemic. We all know that we're seeing the ups and downs of occasional increases of spikes in markets around the globe. That said, I would say that we were pleasantly surprised by our performance in international. Our team did a great job executing in this very challenging environment. I think that we've seen, while each market is a little different and the use of the category is a little bit different, consumers are really looking during this time for brands they trust, and we've done a great job over the past couple of years building the Hershey equity.

We were pleased with the rebound that we saw in many of our markets. I think I mentioned in India our business was now up 6%, versus it had been down. We gained market share across almost every market on our core chocolate category. So, I wouldn't say that we believe our ability to drive the business has been impaired in any market on a permanent basis. Just as we are pivoting in the U.S., I think we've pivoted to where the opportunities are in international, and we feel good about the recovery and plan to continue to deliver against that.

Robert Moskow

Thanks. Can I dive a little bit deeper into Mexico? Are there any packaging requirements that the government is making on nutritional values, or any concerns about the category, how that might impact the category?

Michele Buck

Yes, absolutely. The government did put in place front-of-pack labeling changes in Mexico, and that new packaging is now in the market and we are beginning to monitor the trends. We believe consumers know our category as a treat, they know it has sugar, and so we expect that we'll see less impact from that than perhaps other categories will, but we will, of course, keep a close eye on that. I would say Mexico has been one of the harder hit developing markets relative to COVID, so we feel good about the progress we're seeing, but it's a little slower than some of the other markets.

Robert Moskow

Very good. Thank you.

Operator

Thank you. Our next question comes from the line of David Palmer with Evercore ISI. Please proceed with your question.

David Palmer

Thanks. Good morning. A question on your share gains in the U.S., and particularly in chocolate. In your prepared remarks, you touched on this, how adaptive you were by market, by channel, by each state, in terms of S'mores. Some of that's related, or might be related to supply chain. Could you talk about that part of it? The reason I'm asking is because, if there is a supply chain breakdown or lack of adaptability by a competitor, maybe that will represent share gains that they can reverse somewhat in '21, and I have a follow-up.

Michele Buck

Yes, absolutely. I would say I believe our share gains are a testament to both our strong brands, our consumer understanding, our programming, as well as to the supply chain execution and execution at retail, both of which tend to be core advantages for us as a company. So, I think we're seeing our categories and our brands are definitely resonating with consumers, and, as you mentioned, we really pivoted with the consumer. Very early on, we tried to understand how consumer behavior was changing.

We've talked to all of you before about the fact that our category split is a third, a third, a third, take-home, instant consumable and seasonal, and as we saw consumers shift to more at-home behavior, we very early on shifted the focus in our portfolio to really dial up S'mores, Twizzlers for movie nights, our baking product activities, and then within the seasons, even with Halloween, we made that decision to lean in and drive and build a Halloween season, versus back away from it, and everything related to that, relative to let's set the season early, so we can get consumers in, in pre-trick-or-treat, you know, let's make sure we are smart about the portfolio that's out there and not overly index to seasonal SKUs, etc., and then we worked really hard on messaging, to message consumers safe ways to celebrate the holiday. We dialed up e-commerce as consumers shifted to e-commerce, and because we had invested in capabilities in that, we were able to do that.

Then, I think a lot of the strong investments we've made in other capabilities over the years helped us during this time to execute well, and some of those go beyond supply chain. We've made investments in better understanding consumer trends, we've made investments in our ability to forecast at a much more granular level, we've made media investments to target better, and certainly we've invested in our plants all along the way, which really enabled us to pivot quickly to safety protocols and really be able to continue to execute, and then we made the decision to keep our retail sales teams at retail.

So, as I think about that share gain, I would say, clearly, we would expect to continue to see share gains, clearly, through the spring of '21. We would expect that they would moderate after that, though we're certainly expecting to hold onto share. We will continue to drive our outstanding programming, and also continue to execute supply chain with excellence.

David Palmer

That's helpful, thank you, and then just on—any sort of one-times from this year that we should be thinking about from a model perspective? I'm thinking about COVID-related friction costs this year, but also you might add back some SG&A in parts and other. So, any one-time-type comparisons that we should think about? Thanks.

Steven Voskuil

Yes, I think we talked about in the prepared remarks. On the top line, we had about a two-point impact, so you can right away say there's a drop through that two points into profitability, but then if you take a look at the net costs for COVID, so protective equipment and employee incentives that we had early in the year, and you net them against the DME optimization, the media optimization that we did, as well as the T&E savings, it was a net slight positive on those two pieces, and so that, we would expect to mostly go away. We'll have some lingering costs next year, probably less one-offs in any quarter related to COVID, PPE and so forth, that continue, but net, it was just a slight positive, outside of the two-point drag on the top line.

David Palmer

Thank you.

Operator

Thank you. Our next question comes from the line of Chris Growe with Stifel. Please proceed with your question.

Chris Growe

Hi, good morning.

Michele Buck

Good morning.

Chris Growe

Hi. I had a question for you. If I look back at Halloween, I'm curious, if you split the season apart—you had given some information around this last quarter—sort of the early season part and the trick-or-treat season part, kind of how each piece performed, if you can give a color on that. We have some information from IRI, but I'm curious if you have better information than we have. Then, I'm also curious, as I think about that early part, if that's more indicative of what you expect for the holiday season, as we move into Christmas, and that kind of time, where you don't have a trick-or-treat event. Could that early season, if you start that season early, in particular, in stores, be more like what we saw in the early part of Halloween, if that makes sense?

Michele Buck

Yes. Clearly, we saw that, within the season, the early part of the season performed more strongly, and the later part, that's more trick-or-treat focused, performed a little bit softer. Now, we had anticipated that, so, overall, the season performed exactly in line with our expectations. As we look at the total season, we were quite pleased that our sales were actually up versus year ago, as was our sell-through up versus a year ago. So, during a time of the global pandemic, I think it speaks to the resiliency of the category and the consumers' desire to really hold onto and continue to celebrate the traditions and fun occasions, like this, in their family lives.

As we look at holiday, holiday has some different consumer dynamics than Halloween, and so we believe it'll behave a little differently. I don't think we're going to have some of the pressure that we anticipated coming into Halloween. The category should be quite strong. Consumers use the product in different ways. It's much more about family occasions. We aren't as big in gifting, some of the areas of the category that might be a little bit more hard hit. So, we expect solid results, given that skew to at-home consumption.

Chris Growe

Okay, thank you, and then just a follow-on that, are you shipping in holiday product early, and would that have been an incremental benefit? Did we see some of that in the third quarter more than we would have seen historically?

Steven Voskuil

Yes, we did, just like we did with Halloween, started shipping in holiday a bit early, so you do get some pickup in the third quarter for that. That'll take a way a little bit from the fourth quarter, maybe on the order of 50 basis points.

Chris Growe

Okay, great.

Michele Buck

We also did that to drive the consumer behavior early, as well, just as we did with Halloween. As Halloween was still on the floor, holiday was also out there, so that consumers could also gravitate to the holiday pretty quickly. Yes, strong Halloween sell-through really helps us, because it helps us get that fast start to holiday, because it clears the space to be able to put holiday on the floor.

Chris Growe

Okay. Thanks so much for the color there.

Michele Buck

Absolutely.

Operator

Thank you. Our next question comes from the line of Jason English with Goldman Sachs. Please proceed with your question.

Jason English

Hey, good morning, folks. Congratulations on a good quarter. That bodes well.

Michele Buck

Thank you.

Jason English

I want to pick up on the back of Chris' questions and try to tease out a little bit more of the outlook on holidays going forward. The Halloween early part selling was phenomenally stronger, much better then, I think, any of us as expected. I think a big part of that's due to the merchandising programs that retailers had. It seems like they started bigger and earlier than they usually do. Has that, do you think, influenced how they're going to approach other seasons going forward? Said more directly, do you expect retailers to provide more merchandising support behind the category into holiday, into Easter, than they otherwise would, coming out of the success they saw in Halloween?

Michele Buck

We've always had pretty strong merchandising support at every season, and one thing we always think about with seasons is when we get it on the floor, because we know that consumers will buy that holiday or seasonal product, whether it's Easter, wherever, early for in-home consumption. If you get it out there, it kind of sparks the trigger of, you know, fun moments earlier. So, I don't know that I could say specifically that we can anticipate that retailers are going to merchandise it even more than they ever have. I do think that they will be focused on making sure that they definitely get it out early to capture the early part of the season, since that is the piece that is a bit more stable.

There were a few retailers—as you can imagine, with the uncertainty of Halloween, and the fact that all these decisions about what to do with Halloween really had to be made in early made, when things were quite uncertain, and schools were closed, and bars and restaurants, and all of that, so there were a few retailers who had pulled back on Halloween, and based on the results of the season this year, they will likely have more confidence going forward, which should help to make for an even stronger Halloween next year, and probably also build confidence for the other seasons, like Easter.

Jason English

That makes a lot of sense, and then one more question on the—I'm sticking with follow-ons to Chris' question, which I thought was solid. The early part of the season versus the latter part of the season, the earlier part of the season was exceptionally robust, and you said the late part was a bit softer, but somewhere in your remarks, I think you said all-in total holiday—so both early part and late part—finished down mid-single-digits for the category. I think, mathematically, if you get the category down in single-digits, we're going to have see some pretty sharp declines coming through the retail sales data in the next couple of weeks, as we capture that late part of the season. Am I thinking about it right? Am I interpreting your comments correctly?

Michele Buck

Yes. Yes, you are interpreting them correctly. Category was down mid-single-digits overall, as much as our business was actually up, and we will see some of those declines.

Jason English

Okay. Thank you very much.

Melissa Poole

Yes, and, Jason—it's Melissa—one other thing to just keep in mind, there is a little bit of a timing impact from the Nielsen and IRI data given the season was on a Saturday versus a Thursday, and based on retailer reporting days, so you will probably even see it down even more, and you'll have to wait until kind of mid-November until you see some of those last couple of days being reported. So, some of it, when you see, will be just the timing shift because of the day of the week, and some of it will certainly be the declines in trick-or-treat at the end.

Jason English

Understood. Thank you.

Operator

Thank you. Our next question comes from the line of David Driscoll with DD Research. Please proceed with your question.

David Driscoll

Great, thank you. Good morning, and congratulations on great execution in the quarter.

Michele Buck

Thanks, David.

David Driscoll

I had two questions. The first one—just two relatively small ones. On the other expense commentary, I think through the year-to-date period other expense is only a small number, but your full year projection of $100 million to $110 million dollar on that means it's a very massive number in the fourth quarter. Am I doing the math right? Is that correct, on how the pattern lays out for other expense. Then, related—just another follow-up on your volumes expected in the fourth quarter. I think in your prepared comments you said North American organic growth similar to third quarter, but pricing only like a half-point, so that would mean volume is something like five percentage points positive in the fourth quarter. Am I doing those two pieces right? Any color you can give on those two comments?

Steven Voskuil

Yes, I'd be happy to. So, on the tax side and other expense, you're exactly right, we will have a large other expense in the fourth quarter. Now, that's consistent with what we've been saying, even in the early guidance earlier in the year. Then, along with that, a lower tax rate in the fourth quarter. If you do the math on the tax rate, you also have to settle for a lower tax rate. So, that's how those two lines will play out.

Yes, on the volume up in the fourth quarter, you're thinking about it the right way. We do have some inventory replenishment that will happen in the fourth quarter. We saw that in the third, we'll see some more of that, or that continue into the fourth. We're also lapping some elasticity after the price increase last year, and then this continued strong share gains. Those three things are part of driving that fourth quarter volume.

David Driscoll

Michele, a bigger picture question. Hershey took pricing in most of the portfolio, outside of seasonal candies, in 2018, and then in 2019. Given the negative impact to Halloween for the category, would you agree that now is probably not the time for seasonal price increase actions, maybe this gets delayed to 2022, or sometime later, until we get a normal consumer environment? Essentially, I'm just asking you to assess our ability to pass through cost increases through pricing actions. It's a weird environment and I don't know how it's altered that calculus. Thank you.

Michele Buck

Obviously, I can't speak to any specifics about our specific—any upcoming specific pricing actions. What I can say is there's been no change to our pricing strategy of smaller, more frequent increases. That doesn't necessarily mean we're going to have the same amount of pricing every year, or that we would always announce pricing at the same time. We did, for example, actually have a small price increase this past year on our food service business in the third quarter. If we look over time, we have been able to price at various times and various economic conditions.

What's important to us is—we do think pricing is an important part of our algorithm, but as we've talked about before, we really want to grow through balanced growth across levers, distribution, velocity, innovation, price, etc. We know that that is certainly the one piece of the portfolio that we have not yet priced, and I think it's fair to say that, given that we haven't announced a price increase at this moment in time, the magnitude of pricing in '21 would be less than we've seen in prior years, at least at this point.

We've been pleased that we've seen conversion be pretty good this year, even in a very difficult economic environment, and I think that continues to demonstrate what we've seen over the years, which is the category is very resilient, our brands our strong, we continue to invest into our brands, and that does allow us for an even greater amount of pricing power.

David Driscoll

Really helpful. Thank you so much.

Operator

Thank you. Our next question comes from the line of Steve Powers with Deutsche Bank. Please proceed with your question.

Steve Powers

Yes, hey, thanks. Good morning. I guess, building somewhat on earlier questions, I'd love a little bit more color around just your general mindset heading into '21, as you work through your planning process. Clearly, there are parts of your business that have been under pressure this year, international, movie theaters, vending, specialty, etc., and hopefully all those set up for at least directional recovery in the year ahead, but at the same time you've been gaining a lot of share. You had great success in at-home categories, like baking and with initiatives like S'mores, all of which is fantastic momentum, but, again, could set up for difficult year-over-year comparisons. So, as you size it all together, I guess, is there a way to frame your thinking at a summary level to what degree those various puts and takes sort of just net each other out in your mind, or are you approaching '21 planning thinking we've got either a net easier or net harder setup versus what one might consider typical? Thanks.

Michele Buck

We're pleased with the momentum that we are seeing, and I would say your call-outs and what you shared about some of the ups and downs of the business, I think are very accurate. We believe we're seeing that our category and our brands really resonate with consumers, and especially at a time like this, where they're looking for some of those moments of goodness, moments of happiness. We're really pleased with how we've been able to pivot with the consumer, and also pivot with our capabilities, to be able to execute within this environment, and we feel good about that momentum and our ability to continue pivoting.

This year, obviously, it was consumers shifted to take-home, and so we dialed up S'mores and we dialed up Twizzlers and we dialed up baking, and we leaned in to create the season, to make sure that we could capture that opportunity, giving consumers new ways to participate in Halloween, that, frankly, we believe those things, like candy slides and candy graveyards, and all the creative things people did, will probably become a part of their ongoing traditions, and they have just evolved.

As I mentioned, we were able to dial in and accelerate e-commerce, and I think as we look to next year, we are prepared, if the consumer pivots yet again, to be able to pivot with them. I think we've built—we've demonstrated an ability to execute well during this environment, and also to pivot from an executional perspective, whether it's at retail or in our manufacturing facilities. So, we're very focused on that. We've captured, as well, some cultural positive effects, I think, capabilities we've built in terms of operating in this environment, that perhaps allow us to make decisions more quickly, and we think that is an enabler for us going forward. So, we feel good as we look to the future.

Steve Powers

Thanks for that, Michele. I don't know if you want to take this one, or Steve, but just as a follow-up, sort of unrelated, any comments you might have on just current levels of promotion, the promotional environment, and what you expect to see there over the balance of 4Q and into '21? Thanks.

Michele Buck

Yes, we don't see any significant change relative to promotional activity. We didn't really see it this year, we didn't execute anything significantly differently, and nor do we expect to see anything in the future.

Steve Powers

Okay, perfect. Appreciate it.

Operator

Thank you. Our next question comes from the line of Nik Modi with RBC. Please proceed with your question.

Nik Modi

Yes, good morning, everyone. Michele, I was hoping you could provide some context on the partnership with Google that you used during the Halloween period, and do you believe this capability can be leveraged for this holiday season, but also kind of for your everyday business, as you kind of look forward?

Michele Buck

You know, we are continuing to leverage different types of data and analytics and insights more and more across the business, and we continue to really try and stay on top of tracking consumer sentiment, and leveraging data and analytics to tailor copy, to tailor messaging, to tailor media. So, more and more, we are operating at a more sophisticated level, relative to using multiple data sources, and also using that to reach consumers at the right places with the right message at the right time.

Nik Modi

I guess what I'm trying to get at is, you know, is this kind of new way of kind of targeting consumers—like, the return that you see from what you've done, can you just give us any kind of understanding? Because, one thing I'm noticing across the entire CPG landscape is companies are spending more money, but they're spending more money on the same message, and, in fact, new consumers are being recruited, usage occasions are changing, and so it really requires a change in how you talk to those consumers, and so I find this Google partnership incredibly compelling for you guys. I'm just trying to get better context on how it's changing the return profile of your spend, if you can provide any context on that.

Michele Buck

We have a continuous focus on optimizing media and the returns on our media, we always have. We've had strong media ROIs forever, and our challenge is how do we keep making them better, and then we continuously optimize based on that. Right now, it's a big spend area for us. It's an area we're very focused on elevating, and it is about making sure—right now, I would say, some of the biggest opportunity is that opportunity of even more precise targeting, and then once you have that target, the ability to alter the message, and then we alter our media mix accordingly. I would say we see significant movement in that mix on a year-to-year basis as we get better at that. I think we've raised some of the opportunities of how we've gone just very deep relative to specific seasons, whether it's S'mores by zip code, or whether it's specific holidays and looking at sell-through at a store level basis, to be able to dial up media on a zip code level basis, so you'll continue to see more of that. Frankly, that's just becoming a way of how we operate now.

Nik Modi

Great, and last question, just from an innovation standpoint. Can you just provide any context on kind of what's remaining in terms of innovation this year, and how things are going to work in 2021, if there's any clarity you can provide on the launch timing?

Michele Buck

We feel very good about our innovation. Some of the innovations that we are excited about, that are new to the market, include the Reese's pretzel product, a Reese's cup with pretzels in it. We've had a range of KIT KAT flavors. We know, on a global basis, a big part of the KIT KAT portfolio are flavors, they tend to do quite well. We are, on a very small level, launching Snack Cakes, under our Reese's trademark, which delivers that Reese's experience in a slightly different type of product form, and we feel good on that, based some of the early test results, and we will have more coming, some items on our take-home side of our business, that won't get announced until early next year, which is typically the time we announce those things just given reset windows. No major change in our innovation strategy. We think it's working very well for us, we think it's right-sized, and we think it's delivering much more sustainable results.

Nik Modi

Great. I'll pass it on. Thank you.

Operator

Thank you. Our next question comes from the line of Michael Lavery with Piper Sandler. Please proceed with your question.

Michael Lavery

Thank you. Good morning.

Michele Buck

Good morning.

Steven Voskuil

Good morning.

Michael Lavery

You've talked about the increase in e-commerce sales, even if it might have decelerated a little bit, but it's up very strongly. You've said in the past the baskets and dollar ring are higher online. Is that still holding true with the growth that you're seeing now? On the margin side, you've mentioned that there's a small gap, but that you were narrowing it, and that scale would help that. Is that coming along the way that you would have expected and how does that look now?

Michele Buck

Yes, I mean, we've generally seen larger basket sizes, in general, across most channels this year, as people are doing fewer trips and more quantity per trip, so I think that's been somewhat of just an underlying dynamic given the pandemic impact in the marketplace. For us, on our e-commerce business, we've seen very significant growth across the board, but particularly in click-and-collect, where people actually go and pick up their groceries, and also in the local delivery models, as well, versus kind of national deliver. The margins that we have are similar to what we see in bricks-and-mortar.

Michael Lavery

Okay, great, that's helpful.

Michele Buck

In those two areas, where we have similar products, obviously, that we sell in bricks-and-mortar.

Michael Lavery

Right, right.

Michele Buck

Steve, anything you want to add?

Steven Voskuil

Yes, all I'd say is that, you know, we've said in the past that, overall, e-commerce margins are a little bit dilutive. As Michele just said, in click-and-collect and local delivery, very similar, not much impact, and that's two-thirds of our e-commerce business. The piece that is more dilutive is the ship-to-home and, in particular, cold ship, and that's an area where we continue to work with our customers and look at our overall investment with those customers, and joint business planning, to drive efficiencies over time, so that those margins align.

Michael Lavery

Okay, thanks, and I just want to follow up on S'mores. I thought that your data analysis and insights there to push that the way that you did was interesting. As you're seeing cases rise again now, are you replicating that? Are you seeing similar results? Is there a S'mores surge, we should expect? Would it be right to assume that those Hershey's Mile Chocolate Bars are probably some of the highest margin ones that you have?

Michele Buck

We have really expanded S'mores from—at one point, it was a very focused time of year to really capturing S'mores as a year-round opportunity. Especially, if you think about how different weather is across the entire country, there are lots of opportunities to continue to expand that. So, we're very focused on that. We're also very focused on the upcoming baking season, where we know that consumers will be spending time at home. It's already a natural baking season. So, we'll be looking to really optimize. We're able to drive, you know, levering insights around that season, as well.

Michael Lavery

Okay, great. Thanks a lot.

Operator

Thank you. Our next question comes from the line of Bryan Spillane with Bank of America. Please proceed with your question.

Bryan Spillane

Hi, good morning, everyone. Just one question for me. I think there was a little bit of a commentary in the prepared remarks about inflation and cost of goods sold, so maybe, Steve, could you just give us kind of a lay-of-the-land right now in terms of what commodity costs and just cost of goods inflation looks like currently in the context of—it seems like freight costs are going up, you've had some competitors talk about cocoa prices going up. So, just trying to get an understanding of, you know, directionally, where inflation is headed right now.

Steven Voskuil

Sure. Yes, for us, I'd say, overall, it's been relatively stable. On the commodities side, relatively stable. You saw big movements in commodities across Q2 and Q3, and of course we've talked in the past we mitigate some of that volatility with our hedging program, and I would say today they're fairly stable. There are increases in freight costs. There, too, our teams do a great job of longer term contracting, which helps mitigate some of that increase, so that hasn't been a real material impact for us. We have seen some increased warehousing costs, and part of that's volume and flow-through, along with the share gains and the volume increases that we've seen, so we called that out in the prepared remarks. But, in total, at least sitting at this point, I would say overall COGS is fairly stable, and we'll give more guidance on 2021 when we get into the fourth quarter call.

Bryan Spillane

But I guess we could infer from that, at least from where we sit today, that stable is something that looks like it carries into next year, unless something changes?

Steven Voskuil

Yes, I think that's fair. Next year, you're going to have the 2020 and 2021 crops of cocoa start to bear the LID, so we know there's that to consider, and then there's other things, obviously, on the gross margin side. As Michele said, we'll have a little bit more volume driven than price driven, mix driving gross margin next year, we'll have our continuing productivity goal, and, again, a lot more on that to come when we talk on the fourth quarter call.

Bryan Spillane

All right, thanks, Steve, that's very helpful. Have a Happy Thanksgiving, everyone.

Michele Buck

Thank you.

Steven Voskuil

Thank you.

Operator

Thank you. Our next question comes from the line of John Baumgartner with Wells Fargo. Please proceed with your question.

John Baumgartner

Good morning, and thanks for the questions.

Michele Buck

Good morning.

Steven Voskuil

Good morning.

John Baumgartner

Michele, I'd like to follow up on the Reese's Snack Cakes. You mentioned that it's small right now, but Hershey went down this path about 15 years ago and it didn't really translate into anything material, so I'm curious what the data tells you in terms of changes to the landscape now. Does this maybe mark a new phase of the snack section evolution? I guess, where do you think it slots in? I mean, does it compete against a Twinkie, is it cookies? Just where's the target market? Any big picture thoughts would be appreciated.

Michele Buck

Yes, absolutely. I think we've approached this in a very thoughtful and measured way, which was not a mass launch where we just threw it out there and tried to make it as big as we possibly could at one point in time, but we did a very targeted end-market launch for an extended period of time, so that we could really learn about the proposition. We spent a lot of time in terms of developing the product to make sure that we really understood some of the drivers of liking in this snack area, and we also really thought about where and how we wanted to play and launch. This, for example, is very C-store focused. It is a single-serve type of item. So, we're keeping it as a focused launch.

It is definitely bringing the great chocolate and peanut butter taste profile that we have on Reese's to the snack cake market. So, yes, it is playing in that snack cake area versus other snack cake brands. We had participated in this category for many years through licensing and we learned through that that our brands could participate and extend to the category. We also know that morning snacking has been a growing trend, and our confection items skew more to afternoon and evening, so this is a chance for us to participate in some of that growth, because that is where the snack cakes get utilized.

So, again, we're going to have a very focused rollout and we'll put it in locations where we think we can garner incremental space and where we think there's a strong consumer fit, starting at C-store and looking at other select areas, and then, if it continues to perform well, we will expand, but we will watch it closely and take a measured approach.

John Baumgartner

Great. Thanks, Michele.

Michele Buck

Sure.

Operator

Thank you. Our next question comes from the line of Alexia Howard with Bernstein. Please proceed with your question.

Alexia Howard

Good morning, everyone.

Michele Buck

Hi, Alexia.

Steven Voskuil

Good morning.

Alexia Howard

Hi back. Can I just talk about the C-store channel specifically? It's obviously been under pressure because of the pandemic, but I imagine that there has been some sequential improvement in there. Could you maybe just give us some numbers about how that channel is recovering?

Michele Buck

Absolutely. So, as you said, we've continued to see strength in food and mass and dollar as consumers eat more at home. The C-store class did see a bit of recovery in the third quarter. We saw the business grow in the low-single-digits in the third quarter, which is definitely an improvement versus those early pandemic trends. It did then slow a little bit as summer ended and those summer road trips decreased, with kids going back to school. Our business has tracked pretty much in line with the channel, and significantly ahead of the category, so we have share gains of about 120 basis points in Q3 in that channel. So, seeing some rebounds and some recovery versus where it was in the past, as people are out and about a little bit more than they were.

Alexia Howard

Great, and then as a follow-up—a follow-up, actually, on Bryan Spillane's question about freight costs. I remember back in 2018, as freight costs spiked back then, and that was quite a bit of a headwind for you. It seems as though it's not so much of a problem this time around. Are you able to tell us roughly what proportion of COGS freight actually represents, and how much of that is already contracted out, and what you've learned since 2018 to make the situation this time around a bit more manageable? Thank you.

Steven Voskuil

Sure. Yes, freight costs right now, we don't see as a material impact. If it continues to rise, it'll have a bigger impact. Right now, again, because we're contracted and our teams do a great job of managing those contracts, it's not having a material impact. It's roughly 10% of COGS overall. It's not immaterial, but right now not seeing enough movement there, given the contracting, to really drive a material impact on overall COGS.

Alexia Howard

Great. Thank you very much. I'll pass it on.

Operator

Thank you. Our next question comes from the line of Jonathan Feeney with Consumer Edge. Please proceed with your question.

Jonathan Feeney

Good morning, and thanks very much, and thanks for a great Halloween, personally and professionally. The leanest of my financial ambition has been to give out full-sized candy bars, which I was again able to execute, so thank you.

I have two quick ones. I noticed in the data your pricing in North America is plus 19 on the takeaway, plus 33, is what you reported. Is that just the math, or is there some shrinking or different mix within retailer margins? That was my first question.

Secondly, historically, when you look at—today's velocity is generally tomorrow's distribution, and your velocity has been fantastic. This is a weird year, a lot of people's velocity is fantastic. But, do you anticipate gaining shelf space in that everyday place? You look at these baking items, you look at these take-home items. Like, this is phenomenally better velocity, forget about just the total sales that you're seeing there. Do you anticipate significant share gains, perhaps structural ones—I'm talking share of shelf here—as retailers do resets for holiday and going forward? Thank you.

Michele Buck

Sure. So, two parts to your question. The first was around price and some of the discrepancy, and, yes, there is a mix impact. Honestly, it might be best if Melissa takes you through a deep dive on that, because there's some complexity associated with it, but the P&L is definitely accurate.

As it relates to velocity, yes, good velocity. I like your phrase, today's velocity is tomorrow's distribution, I do think that is very accurate. As we look at the seasons—you asked about holiday—we certainly have been able to garner incremental distribution, incremental SKUs throughout the year, both in terms of everyday and seasons, because we've been able to deliver, and the items that we then put on shelves, not only could we supply them, but then they moved. So, we do feel good about that. We'll continue to take a very disciplined approach and be very careful that we don't over-SKU, so we really have to look at the productivity of every SKU, and as long as it's good, we will be there. But, yes, we have been able to gain some distribution, and going forward, I anticipate that we will continue to be able to, perhaps even through the first part of next year.

Jonathan Feeney

Thanks very much, and I'll follow up with Melissa.

Michele Buck

Very good.

Operator

Thank you. Our next question comes from the line of Ken Zaslow with BMO. Please proceed with your question.

Ken Zaslow

Hey, good morning, everyone.

Michele Buck

Good morning.

Steven Voskuil

Hey, Ken.

Ken Zaslow

I just have one quick question. Everything's been asked and answered. You make a reference in the prepared remarks about Pirate's Booty tracking ahead of your strategic plans. Can you talk about what are the key learnings that you've developed through your years as a CEO that has really helped you kind of make this a better acquisition and implement it? What are you key learnings and what do you take forward to future acquisitions?

Michele Buck

Well, I think a lot of learnings along the way. I guess I would start with—you know, there's a business model for brands that we, as a company, are best with, and that is branded items, where brand matters, where the business has significant scale, probably close that $100 million mark, and it needs to be a business that has a high gross margin, because that's what our business model is. We're a branded company, we invest a lot in marketing, and we have high margins that enable us to kind of invest and grow, invest and grow, and that's our model, that's what we need. So, I think that was one of the biggest learnings to help us select the asset.

I think, secondly, really understanding the strength of the brand and really being able to do the right deep dives on which KPIs we think predict the ability for a brand to scale. Then, I would say really trying to scale the business well, and I would say, hey, we've learned lessons the whole way along the way. As you know, in the past, we bought some businesses that were too small, we bought some businesses that had lower margins, and we had some that we perhaps didn't execute on the scaling as well, and I think we've had a very focused effort on the scaling, as well, and we've gotten much better at that, relative to supply chain, relative to the talent that we need when we buy a company like this, where we want to keep the entrepreneurial spirit, where we want to keep people who know the brand and the business, but we also have to be focused on the point that we're also at a point where we want to scale the business.

I mean, I go back to the scale, the branded nature, the high margin, are probably the biggest ones, and then picking the right underlying KPIs that say it's a sustainable business, because if we can do that, we can make it hum.

Ken Zaslow

Great. I really appreciate it, thanks. Stay well.

Michele Buck

Thank you.

Operator

Thank you. Ladies and gentlemen, that concludes our question and answer session. I'll turn the floor back to Ms. Poole for any final comments.

Melissa Poole

Thank you all for joining us this morning. I will be available after the call to answer any additional questions you may have. Have a great day.

Operator

Thank you. This concludes today's conference, you may disconnect your lines at this time. Thank you for your participation.