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Hormel Foods Corp. (HRL)

Q3 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning everyone and welcome to the Hormel Foods Third Quarter 2022 Earnings Webcast and Conference Call. All participants will be in listen-only mode. [Operator Instructions] After today's presentation, there will be an opportunity to ask questions. [Operator Instructions] Please note this event is being recorded.

At this time I'd like to turn the floor over to David Dahlstrom, Director of Investor Relations. Sir, please go ahead.

David W. Dahlstrom

Director-Investor Relations, Hormel Foods Corp.

Good morning. Welcome to the Hormel Foods conference call for the third quarter of fiscal 2022. We released our results this morning before the market opened, around 6:30 AM Eastern. If you did not receive a copy of the release, you can find it on our website at hormelfoods.com under the Investors section.

On our call today is Jim Snee, Chairman of the Board, President and Chief Executive Officer; and Jacinth Smiley, Executive Vice President and Chief Financial Officer. Jim will provide a review of the company's third quarter results, an update on business initiatives, and a perspective on the remainder of fiscal 2022. Jacinth will provide detailed financial results and further commentary on the third quarter and our outlook.

The line will be open for questions following Jacinth's remarks. As a courtesy to the other analysts, please limit yourself to one question with one follow-up. If you have additional questions, you're welcome to get back into the

queue. An audio replay of this call will be available beginning at noon today, Central Standard Time. The dial-in number is 877-344-7529 and the access code is 1874087. It will also be posted to our website and archived for one year.

Before we get started, I need to reference the Safe Harbor statement. Some of the comments made today will be forward-looking and actual results may differ materially from those expressed in or implied by the statements we will be making. Please refer to our most recent annual report in Form 10-K and quarterly reports on Form 10-Q, which can be accessed at hormelfoods.com under the Investors section.

Additionally, please note the company uses non-GAAP results to provide investors with a better understanding of the company's operating performance. These non-GAAP measures include organic volume, organic net sales, adjusted operating income, adjusted operating margin, adjusted diluted earnings per share and net debt to EBITDA. Discussion on non-GAAP information is detailed in our press release and third quarter earnings supplement, which can be accessed from our corporate website or located on our investor website, investor.hormelfoods.com.

I will now turn the call over to Jim Snee.

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Thank you, David. Good morning, everyone.

With the results we announced this morning, we have successfully achieved seven straight quarters of record sales and four consecutive quarters of earnings growth. In the current environment, this is an especially notable achievement.

Over the last 12 months, we have delivered four consecutive quarters of record sales in excess of \$3 billion. We've grown diluted earnings per share 15%, compared to the trailing 12-month period. We've made considerable progress across our supply chain, including investments in capacity to support high-growth categories and improvement in the staffing levels, production volumes, inventories and fill rates.

We've integrated our largest acquisition to date with the Planters snack nuts business, we began transformational work on the Jennie-O Turkey Store segment, while simultaneously managing through the impacts of HPAI. We further derisked commodity profitability with a new pork supply agreement. We have generated over \$1 billion in operating cash flow, and we've increased the dividend for the 56th consecutive year. Our experienced management team has again proven their ability to navigate and grow the business in volatile market conditions. And these results demonstrate that our business is built for growth, our brands remain vibrant and relevant, our strategies remain effective and our inspired team members around the world truly embody our results matter mentality.

In the third quarter, we delivered another quarter of record sales and double-digit operating income growth. Our team's execution again played a pivotal role in growth this quarter. As together, we overcame significant challenges, including continued broad-based inflationary pressures, persistent upstream and downstream supply chain disruptions, limited turkey supply and impacts in China from COVID-related restrictions and temporary plant shutdowns.

Double-digit operating income growth this quarter was led by outstanding contributions from Jennie-O Turkey Store and Refrigerated Foods. The Jennie-O Turkey Store team significantly outperformed our profit expectations

for the quarter as the team effectively managed limited turkey supply and maximize operational performance, all while working to restore the impacted turkey farms across the supply chain. Refrigerated Foods delivered double-digit, value-added earnings growth on retail and foodservice items, more than offsetting lower commodity profitability.

Similar to prior quarters, our balanced business model was able to offset inflationary pressures and supply chain disruptions, which were both significant headwinds during the quarter. Most importantly, our performance indicates our brands remain healthy and are generating growth. Consumers and operators have continued to engage with our brands due to their value, convenience and versatility. The team drove volume, sales and share gains at retail for brands such as SKIPPY, Hormel Gatherings, Hormel chili, Dinty Moore and Mary Kitchen. I would like to acknowledge the tremendous work and coordinated efforts of the SKIPPY team who supported our customers and the category this past quarter. We continue to drive growth across our premium retail brands for products such as Applegate natural and organic meats and Columbus charcuterie. We also experienced an acceleration across our center store portfolio, which is firmly aligned with the value shopper.

The Grocery Products segment delivered strong organic volume and sales growth during the quarter and is well positioned to grow as consumers seek flexibility, versatility and yield at lower price points. Demand for foodservice products remained elevated as well as operators again turn to our items to help mitigate labor pressures and diversify menu offerings. Value-added products such as our premium bacon and sausage, sliced meats and line of premium prepared proteins performed exceptionally well this quarter. We saw great demand for brands, including Austin Blues, Natural Choice, Bacon 1, Café H and Old Smokehouse.

Regardless of channel, our brands have responded well to the pricing actions we have taken over the past 18 months, even as current macroeconomic conditions pressure some of our customers, consumers and operators. The demand environment has remained favorable, especially for food and convenient meal solutions. We have seen this in the positive syndicated data for many of our grocery and refrigerated products and in the momentum behind our branded foodservice items.

In some cases, demand is still outpacing our ability to fully supply. Our broad portfolio of products, spanning value tiers, eating occasions and channels positions us well. We anticipate some additional impact from elasticities, as new pricing actions are reflected in the marketplace and we have accounted for this in our outlook.

To date, the impact of price elasticities has been muted by other factors, such as distribution and assortment gains, and as we have increased production to drive improved fill rates. Our teams remain keenly focused on the long-term needs of the business, our strategic priorities, and protecting the equity of our brands.

Hormel Foods has a history of continuously evolving to become a better, more agile and more balanced global branded food company. In early August, we announced the next step in our strategic evolution, our Go Forward initiative. Effective October 31 of this year, the beginning of fiscal 2023, we will be organizing the business into three empowered segments: Retail, Foodservice and International. As a result of this initiative, we expect to elevate our clear strategic growth priorities; better align the business to the needs of our customers, consumers and operators; deepen our sales capabilities; simplify our approach to customers and operators; and enable faster decision-making. The three new segments will continue to be supported by the company's One Supply Chain team and corporate functions.

We are a much different company today than we were even a decade ago. Since the acquisition of SKIPPY in 2013, we have shifted to becoming a global branded food company with a food forward mentality and a growing set of leading brands across channels. This shift has involved a series of intentional and strategic actions,

including numerous strategic acquisitions focused on snacking and entertaining, growing our branded leadership positions in retail and foodservice and expanding our geographic footprint.

It includes regular evaluations of the portfolio, which in some cases led to divestitures of businesses where we identified a better long-term owner. It includes a rightsizing of our pork supply chain, including the divestiture of two hog harvest facilities and the entry into long-term pork supply agreements. It includes the creation of One Supply Chain, which centralized operations, logistics and sourcing decisions to drive the efficiencies for the total company. The modernization of our technology and e-commerce capabilities, including Project Orion and the creation of the digital experience group, and most recently, the transformational efforts at Jennie-O Turkey Store.

This next step, a new operating model is a culmination of these recent strategic actions. As part of the Go Forward initiative, we will be [indiscernible] (00:13:13) the important work we've been doing to transform the Jennie-O Turkey Store segment. As we said, when we announced the transformational efforts, turkey will continue to play an important role in our company and will contribute to growth in both Retail and Foodservice. We remain on track to integrate all business functions, combine the Jennie-O Turkey Store supply chain into the broader Hormel Foods One Supply Chain and drive SG&A cost synergies of approximately \$20 million to \$30 million annually by fiscal 2023.

Our successful transition to the new strategic operating model is dependent on strong leadership and execution from our teams. As previously disclosed, Deanna Brady, Mark Ourada and Swen Neufeldt will be leading the Retail, Foodservice and International segments, respectively. Each of these leaders has over 25 years of experience with the company and reputations for delivering results. Under their leadership, we expect to drive sustainable growth in line with our long-term growth goals of 2% to 3% top line growth and 5% to 7% bottom line growth. There has been a tremendous amount of what we've done on this initiative and more work to do in the coming months as we create the Hormel Foods of the future.

We will provide more information on Go Forward next week at the Barclays Global Consumer Staple (sic) [Staples] (00:15:01) Conference. We will also be releasing recast financial information during the first quarter of fiscal 2023 to aid in comparability to historical financial data.

Earlier this week, we released our 2021 Global Impact Report, which details how we are advancing corporate responsibility, ESG, and Our Food Journey at Hormel Foods. This is the 16th year we have published a report of this kind. Thanks to the incredible work and dedication of our team members, partners and suppliers, Hormel Foods is making a difference. We remain committed to our mission to be one of the top corporate citizens in the world and encourage you to review the report and the progress we have made to advance efforts through our 20 By 30 Challenge.

Our business remains healthy even as we continue to navigate some of the most difficult operating conditions in the company's 130-year history. Our revised full year guidance reflects both the continued top line strength we expect to see across our business and escalated cost pressures which are impacting the back half of the year.

For the full year, we are increasing our net sales expectations to \$12.2 billion to \$12.8 billion, and we are lowering our diluted earnings per share guidance range to \$1.78 to \$1.85 per share. There are two key takeaways from our guidance revision. One, we expect top line strength across our businesses to continue as our portfolio is well positioned for the current macroeconomic climate. And two, an escalation in certain operational, logistical and inflationary costs, which began impacting results in the third quarter has lowered our earnings expectations for the back half of the year. However, we believe the majority of these cost pressures to be transient in nature and to subside over time.

First, from a top line perspective, momentum remains very strong. We are confident in our ability to exceed our previous sales guidance due to strong demand for our foodservice and center store grocery brands, higher turkey markets and the pricing actions we have taken across the portfolio. Our long-term strategy to meet consumers where they want to eat, with a broad portfolio of products, has been a key differentiator in the current environment.

Second, we expect to absorb incremental costs in the fourth quarter related to certain operational, logistical and inflationary headwinds similar to what we experienced in the third quarter. In terms of magnitude, we view each of these cost buckets similarly. Starting with operational costs. We have made progress across our supply chain over the past year as a recovery in staffing levels has contributed to higher production volumes, inventories and fill rates. As we said last quarter, inefficiencies related to new team members and turnover have impacted operations leading to higher costs. We continued to see this pressure in the third quarter and do not expect meaningful improvement for the balance of the year. We are also experiencing higher-than-expected freight and warehousing costs both domestically and for our international business.

Freight rates have moderated recently, but this benefit has been more than offset by elevated fuel surcharges and significantly higher warehousing costs. Protein prices on key inputs have remained elevated compared to our expectations and historical averages. While we have mechanisms in place to manage the impact of elevated and volatile protein costs, markets have generally sustained higher price levels for longer than we anticipated in our previous outlook. We believe these cost pressures are transient and likely to subside over the coming quarters.

We fully expect our One Supply Chain team to continue to improve over time as our teams effectively onboard, train and retain our new team members, while striving to provide a best-in-class workplace experience. This is in addition to the investments we are making in automation and supply chain optimization. We also expect to benefit from the work the team has been doing to control freight expenses and capture the benefits from our recently expanded logistics network.

Finally, we are starting to see relief across key input cost markets that are better aligned to our expectations, which should present the opportunity for margin expansion in the coming quarters. The revision to guidance for the year is disappointing, but we will continue to manage the business for the long-term as we navigate these difficult business conditions, leveraging our balanced business model and experienced management team.

As I look beyond the fourth quarter, I have a high level of optimism regarding our future. We expect our brands to continue to perform well and plan to introduce an exciting slate of innovation in 2023. We anticipate improvements in our supply chain and the industry-wide supply chain as the broader markets stabilize.

We expect turkey supply to normalize, allowing our teams to continue their work to create a demand-oriented and optimized turkey portfolio. We fully expect our International business to be a significant growth driver for the company and to benefit from the investments we have made during the year, including the new Asia Pacific Innovation Center. And once implemented, our new strategic operating model will better align the businesses to the needs of our customers, consumers and operators to drive sustainable long-term growth. For all of these reasons and from the inspired work of our 20,000 team members around the world, I could not be more excited for the future of our company.

At this time, I will turn the call over to Jacinth Smiley to discuss financial information relating to the quarter and provide more color on key drivers to the outlook.

Jacinth C. Smiley

Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

Thank you, Jim. Good morning, everyone.

Record third quarter sales were \$3 billion. Net sales and organic net sales increased 6% and 3%, respectively, compared to last year. Volume for the quarter was 1.1 billion pounds, down 9% compared to last year. Organic volume declined 11%. These declines were in line with our expectations and are attributable to our effort to rationalize lower-margin commodity pork volume and lower turkey sales as a result of HPAI. These volume declines generally [ph] hit (00:23:23) strong underlying growth for many of the value-added businesses.

Gross profit increased to \$83 million compared to last year, a 20% increase. Gross profit margin was 16.7% compared to 14.8% last year. Improvement was driven primarily by strength in Jennie-O Turkey Store and Refrigerated Foods, in addition to strategic pricing actions to help offset inflationary pressures.

SG&A expenses declined 2% in the third quarter, as we lapped the Planters acquisition related expenses last year. SG&A as a percentage of sales for the third quarter decreased to 7.3% from 7.9% last year. We continued to generate strong sales and demonstrate disciplined cost management.

We again increased support for our leading brands. For the quarter, advertising expense increased 21% or approximately \$0.01 per share. Advertising expenses have increased 29% year-to-date.

Operating income increased 40% to \$291 million. On a comparable basis, which removes the impact of Planters onetime costs last year, adjusted operating income increased 17%. Operating margin for the quarter was 9.6% compared to 7.2% last year. Adjusted operating margin was 8.7% last year.

The effective tax rate was 24.5% for the quarter, up from 13.3% for the same period last year. Last year's rate reflected the benefit from a large volume of stock option exercises and onetime foreign tax benefit. Our effective tax rate guidance range of 20.5% to 22.5% remains unchanged.

For the quarter, diluted earnings per share of \$0.40 represented a 25% increase compared to last year. On a comparable basis, adjusted diluted earnings per share increased 3%. The company continued to generate consistent and strong cash flow. Operating cash flow for the third quarter increased 143% to \$186 million and operating cash flow through the first three quarters increased 74% to \$763 million.

We paid our 376th consecutive quarterly dividend effective August 15 at an annual rate of \$1.04 per share. This completes the 94th consecutive year of uninterrupted dividend payments to our shareholders.

Capital expenditures in the third quarter were \$61 million, compared to \$54 million last year. The fiscal 2022 target for capital expenditures is unchanged at \$310 million. We are benefiting from new production capacity we have added to our system over the past year and remain on track to open new capacity for SPAM in the first half of fiscal 2023.

Remaining investment-grade is a top priority for the company. Since acquiring Planters business last year, we have grown our cash position and EBITDA. On a net basis, we are now well within the stated goal of 1.5 to 2 times EBITDA by 2023.

Turning to our segment results for the quarter. Refrigerated Foods volume declined 18% and organic volume decreased 19% compared to last year. As referenced earlier, this anticipated decline in volume was primarily due

to lower commodity sales resulting from the company's new pork supply agreement. Sales increased 2% and organic sales increased 1%. Retail products such as Applegate natural and organic meats, Hormel Gatherings party trays, Hormel Natural Choice sliced meats, Hormel Square Table entree and Lloyd's barbecue grew volume and sales for the quarter, while the foodservice businesses delivered another excellent quarter. Refrigerated Foods segment profit increased 16% and driven by strong results from the value-added businesses, more than offsetting higher operational and logistics costs and lower commodity profitability.

Grocery Products volume increased 15% and sales increased 25%, led by strong demand across the nut butters, Mexican and simple meals portfolio and the addition of the Planters business. Organic volume increased 8% and organic sales increased 13%. Organic sales gains were led by products such as SKIPPY spreads, WHOLLY Guacamole, Hormel chili, Dinty Moore beef stew and Mary Kitchen hash. Segment profit declined 5% due to the impact from continued inflationary pressures and lower results from MegaMex.

Jennie-O Turkey Store delivered another outstanding quarter despite challenges related to HPAI. Volume and sales declines were less than expected and segment profit increased by more than \$30 million due to higher commodity prices and foodservice sales.

For the International & Other segment, volume was down 11% and organic volume declined 12%. Net sales declined 5% and organic sales fell 6%. Higher global sales of SPAM luncheon meat and improved results in Brazil did not overcome an overall decline in export sales and lower sales in China. Export volumes declined because of current export logistics challenge and lower commodity sales due to the company's new pork supply agreement. Sales in China was negatively affected by COVID-related restrictions and temporary plant shutdown. Segment profit declined 9% as growth in China did not offset the impact of lower export sales.

We have revised our full year fiscal 2022 sales and earnings guidance ranges. Consolidated net sales are expected to exceed our previous expectations benefiting from continued top line strength and pricing actions implemented across the Grocery Products portfolio at the start of the quarter. We project elasticities to remain below historical levels.

From a segment perspective, we anticipate profit growth from the Jennie-O Turkey Store and International & Other segment and anticipate declines for Refrigerated Foods and Grocery Products. As a reminder, all segments benefited from an additional week of sales in the fourth quarter of fiscal 2021.

Jennie-O Turkey Store remains on pace to exceed profit expectations for the year with significant profit growth in the fourth quarter. Sales volumes are projected to decline approximately 30% in the fourth quarter due to continued supply gaps in its vertically integrated supply chain and whole bird sales pulled forward into the third quarter. Further, with the positive cases identified earlier this week in our supply chain, we expect the impact from HPAI to reduce production volume in our turkey facilities through at least the end of the first quarter of fiscal year 2023.

The International & Other segment anticipates growth in the fourth quarter, driven by branded exports and improved profitability in China. Persistent shipping interruptions pose a risk to export sales and profit growth while additional COVID-related restrictions in China could pressure in-country results.

Refrigerated Foods expect continued strength in the foodservice businesses and strong demand for its retail products. Profits will be pressured by higher raw material and operational and logistics costs.

Lastly, Grocery Products expect improved results sequentially due to strong demand across the business and from pricing actions effective at the beginning of the fourth quarter. As Jim detailed, we continue to battle extreme input cost volatility and inflation during the third quarter and expect this to continue for the balance of the year.

Our previous outlook assumed key protein markets to move seasonally lower into the fourth quarter. Given that prices on key inputs remained elevated for the majority of August, we are managing through higher-than-expected inventory costs to begin the quarter.

We have seen some relief in these key markets over the past week which, if sustained, would benefit margins in the back half of the fourth quarter. Lower industry-wide turkey supplies are expected to keep prices higher near term. Breast meat prices set a record in the third quarter and have yet to moderate. Our team has done an exceptional job managing through disruptions caused by HPAI.

We continue to see increased hiring and applicant flow at our production facilities. Inefficiencies and elevated production costs related to newer team members turnover, absenteeism and overtime, have affected operations but should ease over time. Investments in value-added capacity are paying off strategically, including our pepperoni expansion in Omaha, new bacon lines at the Austin facility and the addition of co-manufacturing partners to support multiple product lines. We expect freight and warehousing costs for the domestic and international businesses to remain elevated. Our One Supply Chain team is actively looking for ways to drive efficiencies and control costs.

In closing, I am excited for the next step in our evolution as a global branded food company, the Go Forward initiative. This will create greater focus on our six strategic priorities, better align our business to the needs of our customers, consumers and operators and position us well to drive sustainable long-term growth and shareholder value.

At this time, I'll turn the call over to the operator for the question-and-answer portion of the call.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question today comes from Rupesh Parikh from Oppenheimer. Please go ahead with your question.

Rupesh Parikh

Analyst, Oppenheimer & Co., Inc.

Q

Good morning. Thanks for taking my question. So I want to start with a longer-term question, it may – I'm guessing this may have to wait until next week. But with your Go Forward initiative, which segments do you think will see the greatest impact from the structure change?

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. Good morning, Rupesh. I mean – so obviously, the biggest impact is going to happen in our Retail segment. And that's really the segment that – we're excited about all of them, but as we think about the opportunities for us to really accelerate progress on our six strategic priorities, that's the one that's going to have the biggest impact. So really being able to align the operating model with the strategic initiative in a bigger way than we ever have before is really going to be exciting. Foodservice will have some impact, as we move our – some of our affiliated business in there and then also move the Jennie-O foodservice business in there, it will strengthen us in certain channels or segments like K-12. International will be the least impacted of all the three. So really Retail, then Foodservice and then International.

Rupesh Parikh

Analyst, Oppenheimer & Co., Inc.

Q

Okay. Great. And then maybe one additional question. I'm not sure – same thing, I'm not sure if you guys can comment onto it. But if you look towards next year, like any early puts and takes on the operating margin line? I'm just trying to get a sense just given all the moving parts with your Jennie-O, some of the cost pressures whether you think you can actually expand operating margins versus your current guidance for this year?

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. I mean, it's early to look into 2023. I mean, as we're thinking about it, so far, we expect that our brands will continue to perform well in face of pricing. We talked about some of the innovation that we'll be able to bring to the marketplace as supply chain improves. We do expect to see some supply chain improvement. We talked about some of the operational challenges that we've had with new labor turnover, some variances that we hadn't planned for. We know that we've got to get better on that side. So there's certainly going to be opportunities for us in 2023, also recovery in our International segment as we think about maybe lockdowns not being as frequent in China, exports being able to pick up. And then we do expect benefit from our Go Forward initiative as we think about how we can really accelerate the progress on our six priorities.

Rupesh Parikh

Analyst, Oppenheimer & Co., Inc.

Q

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

Operator: And our next question comes from Ben Theurer from Barclays. Please go ahead with your question.

Benjamin M. Theurer

Analyst, Barclays Corporate & Investment Bank

Good morning, and thanks for taking my question. I actually wanted to elaborate a little bit, and you alluded to it on the sensitivities. So I wanted to understand if you could share a few more details and between the volume performance versus the pricing performance, because it really feels pricing was a big driver during the quarter. Volume down, I get it in Refrigerated just because of like the change in the business model. But then, obviously, if we put it all together, it feels like volume was a little more under pressure. Would you assign this to certain elasticities because of the pricing actions? And how do you think you're going to be able to recover some of the volume over time if we look into fiscal 2023?

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Yeah. As we think about the business spend, clearly, really pleased with the overall health of the business and the performance in the quarter. You touched on it. We knew we were going to have some Refrigerated volume declines. Jennie-O clearly had volume declines tied to HPAI. Our Grocery Products business had strong volume growth. As you dig into some of the specific brands and categories, I would say probably the most softness we had was in the area of bacon, and a lot of that would be tied to the belly market and some of the escalated pricing that we saw throughout the quarter.

Benjamin M. Theurer

Analyst, Barclays Corporate & Investment Bank

Okay. Perfect. And then just a quick follow-up, if I may, on the new operating model, and obviously, we can explore this more in detail next week. But if we kind of – and you said it about the importance of it, and we've seen, obviously, Retail performing year-to-date relatively strong, up 12%, but Foodservice even more. Can you give us a little bit of a preview in terms of like the distribution of these segments in terms of relevance? It clearly feels like Retail is like – most likely more than 50% of it, and that's why this has the most focus – where you're most excited about, correct?

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Yeah. I mean, obviously, Retail will be roughly about 60%. We've talked about Foodservice in total being just over 30%, and International high-single digit. So, we're excited about all of them. And really, when we talk about Retail being the most impacted, it's because we are [ph] ringing (00:42:48) together our Retail, Refrigerated, our Grocery Products unit, our Jennie-O retail. So, you do have the most change occurring there. But we also have the most opportunity to really generate the alignment that we need. And so a perfect example of that, I believe, is when we've talked about entertaining and snacking in a bigger way, being a strategic priority for our organization.

Historically, we've had pepperoni in refrigerated retail. We've had our Gatherings party trays in our deli organization. We've had – of course, now Planters in our Grocery Products organization. And now the ability to bring those together under one pillar and really talk to customers and consumers in a way that we haven't before really excites us for the future.

Benjamin M. Theurer

Analyst, Barclays Corporate & Investment Bank

Perfect...

Jacinth C. Smiley

Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

A

Yeah. And just a quick add there, Ben. As – Jim described all of that from a strategic standpoint, if you think about how we go to market as well, what this model actually does, it really just bolster how we go to market as a company and just bringing that one Hormel to bear, and that's truly going to be a strategic advantage for us.

Benjamin M. Theurer

Analyst, Barclays Corporate & Investment Bank

Q

Perfect. Thank you.

Operator: Our next question comes from Ken Zaslow from Bank of Montreal. Please go ahead with your question.

Kenneth B. Zaslow

Analyst, BMO Capital Markets Corp.

Q

Hey. Good morning, guys.

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Good morning.

Kenneth B. Zaslow

Analyst, BMO Capital Markets Corp.

Q

My first question is on SKIPPY. With all the volume that was created where did the profit go to? It seems like there would be a greater association with the increased opportunity created there. Did you guys have co-packers? Was there shortfall of supply? It just seems like there was a lot of top line but didn't really translate to the bottom line.

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. Good morning, Ken. There definitely was a benefit from SKIPPY in the quarter. Really, as we talked about it with the escalation in costs, it's really across the board. We've talked about the operational inefficiencies. So, even though in aggregate we're at a good place with our total number of employees. Those employees are younger, less experienced and we are seeing that turnover.

And then, we talked about some of the input costs, so continued escalation for – across the supply chain, and then specifically towards the end of the quarter as we saw some of the raw materials run up. And so that really is what created that erosion of the benefit from SKIPPY. But we definitely did see a benefit in the quarter.

Kenneth B. Zaslow

Analyst, BMO Capital Markets Corp.

Q

Okay. And then my second question is – is when you think about your long-term guidance, look – look, the last couple of years, you really haven't been within that. What is it that changes? And is 2023, 2024 back into that long-term guidance range? Or is it going to still take time to reestablish your growth algorithm on a more consistent basis? How do you think about that?

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. I mean, we're very positive about the business. We know that the brands are strong, the business is strong. We continue to fight the escalation in costs. We know that we have work to do. On the operational front, we talked about our need to really capture the synergies and the value in our expanded logistics model. We've taken appropriate pricing. We are starting to see some relief on input costs here in the fourth quarter. That should translate into 2023. We've got back to pricing, the full year impact of some of the pricing that we've put in place.

I think for us it is a better internal supply chain performance that will be a key driver for us. We do expect brands to continue to perform well. And so we're confident in our ability to deliver our long-term growth algorithm. We do have some work to do, but we're confident that we can get it done.

Jacinth C. Smiley

Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

A

Yeah. And just to add to that, we also are currently underway executing the automation and really getting – optimizing in different fronts from an operation standpoint. So that should certainly add to us being successful at executing on our long-term goals as well.

Kenneth B. Zaslou

Analyst, BMO Capital Markets Corp.

Q

Okay. Thank you.

Operator: Our next question comes from Tom Palmer from JPMorgan. Please go ahead with your question.

Thomas Palmer

Analyst, JPMorgan Securities LLC

Q

Good morning, and thanks for the question. I wanted to ask on the Grocery Products side. Is the pricing that you've taken enough to offset the inflation that you're facing? Do you need additional rounds of pricing to address this still mounting inflation? Or maybe given your view that costs ease or added rounds of pricing maybe not planned at this point? Just trying to understand that dynamic and what kind of causes the inflection in Grocery.

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. Thanks, Tom. Obviously, we're pleased with the strong organic top line growth, the strong demand for the Grocery Products portfolio. And you described the cost and pricing scenario very well. With the relief that we've recently seen from some of the key inputs, we don't believe that additional pricing is going to be necessary, that the pricing that is now going into effect in Q4 will be sufficient. But we did have pressure at the end of Q3 and in the early part of Q4 because of those elevated markets.

Thomas Palmer

Analyst, JPMorgan Securities LLC

Q

Understood. Thank you. And then maybe to ask another question on the 4Q outlook. So it sounds like the third quarter overall was pretty consistent with what you had talked about a quarter ago. So it would seem that essentially the guidance cut was mainly for reduced expectations around the fourth quarter. From the comments today it sounds like the kind of greatest incremental pressure was on Refrigerated Foods. Is that accurate? And

then to what extent do these easing costs that you mentioned in the last week, are they factored into the guidance range?

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. So it's a couple of things. The Refrigerated Foods group is impacted by the elevated markets as well. And as we think about the fourth quarter, there's always going to be the puts and takes. We've obviously seen a reoccurrence of HPAI [ph] with – with jobs (00:50:20). And so really, watching to see how that plays out throughout the quarter from a upside potential, or is there some risk, really understanding what will happen with the consumer with this last round – most recent round of GP pricing. And then the other part that is – is on our radar is although we've seen this market relief, we have also seen just an incredible amount of market volatility throughout the year. And so we've seen significant moves up and down. And so while we're in a better position today, we'll be watching that closely because we know how quickly that can change.

Thomas Palmer

Analyst, JPMorgan Securities LLC

Q

Okay. Thank you.

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah.

Operator: Our next question comes from Robert Moskow from Credit Suisse. Please go ahead with your question.

Robert Moskow

Analyst, Credit Suisse Securities (USA) LLC

Q

Hi. A couple of questions. In the Grocery division, I'm now forecasting, based on your guidance, I think a decline in profits for the year, about \$20 million, \$30 million. And that's despite having seven months incremental of the Planters acquisition. So, I guess, I'd like to know, is Planters weaker than you thought? I didn't hear you reiterate Planters is a double – accretion number today. Maybe that's just – it's still there. But – and if it's not that, what is it, is it – which of the other brands? And then I've a follow-up, please.

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. Rob, so a couple of things. Your assessment of the GP division is correct. That will be down for the full year. When we think about Planters, although we probably weren't as intentional, the sales of – we're on track for the sales guidance that we've provided in line with our \$1 billion guide, our earnings continue to be at the high end of that accretion model. And really for us, the long-term strategy is intact, right?

So as we think about this being an important part of our entertaining and snacking platform, the work that we're doing in C-stores, the business is still performing the way we want it. There's always opportunities within categories. But overall, the business is well in line with our expectation. And really what it is, it's the inflation that we've experienced in Grocery Products. And so we've had significant packaging inflation. We've taken incremental pricing along the way. This most recent round of pricing should be very positive and favorable as we head into 2023.

Robert Moskow

Analyst, Credit Suisse Securities (USA) LLC

Q

Okay. Maybe a follow-up then. When you talked about transitioning to One Supply Chain model, it sounded like a great idea, and it consolidated a lot of the information, consolidated a lot of the, I guess, the decision-making. And yet, here we are in a year where your warehousing costs are higher than you thought, your freight is, and you're having still lingering labor issues. And I guess I have to ask, did this transition – did it exacerbate any issues? Did it make any of these issues incrementally easier? Why don't the transition help prevent a lot of these situations?

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. No, great – great question, Rob. I mean – as I sit here, I can't imagine us having gone through what we've gone through over the last several years without having our One Supply Chain in place. Everything you described to have one purview of the supply chain has really helped us throughout COVID and some of these labor challenges. We're not alone in what's happening. You can go across industry and the conversation about turnover and these manufacturing variances, I mean, they're everywhere.

We have work to do. And so we do – we're getting people through the door. We're getting people hired. There's work to do in terms of training and retaining those people so that we do over time develop that experience. That is a problem today. That's not a One Supply Chain issue. That's a broad-based issue. And I think when we think about other challenges, we continue to see countless upstream challenges from our suppliers. So, industry-wide issues persist. And as I – I'll finish where I started in that I – I just can't imagine us having gone through what we went through the last several years without having our One Supply Chain in place.

Robert Moskow

Analyst, Credit Suisse Securities (USA) LLC

Q

Got it. Thank you.

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah.

Operator: Our next question comes from Michael Lavery from Piper Sandler. Please go ahead with your question.

Michael S. Lavery

Analyst, Piper Sandler & Co.

Q

Good morning. Thank you. I just wanted to come back to looking ahead a bit into fiscal 2023. And maybe specifically, can you give a sense of how much of your commodity exposure is already locked in or hedged and how that might compare to what's typical?

Jacinth C. Smiley

Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

A

So we are currently, for the moment for 2022, have hedged our grains at around 80% for the year, and we have already started hedging and have actually locked in our hedge for 2023, albeit at an elevated level, given where grain sits today. So that's, of course, another challenge, and we're not 100% hedged. So we still have a little bit of

exposure to the market and working through as we think about other areas as well, leaning into forward contracts where we can, where we are not able to really execute any hedges in those areas.

Michael S. Lavery

Analyst, Piper Sandler & Co.

Q

So for this time of the year relative to the following fiscal year, are you less or more hedged than normal or covered...

[indiscernible] (00:57:22)

Jacinth C. Smiley

Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

A

We're consistent with where we're normally sitting at this stage.

Michael S. Lavery

Analyst, Piper Sandler & Co.

Q

Okay. And just back to Jennie-O, you touched on the volume impact that will run at least through 1Q 2023. Can you give a sense of the magnitude there? Obviously, third and fourth quarter this year, at least what you reported and expect is pretty different in terms of the magnitude of the impact on volume. What would it look like going forward?

Jacinth C. Smiley

Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

A

So going forward, I think tough – it depends on what happens with HPAI, certainly. I mean, for this year – for the third quarter, our impact was about 20% less volume going into the fourth, will be off 30% volume for the fourth quarter. And our expectation is as we go into the first quarter of next year, if nothing else happened from an HPAI standpoint, we should be rebuilding our supply there and be in a good spot.

Michael S. Lavery

Analyst, Piper Sandler & Co.

Q

So I think you had mentioned though, just a recent case or something that would add some pressure on 1Q. Would the volume pressure there be more like – more similar to 4Q? Or do you expect it to be improving?

Jacinth C. Smiley

Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

A

No – yeah. We don't expect that volume pressure. So, we actually – and you're exactly right, I mean we've had a couple situations here within the last few days with – but these were really young birds. And so, it is an impact that doesn't impact Q4 at all and actually pushes into the first quarter of next year, but really will be immaterial to the quarter.

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. So Michael, if we stay where we are today, we don't expect a material impact in Q1. As this always is, it's a developing situation. And so we'll be watching it closely. But at this point, it's really too early to tell what the impact for Q1 would be.

Michael S. Lavery

Analyst, Piper Sandler & Co.

Okay, great. Thanks.

Q

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Yeah.

A

Operator: Our next question comes from Ben Bienvenu from Stephens. Please go ahead with your question.

Jim Salera

Analyst, Stephens

Hey, guys. Jim Salera on for Ben. I wanted to drill down a little bit more on some of the labor challenges. Is it that you're seeing more acute labor markets in the areas that you operate your facilities? And maybe as the economy weakens, that loosens up a little bit and gives you an opportunity to hire more people? Or is it just pure wage issue or flexibility? What are some of the specific challenges that are preventing getting those under control?

Q

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Yeah. So the issue of hiring, getting people through the door is not a problem, right? So we're getting people hired. What we are seeing is that they're not staying, that there is higher than normal turnover, there's significant absenteeism. And we do think that's partly driven by the labor market that we've had, the ability to find many jobs elsewhere.

A

So to your point, is it – as the labor market potentially tightens, does that lead to lower turnover, the ability to keep people longer and then build that experience and that training? Absolutely. So it's not getting people hired, it's not a labor rate, it is just keeping the turnover down so that we can build the experience within our facility.

Jim Salera

Analyst, Stephens

Okay. And as you expand automation through your plants, what's the timeframe of how long it will take to get those equipment – get that equipment in the plant and up and running to supplement maybe some of the necessity for those higher turn labor positions?

Q

Jacinth C. Smiley

Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

Yeah. So I mean that's going to vary, right? So we'll continue to always evolve and look for opportunities to take costs out of the plant. So there isn't really any point in time I'd say that we would stop doing that. So it really is a continuing improvement in our mind.

A

Jim Salera

Analyst, Stephens

Okay. And then if I could sneak in one quick question on HPAI. Yeah, I know there's been a couple of cases pop up here more recently despite the weather getting warmer. Do you guys have anything in maybe your

Q

contingency plan? Or if anything you could do to prepare for the possibility of this popping back up as the year progresses?

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. I mean, we've obviously done a lot of work since – you go back to 2015, the biosecurity efforts, the investments that we've made on our farms have been substantial. So we've worked really hard. But clearly, this is still an issue.

To your point, the new development is historically warm weather or heat has really [indiscernible] (01:03:00) us down, but you're starting to see cases in California where temperatures are higher. And then just making sure, again, that we've got the continued emphasis and the continued focus on training with our team members that we keep this top of mind, so that – that we are able to minimize the effect.

Jim Salera

Analyst, Stephens

Q

Okay. Great. Thanks, guys. I'll pass it on.

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah.

Operator: Our next question comes from Peter Galbo from Bank of America. Please go ahead with your question.

Peter T. Galbo

Analyst, Bank of America

Q

Hey, guys. Good morning. I'll keep it pretty quick. Jim, just in the context of going back to the new operating model, I guess – I think you're going to stand up a brand – a new brand center. Just curious, like are there incremental costs or restructuring actions that will come in with the re-segmentation and I guess, streamlining everything. I know, you've talked about some of the synergies you expect to get, but just any of the upfront costs that we should kind of think about?

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. Nothing really significant or material, Peter. We're moving some people around in chairs, focusing their expertise in areas that we need some extra emphasis. So as we think about Brand Fuel, which is that center of excellence, to really support all of our strategic pillars and brands in a bigger way. That'll consist of our digital experience group, which has been a huge benefit to our organization. We'll continue to strengthen that area, making sure that our insights group is being fully utilized across the entire organization. So making a few investments there, continued our good work on innovation, and having that even more ingrained with the brand and the strategic pillars.

So nothing really material as much as it is moving some people in chairs and then making sure, of course, that we've got all the right financial planning and analysis to support the business in a bigger way, but really nothing from a cost perspective that we're thinking about.

Jacinth C. Smiley

Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

Yeah...

A

Peter T. Galbo

Analyst, Bank of America

Okay...

Q

[indiscernible] (01:05:26)

Jacinth C. Smiley

Executive Vice President & Chief Financial Officer, Hormel Foods Corp.

..and the other – yeah, the other piece I'll add there, I mean, really fundamentally, what it has done for us or what it will do is just bring the synergistic brain power into one place to be able to support the business and just take away some of the silos in which we're working today and also bringing jobs as well into play as we integrate them into the organization as part of the transformation.

A

Peter T. Galbo

Analyst, Bank of America

Got it. Okay. No, that's helpful. And then, Jim, I just want to go back to your comments around what I'm assuming mostly pertain to the hog market. Obviously, you've seen a little bit of relief here. Your commentary suggested over time you're expecting some relief. But just as we think out 12 to 18 months, just what are you tracking, what are you seeing that's suggesting you – maybe that you'll get some relief on the protein side? Just given some of the USDA forecasts or maybe for less protein availability next year as opposed to more, and I would think that would keep prices higher. But just curious if there's anything that you're seeing that we should be aware of.

Q

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Yeah. I think the biggest thing there, Peter, is the volatility that we continue to see. So in terms of the absolute supply, I mean, our view is consistent with what everybody else is seeing. We're obviously going to be making some forecasts that are probably tied more to slightly higher than historical averages. But really, the difference in all of this is that, that volatility or when some of these markets are staying elevated longer than they historically have, like we've just seen here at the end of Q3 and for us the first period of Q4. That's where we really start to experience some of that compression. So when you've got the elevation that's higher longer and then some of the volatility that has been persistent throughout the year.

A

Operator: And our next question comes from Adam Samuelson from Goldman Sachs. Please go ahead with your question.

Adam Samuelson

Analyst, Goldman Sachs & Co. LLC

Yes. Thanks. Good morning. A lot of grounds have been covered. But hoping maybe kind of get your view on trade and promotional spending here. I mean, you talked about the specific advertising dollars that – in SG&A that are up, but the trade spend that would be kind of above the revenue line. Any color on what that looks like today relative to maybe pre-COVID? And do you think that's going to have to get a bigger lever to pull over the next 12

Q

to 18 months to combat maybe more risk in consumer price elasticity and retailers that might be a bit more wary of pricing actions?

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. I think, Adam, as supply continues to improve – and we talked about still having a number of categories where demand is outstripping supply, but as supply continues to improve, we do expect that to be a lever that we've – historically, we've always used it. We'll continue to use that in conjunction with the advertising dollars that we need to build the brand equity and build that connection with consumer. So yeah, we do expect to see that to continue to be an integral part of our business going forward. And as we think about our updated operating model and we start to bring these retail businesses together, that's also going to be a benefit for us as we'll have, again, a bigger purview of all the retail businesses in terms of how we're interacting with customers and consumers.

Adam Samuelson

Analyst, Goldman Sachs & Co. LLC

Q

Okay. And then just quickly, in foodservice, any color you could provide maybe by some of the different channels or verticals within foodservice between quick service – for institutional, you guys have a pretty broad kind of customer set there. And just any color on differences in trends between them would be helpful.

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. Not at this point, Adam. I mean, we're seeing continued strength across all of the different channels where we compete. And I would say that a big driver of that, we've talked about some of our labor issues. So many foodservice operators are facing those same labor issues. So they're forced to think differently about how they're going to be able to provide products. And we talked a lot about the value-added offerings that we have in our foodservice portfolio really being able to help those operators move the labor that they do have from back of the house to front of the house, and we are – we continue to see that play out. We have seen a strong back-to-school season, not only with our Jennie-O K-12 business, but with the work that the Hormel side does on the colleges and universities. So again, really, really strong broad-based foodservice business.

Adam Samuelson

Analyst, Goldman Sachs & Co. LLC

Q

Okay. I appreciate that color. Thank you.

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah.

Operator: And ladies and gentlemen, with that, we'll be concluding today's question-and-answer session. At this time, I'd like to turn the floor back over to Jim Snee for any closing remarks.

James P. Snee

Chairman, President & Chief Executive Officer, Hormel Foods Corp.

Yes. Thank you. I want to thank all of you for joining us today. As we've talked about this morning, our business remains incredibly healthy even as we continue to navigate some of the most difficult operating conditions in our company's 130-year history. Our team is focused on a strong finish to 2022, but we're also incredibly excited

about our future with the implementation of our Go Forward initiative to update and better align our operating model against our strategic initiatives. This is a positive and exciting time for Hormel Foods. Have a safe and enjoyable Labor Day weekend.

Operator: And ladies and gentlemen, with that, we'll conclude today's conference call and presentation. We do thank you for joining today's conference. You may now disconnect your lines.

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