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Hormel Foods Corp. (HRL)

Q4 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, and welcome to the Hormel Foods Fourth Quarter 202 Earnings 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.

I would now like to turn the conference over to David Dahlstrom, Director of Investor Relations. Please go ahead, sir.

David W. Dahlstrom
Director-Investor Relations

Good morning. Welcome to the Hormel Foods Conference call for the fourth quarter of fiscal 2022. We released our results this morning before the market opened around 6:30 a.m. 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 fourth quarter and full year results and update on the company's go-forward initiative and a perspective on fiscal 2023. Jacinth will provide detailed financial results and further commentary on the fiscal 2023 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 9562037. 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 on 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 net sales and net debt to EBITDA. Discussion on non-GAAP information is detailed in our press release and fourth quarter earnings supplement, which can be accessed from our corporate website and is also located on our investor website, investor.hormelfoods.com.

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I will now turn the call over to Jim Snee.

James P. Snee

Chairman, President and Chief Executive Officer

Thank you, David. Good morning, everyone. Fiscal 2022 was a return to growth for our business as we delivered record sales and double-digit earnings growth compared to last year. Fiscal 2022 marked the third consecutive year of record sales and the second most profitable year in our company's 131-year history. In addition to achieving strong year-over-year growth, our team made considerable progress on our six strategic priorities.

First, we continued our efforts to protect and grow our core brands. Sales in our retail channel increased 7% in fiscal 2022, led by brands such as SPAM, SKIPPY, Hormel Natural Choice, Dinty Moore, Hormel Square Table entree, and Mary Kitchen. Of note, the SPAM family of products achieved its eighth consecutive year of record growth.

Second, we made progress amplifying our presence in snacking and entertaining. We delivered excellent growth on the Columbus and Hormel Gatherings brand, and we have successfully integrated the Planters business. We have a powerhouse of brands with the goal of becoming the leading solutions provider in the snacking and entertainment space.

Third, we saw growth from our ethnic and food forward portfolios. Both our MegaMex joint venture and Applegate business achieved sales milestones this fiscal year, driving growth behind the WHOLLY, Herdez and Applegate brands, respectively. These businesses are well positioned in the marketplace due to their strong and reputable brands, on-trend innovation and loyal consumer bases.

Fourth, we continue to expand our leadership position in food service. Sales in the foodservice channel grew 20% compared to last year, as operators again turn to our items to help solve for labor pressures and to diversify menu offerings.

We drove excellent growth in this critically important channel, highlighted by brands such as Bacon 1, Austin Blues, Hormel Fire Braised and Café H. Our foodservice portfolio and direct selling organization remain key differentiators and growth catalysts for the company.

Fifth, we invested into our international business, as we look to aggressively develop our global presence. In fiscal 2022, we commissioned a state-of-the-art innovation center, supporting the Asia Pacific region and approved another capacity investment to support our growth in China. Our international business is expected to be a significant growth driver for the company.

And finally, we continue to transform our company. We made noteworthy progress on our transformational efforts at Jennie-O Turkey Store and lay the groundwork for the next step in our evolution as a global branded food company, our go-forward initiative.

We also made considerable progress on our 20 By 30 Challenge. Some of the year's highlights included: matching 100% of our domestic energy use in fiscal 2022 with renewable sourcing; remaining on track to have an approved science-based target for the reduction of greenhouse gas emissions by 2023, becoming a major sponsor of up to 50,000 acre regenerative agriculture pilot project in Central and Southeast Minessota; announcing our commitment to create a food secure community program in Austin, Minnesota, with the additional goal of sharing the blueprint and findings globally.

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We are making a difference, thanks to the incredible work and dedication of our team members, partners and suppliers. Our team showed tremendous resolve to deliver growth in fiscal 2022. The team overcame broad-based inflationary pressures, supply chain disruptions, the impacts from highly pathogenic avian influenza, or HPAI, and numerous headwinds in our international business. I want to express my sincere gratitude to the team for their dedication, hard work and for demonstrating our results matter mentality again this past year.

In the fourth quarter, our team delivered diluted earnings per share comparable with record results last year and last year included an additional week of sales. These results further demonstrate that our brands remain healthy and the strategic investments we have made are enabling growth.

We achieved another quarter of organic sales growth led by our center store grocery portfolio and solid performances from our foodservice businesses. Segment profit growth was due to the Jennie-O Turkey Store segment as the team again managed Turkey supply effectively and maximized operational performance.

We also made progress across our supply chain to increase production capabilities and restore inventories on key product lines. Fill rates for retail, deli and foodservice items all improved compared to last year and the third quarter.

As we announced in August, we recently began transitioning our business to a new strategic operating model. As of October 31, we have moved to three operating segments: retail, foodservice and international.

Over the last month, we have been working to create a unified retail organization with scale, experience, expertise and passion to grow our almost $8 billion portfolio of brands. We are approaching customers differently, bringing together subject matter experts from across our businesses to find growth opportunities and execute strategies in the marketplace.

We are leading with a more food-forward mentality, thinking and acting differently in the ways we position our brands with consumers. This has created new opportunities that were not easily executed in our old model. And we are working with a newly created brand fuel team to ignite the potential of our products in store and on shelf.

And these early successes are not limited to our retail team. Our combined foodservice team will further leverage the scale of planters in the convenience store channel, while assuming full control of the company's foodservice Turkey business, including the Jennie-O brand.

Though we are only in the initial stages of the implementation, we are receiving positive responses from our customers and operators. Our immediate focus is to accelerate the execution of our six strategic priorities while continuing to meet the needs of our customers, consumers and operators.

Specific to the first quarter, our teams will be working to adopt the new organizational design, management structures and accountabilities. The teams will be working to continue the work to integrate Jennie-O Turkey Store into the company's one supply chain and new operating segments. And our teams will be working to stand up the brand fuel Center of Excellence, which will house enterprise-wide brand management expertise, e-commerce capabilities, insights-led innovation and analytical support to better enable data-driven decisions.

Earnings will be reported under this structure beginning with the release of fiscal 2023 first quarter results in early March. We will be supplying recast financial information for fiscal years 2021 and 2022 in February 2023.

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The deliberate and thoughtful steps we have taken thus far are all about better aligning our structure with our proven strategy to create the Hormel Foods of the future. We are excited for the additional collaboration, capabilities and value we will realize from this transition and remain confident in our ability to drive long-term sustainable growth.

Turning to our outlook. We expect to grow both sales and earnings in fiscal 2023. We enter fiscal 2023 well positioned for the current macroeconomic climate and expect top line growth from all three of our new segments: retail, foodservice and international. In retail, we expect demand for our center store grocery business to remain strong as consumers continue to seek products and brands that offer high value, versatility and convenience.

We expect growth from Planters and the rest of our snacking and entertaining businesses, including the Columbus and Gatherings brands. Planters will be rolling out meaningful innovation throughout the year to complement and expand on the new flavor varieties and packaging introduced in fiscal 2022. We expect to benefit from the investments we have made in additional Black Label bacon and Hormel Pepperoni capacity and are excited for the new SPAM capacity to be operational in the first half of the year.

And lastly, we expect a recovery in turkey volumes in the back half of the year, allowing our teams to continue to create a demand-oriented and optimized turkey portfolio. This is heavily dependent on any future impacts to the supply chain from HPAI. We expect that the pricing actions taken over the past few quarters should result in a benefit to net sales in fiscal 2023. However, we have also accounted for additional impacts from elasticities as these new pricing actions are adopted in the marketplace.

To help mitigate risk to our retail volumes, we plan to increase advertising and brand investment, make further progress on our efforts to continue to improve fill rates and return to full assortments across our leading platforms. We plan to deliver innovation across the portfolio. We'll leverage the capabilities of go forward, which include our well-established revenue growth management and digital experience teams, our combined direct selling organization and our newly created Brand Fuel team.

In Foodservice, we are expecting another year of growth from our solutions-based portfolio and direct selling team. We entered the year from a position of strength after two consecutive years of robust growth during the industry recovery. The consistent inroads our teams have made over time, including during previous economic slowdowns to diversify our presence in emerging and non-commercial channels will help us navigate through future market volatility and uncertainty.

Additionally, the team plans to leverage the Planters and Jennie-O brands to make further gains in the convenience and K-12 channels, respectively. Our international business had a challenging year in 2022, but we expect a strong return to growth in fiscal 2023. Demand for our products globally is robust, and our production capabilities and inventory levels are healthy to support this demand.

We believe that many of the export challenges we experienced this past year will gradually subside. Like many, we are currently monitoring the situation in China. We are actively engaged with our in-country management team and are prioritizing the health, safety and well-being of our team members. This team has been resilient in the face of numerous challenges and will continue to deliver growth with balance between retail and foodservice.

From an overall bottom line perspective, we anticipate earnings growth to be driven by our foodservice and international segments and improvements across the supply chain. We expect to operate in a volatile, complex and high-cost environment again in fiscal 2023, which is why we are increasingly focused on reducing costs and inefficiencies as part of our One Supply Chain initiative.

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We have a strong track record of consistently capturing approximately $75 million per year of supply chain savings through our continuous improvement programs. Though these efforts continued over the last three years, the benefits have been masked by pandemic-related impacts, labor shortages, industry-wide supply chain disruption and most recently, broad-based inflation. We will continue to identify and capture cost savings opportunities, find the efficiencies and drive unnecessary costs out of our system.

We fully expect that over time, these actions, in addition to the benefits of broader market stabilization will result in more normalized operating margins for our business. Taking all of these factors into account, we expect full year net sales of $12.6 billion to $12.9 billion and diluted earnings per share of $1.83 to $1.93 per share. We have continued to benefit from our balanced business model, which is not heavily dependent on any one channel, protein, input or product category.

We also have a dedicated well-respected, experienced and stable management team that has again proven their ability to navigate and grow our business in volatile market conditions. Our long-term strategy to meet consumers where they want to eat with a broad portfolio of trusted brands and products will continue to be a key differentiator for our business, helping to drive growth for our customers and operators.

At this time, I will turn the call over to Jacinth Smiley to discuss more detailed financial information and provide more color on key drivers to the fiscal 2023 outlook.

Jacinth C. Smiley

Executive Vice President & Chief Financial Officer

Thank you, Jim. Good morning, everyone. I want to start my remarks by congratulating Jim Snee. Jim was recently recognized as the 2022 Responsible CEO of the Year for transformative leadership by 3BL Media. During the award ceremony, Dave Armon, CEO of 3BL Media said and I quote, the world needs business leaders who are operating with their eyes wide open and using the power of their businesses to bring forward meaningful ESG programs and policies to operate in a transparent manner, end quote.

Jim truly embodies these characteristics. We at Hormel Foods are honored to witness firsthand Jim's leadership style and be part of the difference our company is making to inspire a change, lift communities and bring people together. Congratulations, Jim, on this well-deserved recognition.

The company achieved a record full year net sales of $12.5 billion, up 9% from a year ago. Net sales for the fourth quarter were $3.3 billion, a 5% decline from the prior year, which included an additional week. Organic net sales increased 2% for the fourth quarter. Operating income for the fourth quarter and the full year increased 3% and 17%, respectively, overcoming the additional week of sales last year.

Strong results from Jennie-O Turkey Store segment, higher foodservice sales, pricing actions to mitigate inflationary pressures and the inclusion of the Planters business were the primary drivers to earnings growth during the year. Fourth quarter diluted earnings per share of $0.51 was comparable to the record quarterly earnings set last year. Diluted earnings per share for the full year were $1.82, a 10% increase.

The company's actions to offset inflationary pressures were evident in the fourth quarter. Operating margin of 11.2% was significantly ahead of 9.6% in the third quarter. Operating margin for the year was 10.5%, an improvement versus operating margin of 9.9% last year.

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For the full year, SG&A as a percentage of sales fell to 7.1% from 7.5% last year. Advertising spend increased 14% compared to last year with higher investments seen across every segment. In fiscal 2023, we are again planning higher investments to support key brands, including Planters, SPAM, SKIPPY, Columbus, BLACK LABEL, Hormel Pepperoni and Jennie-O.

Net unallocated expenses in 2022 decreased due to Planters acquisition costs last year. In fiscal 2022, higher interest expense and investment losses on the Rabi Trust net of associated deferred compensation, negatively impacted earnings by approximately $0.05.

The effective tax rate for the year was 21.7%, compared to 19.3% last year. The effective tax range for fiscal 2023 is expected to be 21% to 23%. The company again generated strong and consistent cash flow with operating cash flow increasing 13%, compared to last year.

We generated more than $1 billion in cash from operations, allowing us to invest in future growth, return a record amount of cash to shareholders in the form of dividends, supporting ongoing business needs and increase our cash balance to nearly $1 billion.

We invested $279 million in capital projects in 2022. The company's target for capital expenditures in 2023 is $350 million, which includes investment in value-added capacity, technology, and automation to increase production and drive long-term savings and efficiencies.

As Jim mentioned earlier, we recently approved another significant expansion to our operations in China, which we expect to come in operation in fiscal 2024.

We returned a record amount of cash to shareholders in the form of dividends in 2022. We paid over $550 million in dividends during the year, including our 377th consecutive quarterly dividend, effective November 15. We announced a 6% increase in the dividend for fiscal 2023, marking the 57th consecutive year of dividend increases.

Our strong financial position also allows us to continue sharing our successes with our team members. For fiscal 2022, we will share approximately $20 million with the team, including our annual profit sharing for the 84th consecutive year. Remaining investment grade is a top priority for the company.

The company ended the year with $3.3 billion of debt. On a net basis, we're below our stated goal of 1.5 to two times EBITDA. Our first debt repayment related to the Planters acquisition is due June 2024 with a fixed rate of 65 basis points. Our total outstanding debt is fixed, with an average yield of 1.7%.

As Jim previously mentioned, we expect sales and earnings growth in fiscal 2023. I want to revisit some of the comments we made in our third quarter earnings call, in the context of our fourth quarter results and outlook for 2023.

Heading into the fourth quarter, we cited the impact of an escalation in certain operational, logistical and inflationary costs. Generally, these assumptions played out as expected, and we anticipate similar trends in fiscal 2023.

We made additional progress across the supply chain during the fourth quarter and are becoming more efficient and productive. Fill rates improved compared to last year and the third quarter.

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We continue to see increased applicant and hiring flow at our production facilities. Our focus is on onboarding and training new team members and creating a best-in-class experience throughout our operations. Freight and warehousing expenses remain elevated during the quarter. We saw signs of moderation in the domestic freight environment as truck availability improved, though higher diesel prices offset a portion of this benefit. Higher warehousing expenses were driven by a recovery in our inventory levels and industry-wide labor challenges.

In 2023, we expect some of this pressure to be offset by savings from the work the team has been doing to control freight expenses and expand our logistics network. Prices on key protein inputs generally declined during the quarter, except for port trim, higher priced inventory was a headwind in the quarter as we worked through inventory produced during the summer commodity peaks. Protein prices are expected to remain volatile in fiscal 2023.

Additionally, we expect packaging, energy and labor costs to remain elevated or increase in 2023 and for upstream challenges to persist. Actions by our One Supply Chain team will be key to managing and mitigating additional cost escalation in these areas.

Beginning in fiscal 2023, our Turkey business will primarily reside in the retail and foodservice segment. HPAI has reemerged this fall and this unprecedented event has affected our vertically integrated supply chain at about one-third of the magnitude of the spring event. We now anticipate the impacts for HPAI to reduce production volume in our Turkey facilities through at least the first half of fiscal 2023.

Breast meat prices remain historically high and have yet to moderate. Our team has done an exceptional job managing through disruptions caused by HPAI. Reflected in our guidance range or assumptions for higher pension expense and higher feed costs for our Turkey business.

Taken together, these costs are approximately $0.15 of headwind specific to fiscal 2023. In addition to these costs, we have planned incremental investment against One Supply Chain and go forward supporting areas such as infrastructure, automation, data analytics, brand support and investment in innovation capabilities.

In closing, I am extremely excited about Go Forward and our plans to unlock even more potential from our now $12 billion uncommon company. We have a long track record of successfully evolving our company, which is a credit to our strong management team and our inspired team members around the world, better aligning our structure with our strategy, which is at the core of this transition positions us well into 2023 and for the long-term. Said simply, Go Forward ensures that we will continue to deliver on our commitment to our team members, customers and shareholders.

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

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QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Today's first question comes from Peter Galbo with Bank of America. Please go ahead.

Peter Galbo Q

Hey, guys. Good morning. Thank you for taking the questions. Jim, I'm just curious, like, in the overall protein complex and understanding that protein is now a much smaller portion of your overall business than maybe it was historically. But your single biggest input is still pork and that seems to have been less deflationary at this point than the other proteins, beef is down pretty substantially; chicken, obviously, has come off materially. Just curious about your outlook over the next 12 months, what is it going to take to get some of these port prices and particularly the cuts that you buy to kind of match the other proteins that we're seeing in terms of how deflationary they've been? And maybe how that might end up pulling through your business, both from a top line and margin standpoint?

Jim Snee A

Yeah. Thanks, Peter. Good morning. Pork is still a very important part of our complex, as you described. And for us, we think that pork still represents a great value to consumers. As we're looking into 2023 end markets, although we expect some moderate relief are still going to run well above five-year averages. And we've also seen a lot of volatility throughout the last several years, and that's what we really have talked about is it's not so much the point to point, but some of the volatility that occurs.

The other thing that we're watching very, very closely is the export element in terms of what's happening with pork. So one of the things to consider is as turkey prices are higher, we're seeing bone-in hams be exported at an accelerated rate. And then the other thing is just thinking about the continued labor challenges that are out there. And so one of our key inputs across a lot of our business is pork trim. And if the labor is not there to do the necessary boning to get the trim, then we're not going to see that relief.

So there are a lot of variables at play, but we know that there are things that we can control. We know that our brands are going to remain strong. The work that we're doing to drive that demand is very successful. And now we just need some of these other variables that are outside of our control to play out more favorably for us.

Peter Galbo Q

Got it. No, that's helpful. Thank you. And Jacinth, maybe if I could ask a two-parter or just on some of the moving pieces in the guidance for 2023. Of the $0.15 you mentioned that I think is a headwind from pension and turkey. Can you just break down for us what exactly the pension piece is versus the feed costs?

And then also just within the guidance, I don't think I heard any mention on MegaMex, I think avocado prices have gotten more favorable. So any commentary there as well? Thanks very much.

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Jacinth Smiley

A

Yes. Good morning. So yes, so the pension and feed costs definitely headwinds as we go into 2023. The split between the two is about $0.10 related to feed and $0.05 related to pension costs. And as it relates to our MegaMex business, we expect avocado prices to continue to go down. So that will translate into positive impact for us on our MegaMex business.

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

Ben Theurer

Q

Yeah. Hi, good morning everyone, and thanks for taking my question. Jim, could you elaborate maybe a little more on the dynamics and what you're seeing amongst consumers around the elasticity. So you've talked a little bit about it in the prepared remarks, but it would be nice to understand what's like kind of embedded within your guidance on top line, how much of a decline in volume, you kind of anticipate based on the pricing you've done more recently, which obviously still remains a tailwind, particularly in the first fiscal half, because of the prices that you've just implemented more recently. So that would be my first question. Thank you.

James Snee

A

Yeah. Good morning. Ben. So, I mean, it varies category-by-category. As you know, we've got some categories where the elasticities are performing at more historical levels. I think probably our legacy grocery products, which show a big part of that being our new convenience meals pillar. But then we've got some others where we're seeing elasticity, but not quite to the rate that we would have historically. The thing that is positive for us is, we're not seeing anything above historical levels for elasticity. And so that, let's say, a really, really good thing.

The other part that we need to make sure we're thinking about is our foodservice business. A significant part of our overall portfolio. That business -- the demand continues to remain strong. Portfolio is well positioned, and that team is just doing a great job not only driving new demand, but also taking share.

Ben Theurer

Q

Perfect. And then just on the CapEx number, can you elaborate a little bit on like what part of that is how much of that is maintenance? How much is maybe what you didn't execute or initially may plan to execute in 2022 and then couldn't how much a rollover, how much is maintenance and how much is really dedicated new CapEx for 2023?

Jacinth C. Smiley

Executive Vice President & Chief Financial Officer

A

Yes. So we have -- in the plan for 2023, the $350 million of CapEx plan of that, the maintenance portion is fairly consistent with what we have on a yearly basis at about $125 million of that number. I mean in terms of rollover, we certainly have pieces coming over from last year, which is relating to our SPAM and on our China expansion that we're doing.

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Jim Snee A

Yeah. And just on that note, Ben, as we've said in our comments, SPAM capacity will come online the early part of 2023. And then really the China capacity that Jacinth references will really come online until 2024.

Ben Theurer Q

Okay. Thank you very much.

Operator: Thank you. And our next question today comes from Ken Zaslow with Bank of Montreal. Please go ahead.

Ken Zaslow Q

Hey, good morning, guys.

Jim Snee A

Hi, Ken.

Ken Zaslow Q

Two questions. One is, when you think about your pricing actions, which categories have you taken pricing to cover the cost? Which ones do you still need to take pricing to cover the costs? And then I have a follow-up.

Jim Snee A

Yeah. I think as you think about our portfolio, again, going back to our legacy Grocery Products portfolio. We've taken significant pricing but haven't quite covered down all of the inflation that we're seeing. But as part of that, and you know this, Ken, is we're being very sensitive to some of the price gaps that are out there in the category. So we've had to watch that closely. We're seeing some of those gaps start to narrow as others are moving. So that's a good thing. And then we are continuing to look at certain categories. But as always, we're going to have to be very, very strategic. But I would say, as we think about our overall portfolio, that's probably the biggest gap that we have.

Ken Zaslow Q

Okay. You gave guidance kind of on the top line. You didn't give a feel for the operating profit, which ones of the divisions you'll see – even if you do high, low, medium, more than average, less than average. Any sort of commentary on the profit growth outlook by division would be quite helpful, just particularly given that you're changing divisions, and we don't have the same sort of history of understanding how those margins will kind of evolve. So any sort of commentary on that would be really appreciated?

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Jim Snee A

Yeah. I think in our prepared remarks, Ken, we talked about growth really being driven by foodservice and international. As I said, we expect our foodservice business to remain strong. Our current demand is very positive. Portfolio is well positioned. Our international business, we expect to bounce back and some of those headwinds moderate. The retail business, which is experiencing the biggest change in this new operating model is certainly going to have the impact of some of the feed costs that Jacinth has talked about. So consistent with what we said in the prepared remarks, we really expect the drivers of the growth to be foodservice and international.

Ken Zaslow Q

So when you were talking about it, and I don't want to ask a third question, I understand that. But when you were talking about it, you were talking about the sales or the operating profit. I thought during the commentary, you were mostly talking about sales, but you will – you think it applies to the operating profit as well. I just want to clarify, and then I'll leave it there.

Jim Snee A

Yeah. Think about both of them that way, Ken.

Ken Zaslow Q

Okay. Thank you.

Jim Snee A

Yep.

Ken Zaslow Q

Thank you very much.

Operator: Thank you. And our next question today comes from Robert Moskow with Credit Suisse. Please go ahead.

Robert Moskow Q

Hi. I actually have a bunch of questions here. You said that, feed costs are going to be the biggest headwind for retail in fiscal 2023. Is that because Turkey, like the majority of Turkey will be lumped into it. And just in the context of all these other retail businesses that are now catching up to margins, it just strikes me that the U.S. retail outlook is pretty soft. Like, most of your packaged food peers are catching up and exceeding last year's gross margins, because of all the pricing they've taken. So, what's different here? Is it just turkey? Or are there other things? Hello?

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Operator: Hello. Pardon, everyone. This is the conference operator. It looks like we've lost the speaker connection. I want to put music back on, and we'll be right back with you. We ask you please hold the line. Thank you. [Technical Difficulty] And everyone, we thank you for your patience. We've reconnected the speaker location. Mr. Moskow, if you can please repeat your question sir. Thank you.

Robert Moskow Q

Sure. So it was a question about the guidance for retail, I guess, for profits to be flattish or maybe even down in 2023. And you said it was because of feed cost, is that because the majority of Jennie-O will end up in retail. And ex that, would you have expected retail profits to grow? Because in comparison to all these other US packaged food companies, it seems like the next 12 months is characterized by pricing catching up to cost and gross margins re-expanding?

Jim Snee A

Yeah. I think the way you're just -- Rob, first of all, our apologies. Secondly, the way you're describing it is correct and that the feed costs as you think about the value-added business, the whole bird business, a lot of the commodity business that will be flowing now into retail will be impacted by those higher feed cost as just described. So I mean absent that the rest of the business as we think about the pillars are very positive.

Robert Moskow Q

Okay. And could you help us a little bit just on your outlook for Turkey in fiscal 2023, because it must be a pretty wide range of outcomes given the uncertainties around AI. And is your outlook different for commodity than it is for value-add? Is it still very positive for commodity and weak for value-add? How should we think about it?

Jim Snee A

Yeah. You're opening statement is correct. Again, Rob, is that there's a lot of uncertainty as we think about the jobs business going forward. On our last quarterly call, we had talked about us being back to more normalized levels after the first quarter. Now, we're talking about the back half of the year. And then everything that you just described really all depends on the meat availability in our system and then what's available elsewhere. So there is just a lot of uncertainty in the jobs business throughout 2023.

Robert Moskow Q

Can I assume that you're assuming flat profits in Turkey just as a starting point for 2023? Or how should I think about it?

Jim Snee A

Yeah. I mean, I think that's a good starting point. We've got feed costs. You've got breast meat markets, you've got supply. There's just so many variables there as we progress throughout the year. We'll certainly be keeping you well-advised.

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Robert Moskow Q

Okay. Thanks.

Operator: And our next question today comes from Tom Palmer at JPMorgan. Please go ahead.

Tom Palmer Q

Thanks for the question. I wanted to get some clarity maybe on the expected earnings cadence for the year. You made mention, for instance, of certain pork cuts rolling over. It sounds like maybe we see more of a flow-through of that in the first quarter than we did in the fourth quarter. At the same time, there's some operational changes underway. Maybe those present some initial cost headwinds. So how does this shake out just as we think about earnings progression for the year?

Jim Snee A

Good morning, Tom. As we're thinking about the earnings growth that we described, I mean we expect it to be fairly evenly distributed throughout the year, half one and half two. Clearly, we've identified the major impacts that are out there in terms of feed and the pension costs that we've already talked about several times. And as we go throughout the year, we we've talked about the need to really now find some supply chain savings. We've talked about the fact that we expect fill rates to improve -- continue to improve as we progress. We've got some pricing that will continue to roll forward. International, we expect to moderate and improve throughout the year. And so there are some things that will happen sequentially, but as we're looking at the business, we do expect it to be pretty evenly distributed between half one and half two.

Tom Palmer Q

Understood. Thank you. And then I just wanted to ask on the cash balance approaching $1 billion. You highlighted that there's really not any near-term debt due, and it's pretty low cost. So how should we think about deploying this? I mean is this -- you'll retire some debt in the coming year?

Or is it more -- this is put aside as a way to effectively fund M&A without having to go to capital markets and maybe a higher interest rate environment? And then just with regards to that M&A side, I think you talked about international being an opportunity at the Investor Day. Is that still the priority? Or just given macro uncertainty, should maybe domestic be more of a priority?

Jacinth C. Smiley A
Executive Vice President & Chief Financial Officer

Good morning, Tom. So our capital allocation policy and approach will remain -- it still remains the same. And so, yes, I mean, we're happy that we continue to generate very strong cash flow, and we will continue to deploy it strategically as it relates to paying down the debt. We still believe that is not the best use of our cash today.

You know, our first payment doesn't come due until 2024. And so again, we'll continue to be strategic. We're continuing to look at opportunities from an M&A perspective and aligning those with our six strategic priorities. And so that is really how we'll think about deploying our funds, paying our dividends, continuing to remain a

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dividend aristocrat. That's very important to us. And in terms of the cadence of how we deploy the funds, as I talked about, that still remains consistent with our strategic approach for deploying our cash.

James P. Snee
Chairman, President and Chief Executive Officer
A

And from an M&A perspective, Tom, you know, we are still very interested in international opportunities. We believe that we can continue to leverage what we've built in Asia Pacific, China. We've talked a lot about snacking and entertaining as we built out the SKIPPY portfolio, the Planters portfolio, also the work that we've done in Brazil. So international certainly remains a key area for us as we're thinking about the acquisition front.

Tom Palmer
Q

Right. Thank you.

James P. Snee
Chairman, President and Chief Executive Officer
A

Yes.

Operator: Thank you. And our next question comes from Rupesh Parikh with Oppenheimer. Please go ahead.

Rupesh Parikh
Q

Good morning. And thanks for taking my question. So I wanted to just go back to top-line growth of 1% to 3% growth. I was just curious if you can just again walk through the key puts and takes there. At least to me, it seems a little lighter than we thought going into this year.

James P. Snee
Chairman, President and Chief Executive Officer
A

Good morning, Rupesh. I think there are -- just like you described, lots of puts and takes. We do know that we're going to have some positive impact from pricing. We expect strong growth, foodservice and international. We are bringing more capacity online in 2023. But then we also know that we've got elasticities that will be somewhat of an offset.

But as we've already talked about, really the biggest wildcard in terms of the top-line for next year is jobs. And so knowing that we're dealing with this unprecedented fall event and it's already pushed back what we expect to be a more normalized level by a quarter. We have to wait and see what happens in the spring time. And so, really, that's the biggest unknown as we think about our sales outlook in 2023.

Rupesh Parikh
Q

Okay, great. That's helpful color. And then, just on the US consumer. Obviously, you guys are seeing great strength in your Grocery Products business and you're seeing strength of foodservice. So just curious how you think about the consumer just based on your vantage points in both channels.

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Jim Snee A

As we're thinking about 2023, it's continued strength. The brands are doing well. All of the scan data for the most recent 13 weeks are showing really positive dollar sales growth. As you said, the foodservice business just continues to do really, really well, not only finding new opportunities, but they're also doing a really nice job of taking share.

Rupesh Parikh Q

Great. Thank you.

Operator: And our next question today comes from Michael Lavery with Piper Sandler. Please, go ahead.

Mike Lavery Q

Thank you. Good morning.

Jim Snee A

Good morning.

Mike Lavery Q

I just wanted to unpack pricing a little bit. And, I guess, just would love to understand in your guidance. Does it factor in -- can you quantify roughly what amount of pricing is included in the growth outlook? And how much is that, just -- are you counting on just the pricing you've already taken flowing through, rolling into next year? Or do you anticipate new pricing actions on top of that?

Jim Snee A

Yeah. Good morning, Michael. What we've not factored in there right now are the pricing actions that we've taken. And so, again, if you think about the grocery products pricing that went into place in the fourth quarter, our Jennie-O Turkey Store pricing that we put in place really also in the fourth quarter.

On the refrigerated side of the business, we've taken pricing on pepperoni. And so, we've got some pretty significant wraparound pricing there. And as we're thinking about 2023, just what I said earlier is, we're really watching the price gaps in the categories. We have to be very responsible.

We are seeing some gaps close. And we're also looking at those areas where we can be a bit more precise and strategic. So what we have in there today is already what we've taken, but we are assessing where there are those opportunities and where it's necessary going forward.

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Mike Lavery Q

Okay. Thanks. That's helpful. And just on the margin outlook and maybe not necessarily specific to next year or fiscal 2023. It seems like you're guiding for some modest margin expansion. But as you think about just where margin levels were two, three years ago, how much can you restore that? Or how long does it take? What's sort of the outlook as far as the margin build going forward?

Jim Snee A

Yeah. As we're thinking about it, the headwinds that we've covered down or had to cover down over the last several years are pretty significant. And the team has done a great job, when we think about some of the commodity costs that we've had, we've talked a lot about freight and warehousing costs.

So as we think about relief from some markets, we've got in still incredibly high markets, some of the packaging costs. We've got to do a better job of taking costs out of our supply chain and our operations.

And so it's all of those things that we need to focus on, but also get some moderation on, which to say is going to happen in any specific point in time. If we've learned anything over the last three years is that's really hard to do. But thinking about the things that we can control and focusing on those things is really what's going to allow us to continue on this journey of margin expansion.

Michael Lavery Q

Okay, great. Thanks so much.

Operator: And our next question today comes from Eric Larson at Seaport Research Partners. Please go ahead.

Eric Larson Q

Yeah. Thanks. I hope everybody had -- thanks for taking my question. I hope everybody had a good Turkey Day. I was thinking that you could have given your employees a really nice nontaxable bonus just by giving turkey this year.

Jim Snee A

You should have called us sooner.

Eric Larson Q

Exactly. So Jim, I, like others, we're just kind of struggling to kind of think through the process of your new structure, which we will eventually get used to. But for people like me, I've been looking at your business this way previously -- it's measured in decades, as you know.

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So, I guess my first question that I want to ask is -- I think you've now -- and it relates to your commodity sales business -- your commodity sales, your commodity pork sales, which I think you now have effectively by contract. I don't think you have much of that anymore. And I'd like an update on that as well.

And then, the commodity sales also for Jennie-O, I know I don't have a huge Foodservice business, but why would Foodservice not participate in some of the ups and downs in the commodity pricing market, given that neither retail nor foodservice would be responsible for that commodity business solely? So, how do the commodity sales for all the stuff kind of land in your new retail, foodservice, international structure?

Jim Snee A

Yeah. Great question, Eric. So, a couple of things. I mean as we head into this new operating model, I mean, clearly, we're going to continue to provide clarity and education. The key takeaway in all of this is really about how we are able to align our strategy with our structure. And although we've had all of our different reporting segments historically, we haven't had it as well aligned as it could be. So that's really where we're heading. David and the team will obviously be spending a lot of time on the education front to make sure everybody understands what is, where and why.

From a Jennie-O perspective, as we think about how that commodity business in particular falls, it will fall between our retail and international business. And so there will be elements that will fall in both. When the other part of it, as you mentioned, is the foodservice piece, is there's still a significant Jennie-O business in our Foodservice segment.

And then the other part you mentioned was just in regards to traditional pork commodity sales. And that business, I mean, our team has done just a great job over the last number of years, finding ways to really derisk the business, derisk the commodity side. And right now, we're less than 10%. And so that's a journey that we've been on for a very long time. We continue to stay focused on that. And the team has just done a great job. So hopefully, that gives you a little more clarity. But just so you know, as we get into 2023, we'll have those opportunities for education and further discussion.

Eric Larson Q

Okay. Thanks guys. I appreciate the time.

James P. Snee A
Chairman, President and Chief Executive Officer

Yep.

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

Q

Good morning everyone. This is Arthur on for Adam. If you could just talk to us about how Jennie-O performed relative to your expectations. It looks like volume declines weren't nearly as much as we had anticipated and you had noted in the last quarter's call. And if you could also give us some color on -- to whatever extent you can,

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margin headwinds from fixed cost under absorption and how pricing, specifically commodity pricing affected that or offset that? Thank you.

James P. Snee
Chairman, President and Chief Executive Officer

A

Yes. Good morning, Arthur. I would say that our Jennie-O business was actually in line with our expectations. And what we have said for the back half of last year, when we first started to see the outbreak was that we were going to have a 30% decline in volume in the back half of the year, and that's almost exactly what we saw.

So the volume piece was accurate. Clearly, the drivers or what happened with the breast meat market, obviously, whole birds, so there's always a lot of moving parts. But I would say that, by and large, it met our expectations. And then I'm sorry, I missed the second part of the question.

Q

Just to what extent fixed cost under absorption was a headwind on margins? And what offset you had on pricing?

James P. Snee
Chairman, President and Chief Executive Officer

A

Yes. Arthur, I think David is going to have some follow-up calls. So maybe we'd be better served to handle that there.

Q

Okay. Thank you.

James P. Snee
Chairman, President and Chief Executive Officer

A

Yes.

Operator: And ladies and gentlemen, this concludes our question-and-answer session. I'd like to turn the conference back over to the management continue for any closing remarks.

James P. Snee
Chairman, President and Chief Executive Officer

Well, thank you all for joining us this morning. As we close the book on our fiscal 2022, I want to once again thank our team for delivering such strong results for the fourth quarter and full year.

I also want to thank the entire team for their hard work, as we embark on our new operating model. We still have work to do, but their efforts to date have been nothing short of outstanding as we create the Hormel Foods of the future. As we go forward into 2023, I want to wish all of you a happy, healthy and safe holiday season.

Operator: Thank you. And ladies and gentlemen, this concludes today's conference call. We thank you all for attending today's presentation. You may now disconnect your lines, and have a wonderful day.

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