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The Hershey Company

Fourth Quarter 2021 Earnings Prepared Remarks

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CORPORATE PARTICIPANTS

Melissa Poole, *Vice President, Investor Relations*

Michele Buck, *Chief Executive Officer and Chairman*

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

PRESENTATION

Melissa Poole

Good morning everyone and welcome to the pre-recorded discussion of The Hershey Company's Fourth Quarter 2021 Earnings Results. My name is Melissa Poole and I am the Vice President of Investor Relations at Hershey.

Joining me today are Hershey's Chairman and CEO, Michele Buck, and Hershey's Senior Vice President and CFO, Steve Voskuil.

In addition to these remarks, we will host an analyst Q&A-only session at 8:30 am Eastern on the morning of February 3rd. A replay of this webcast and our subsequent Q&A session will be available on the Investor Relations section of our website, along with our corresponding transcripts.

During the course of today's discussion Management will make forward-looking statements that are subject to various risks and uncertainties. These statements include expectations and assumptions regarding the Company's future operations and financial performance, 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 during today's discussion we will refer to certain non-GAAP financial measures that we believe will provide useful information for investors. The presentation of this information is not intended to be considered in isolation or as a substitute for the financial information presented in accordance with GAAP. Reconciliations to the GAAP results are included in this morning's press release.

It is now my pleasure to introduce our Chairman and CEO, Michele Buck.

Michele Buck

Thank you Melissa, and good morning everyone.

In 2021, we delivered a record year of production and double-digit sales and earnings growth, with a strong finish and momentum heading into 2022. While the environment remains volatile, we are confident in our ability to continue to respond to the changes in the world around us and deliver another year of advantaged performance in 2022.

I could not be prouder of the entire Hershey organization for the way they continue to unite to overcome obstacles, show courage and adaptability, and persevere to deliver for our consumers, partners, shareholders, and each other during a period of unprecedented disruption.

Before I get into the details on the upcoming year, I'd like to take a few minutes and provide a recap on our 2021 performance.

Within our core U.S. confection business, we have further strengthened consumer engagement and our marketplace leadership. Our Hershey and Reese's brands were just ranked in the top 10 of the most loved brands in America late last year. The category has consistently grown over the past two years, balanced across both volume and price, and channels and occasions.

In 2021, we saw positive retail sales growth in every one of our top 20 confection franchises with an average gain of over 12%. Reese's retail sales have grown nearly 25% the past two years, driving over 20% of total category growth despite only representing 9% of category sales. We acquired Lily's, a fast growing, premium better-for-you offering to drive scale and leadership in this key subcategory alongside our Hershey branded zero-sugar items. And we set sell-through records for every one of our major seasons last year. This has enabled us to retain over 80% of our 2020 share gains, resulting in a two-year share gain of over 130 basis points.

Our ONE brand recovered from pandemic driven declines, growing almost 10% in 2021 and maintaining its share position for the year. And our grocery business was able to hold on to pandemic gains despite increasing mobility in the second half of the year.

Our U.S. snacking business has also contributed meaningfully with one of its strongest years yet in 2021.

SkinnyPop had a phenomenal year, with retail sales growth of 22%, resulting in market share gains of 280 basis points. Pirate's Booty retail sales grew over 26%, with growth over 60% in the fourth quarter as multi-pack sales rebounded with kids returning to in-person learning.

And we couldn't be more excited to welcome Dot's Pretzel's and Pretzel's Inc. to the Hershey's family to further bolster our growth and presence in snacking. Dot's, along with Skinny Pop and Pirate's Booty, delivered nearly $1 billion dollars in retail sales in 2021 with growth of over 30% versus prior year.

Our international teams have also done a phenomenal job, evolving their business model, growing the topline, and continuing to meaningfully enhance profitability. COVID-19 losses have been more than recovered, and the teams secured incremental distribution and activated new and differentiated multi-country campaigns to drive brand equity and capture synergies. The go-to-market model transition in China was executed seamlessly despite the continued disruptions from COVID-19, helping contribute to one of the highest profitability levels we've ever delivered within our international markets.

As we look forward to the year ahead, we remain focused on execution as well as advancing key strategic initiatives that will be critical for our business in the years ahead.

As we shared last year, despite heroic efforts and a record year of production, we were unable to keep pace with accelerating consumer demand. Our teams have worked cross-functionally across the organization and with our key external partners to balance supply and demand, particularly for the first half of 2022, so that we could meet the needs of our consumers and our employees while improving customer service.

While we have several initiatives underway to achieve these goals, including adding both labor and capacity, as well as optimizing our promotional calendar, the environment remains challenging. Omicron cases have resulted in higher absenteeism and pressured production at both our own facilities as well as our suppliers. We expect this to impact the speed we can rebuild inventories and accelerate investment in demand-generating activities, which will likely be limited until the second half of the year. Steve will provide some additional perspective as it relates to our quarterly expectations.

Despite some of these challenges, we have a fantastic calendar for the year that we believe will drive strong, profitable growth across the portfolio and will continue to advance key strategic capabilities for long-term growth.

We expect another strong year of seasonal performance, led by high consumer engagement and record level sell-throughs from last year. We have a great lineup of innovation this year that will bring news and excitement to the category across both flavors and forms. The teams have done a fantastic job prioritizing the news needed across occasions during the year with supply supportability and complexity. And our category management teams have done a phenomenal job maintaining or increasing shelf space by double- and triple-facing top velocity SKUs as we rationalize select items to free up capacity and reduce complexity.

We have strong media support planned, particularly in the second half of the year, as our production and inventory levels are expected to improve. Consumer reach is expected to increase in 2022, as we leverage new partners and capabilities to drive greater media efficiency and effectiveness.

As you all know, pricing will be an important lever for us this year and is expected to drive most of our growth. Historically, our category has successfully been able to execute price increases and we expect that to be the case this year as well. While there are unique factors that could impact elasticities, we are currently expecting performance in line with historical results.

Continued strength of at-home consumption and less cross-category elasticity could provide a tailwind, while reductions in government stimulus and SNAP payments, along with broad-based inflation higher than wage growth, could be a potential headwind. We will continue to evaluate performance closely and provide updates on expectations as we move through the year.

Within our snacks business, we will build on our 2021 momentum with accelerated media investment and new campaigns in 2022, expansion into new pack types and occasions, price realization and distribution expansion. The team continues to build out our supply chain infrastructure to support the tremendous growth on these brands and enable us to efficiently integrate future acquisitions.

We are working closely with our newest team members at Dot's Pretzels and Pretzel's Inc. to continue the incredible growth they have driven over the past several years. In 2021, Dot's grew over 55% driven by both distribution and velocity gains and they grew their pretzel category share by 330 basis points. Our teams will be focused on sharing learnings, executing with excellence, and developing a successful integration plan to unlock even more top line and bottom line growth in the future.

Within our international business, we will continue to capture new distribution opportunities in India and Mexico, expand on our successful HerSHEy activation from last year across markets, invest in media to drive brand equity and drive price realization, and expand our better-for-you offerings with new portion control packs and more low sugar and dark chocolate offerings.

In addition to remaining laser focused on execution, we will continue to advance key capabilities and initiatives this year that we believe will be critical enablers to our future growth.

Within our supply chain, we are making significant investments in people and technology to enhance our employee value proposition and increase both manufacturing capacity and reliability. In addition to appreciation bonuses, we increased our manufacturing headcount in 2021 to reduce overtime and increase the amount of time employees can have off, added additional plant holidays, enhanced employee support through mentoring and training programs, and increased yearly incentives.

Beyond investing through our people-first manufacturing model, we are also investing in the capacity and reliability of our supply chain. In the past two years, we've brought online four new manufacturing lines while also increasing flexibility and capacity of existing lines, and added a new distribution center with state-of-the-art technology and enhanced agility. And as we shared last year, we have several additional capacity expansion initiatives underway related to North American Confectionery that will unlock additional growth opportunities.

For our snacks business, our teams are also developing a multi-year strategy to drive efficiencies through integration and geographic expansion to get production closer to demand. We are also continuing to advance our digital capabilities with the launch of our new ERP platform in Mexico during the second quarter, new tools to provide enhanced end-to-end planning processes to improve visibility and agility, and the rollout of a proprietary analytics platform that will provide us with deeper consumer insights and more efficient media targeting.

We look forward to sharing a few more details on this capability at CAGNY in a few weeks.

With that, let me turn it over to Steve to provide more details on our financial results and outlook.

Steve Voskuil

Thanks Michele. Good morning everyone.

I want to build on Michele's comments and share how proud I am of the agility and resilience our team continues to show in the second year of the pandemic. In the face of unprecedented industry-wide supply chain disruptions, and a constantly evolving operating environment, we delivered exceptional results each quarter in 2021, culminating in full year reported net sales growth of 10.1% and adjusted EPS growth of 14.3%.

Beyond delivering a record year, we invested in our brands, capabilities and people to drive differentiated growth for the future. We supported over 25 brands, investing nearly 8% of net sales, and expanding our portfolio to new consumer occasions through the acquisitions of Lily's, Dot's and Pretzel's. We progressed key projects, expanding capacity and building our digital infrastructure across the enterprise. And we invested in our people, focusing on wellbeing and safety, improving the total value proposition of our teams, and advancing our diversity and inclusion initiatives.

It's this focus on operating with excellence and investing in our brands and capabilities for differentiated growth that drives our proven track record of on-algorithm earnings growth and peer-leading shareholder returns.

In the fourth quarter, we delivered reported net sales growth of 6.4%, including a 2.2% benefit from acquisitions. Organic constant currency net sales growth of 4% was driven primarily by list price increases across the portfolio, along with lower levels of promotional activity associated with capacity constraints and reduced customer services levels. As expected, volume was approximately a 2-point headwind in the fourth quarter, driven by fewer shipping days.

Net sales growth lagged retail sales growth, driven by the continued contraction of retail and distributor inventory levels, fewer shipping days and strong seasonal sell-through. The impact of these factors was consistent with our expectations.

Now, turning to profitability, adjusted gross margin declined 40 basis points in the fourth quarter to 43.5%. As expected, higher supply chain costs and inflation persisted, along with unfavorable mix, driven by accelerated growth of our North America Salty Snacks segment. These pressures were partially offset by accelerating net price realization. I am extremely proud of the tremendous effort across the organization to respond quickly to stronger-than-expected demand, industry-wide supply disruption, and inflation over the course of the year. While full year gross margin came in below our initial expectations heading into the year, our actions enabled us to capture significant incremental demand and deliver another year of advantaged margin performance.

Advertising and related consumer marketing expenses decreased by 6.9% in the fourth quarter. As we shared last quarter, we continued to optimize marketing investments due to capacity constraints on select brands, particularly in the North America Confectionary segment. These reductions remain purposeful and we continue to invest in strategic and supportable confection brands and occasions such as Halloween and Holiday, while also increasing investment in our salty snack brands.

Operating expenses, excluding advertising expenses, increased 8.2% in the fourth quarter, driven by higher capability and technology investment, along with acquisition costs related to the acquisitions of Dot’s and Pretzel’s Inc.

The adjusted effective tax rate for the fourth quarter was 2.2%, an increase of approximately 10 points versus the year ago period, due to unfavorable country rate differentials and lower tax credits.

The sustained consumer demand and strong execution fueled strong cash generation in the fourth quarter. For the first time in Company history, we generated operating cash flow exceeding $2 billion in 2021, reflecting an increase of over 20% versus the prior year. This cash generation allowed strong reinvestment in the business, and capital return to our shareholders. In the fourth quarter total capital additions, including software, were approximately $150 million, bringing the full year investment to approximately $500 million, which was in line with expectations.

In the fourth quarter we paid $181 million in cash dividends, totaling over $686 million in cash returned to shareholders in 2021.

Now, let me shift gears and share perspective and expectations for 2022.

From a top line perspective, we expect net sales growth of 8% to 10%, with a 3-point to 4-point benefit from the acquisition of Dot’s, Pretzel’s and Lily’s. Price is anticipated to be the primary driver of growth with solid price realization expected across the entire portfolio. The impact of these pricing actions is expected to skew slightly to the first half of the year. Volume elasticities are planned in line with historical levels, and will be partially offset by inventory replenishment and brand activations, including media, innovation and seasons.

From a profitability perspective, we expect growth margin to be down in 2022 at a company level with comparable dilution to 2021. Investments in labor within our manufacturing network and higher logistics and raw material costs will be partially offset by price realization.

Despite gross margin pressures, we remain committed to investing in our business for long-term growth. Brand investment remains a critical lever for growth with plans to invest over $500 million in our brands in 2022. New media partners and capabilities are expected to drive enhanced efficiency and effectiveness, allowing us to meaningfully increase our consumer reach while only moderately increasing our spend. Spending is planned down in the first quarter as we continue to navigate capacity constraints and supply chain disruptions, but will accelerate as we progress through the year and can support incremental volume.

Operating expenses, including both divisional and corporate expenses, are anticipated to grow in line with sales this year. Divisional expenses are expected to increase due to salary and benefit inflation, increased travel and meeting expenses, and amortization related to recent acquisitions. Corporate expenses are expected to be roughly flat versus prior year as incentive compensation favorability is largely offset by salary and benefits inflation and higher capability and technology investments, including incremental depreciation related to our ERP transformation.

We expect our full year 2022 adjusted effective tax rate to be similar to 2021 as we plan to continue to invest in tax credits. Full-year other expense, which includes our spend on those tax credits, is estimated to be between $105 million and $115 million. Finally, interest expense is expected to be roughly $125 million in 2022.

We expect our core business to deliver earnings per share growth at the high end of our long-term algorithm, and with the addition of Dot's, Pretzel's and Lily's, we expect adjusted earnings per share growth of 9% to 11%.

For 2022, our capital allocation priorities remain the same. We expect capital investment to remain elevated this year as we begin to implement our new ERP system and add incremental capacity for our fastest growing brands, with that capacity expected to come online in 2023 and 2024. Approximately 60% of our capital expenditures is related to capacity expansion, while another 20% is related to our ERP transformation and other digital infrastructure projects.

As Michele shared, we are pleased with where we ended the year and the momentum we have entering 2022. But we continue to operate in a very volatile environment; there is inevitably a higher degree of risk in the current operating environment, but we remain confident in our ability to deliver another strong year of balanced top and bottom line growth.

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

Wrap Up / Close

Thanks, Steve.

While the environment remains volatile, I couldn't be more excited about the initiatives we have underway or more confident in our teams' ability to continue to quickly respond and adapt to changes in the marketplace. We are energized by the opportunities ahead of us to delight consumers with even more delicious Hershey products than ever before.

To live our purpose and meet the needs of our consumers, we rely on the dedication of our employees, a strong network of partners and suppliers, resilient growing conditions from which to source the highest quality of ingredients, thriving communities, shareholder trust, and deep relationships with our customers and consumers. Over the past year, we've continued to focus on new and innovative ways to engage these stakeholder groups and work together to bring our iconic products to the market responsibly.

We are honored to be named for the third straight year as one of America's Most JUST Companies and to be in the company of the 100 publicly traded companies leading the new era of responsible capitalism. This recognition comes on the heels of Hershey being named to the Dow Jones Sustainability World

Index and number one on Forbes' list of the World's Top Female Friendly Companies. I couldn't be prouder of the progress we've made and our teams' commitment to putting goodness into action.

Thank you for your time this morning. I invite you to listen to our live question-and-answer webcast, which will begin today at 8:30 a.m. Eastern time and will be available at thehersheycompany.com. Thank you.