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Hormel Foods Corp. (HRL)

Q3 2023 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning and welcome to the Hormel Foods Corporation Third Quarter Earnings Conference Call. All participants will be in a listen-only mode. 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. 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 2023. We released our results this morning before the market opened, around 6:30 AM Eastern Time. 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; Jacinth Smiley, Executive Vice President and Chief Financial Officer; and Deanna Brady, Executive Vice President of the Retail segment. Jim will review the company's third quarter results and give a perspective on our outlook for the balance of fiscal year 2023. Jacinth will then provide detailed financial results and further commentary on our outlook. Deanna will join Jim and Jacinth for the Q&A portion of the call.

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. At the conclusion of this morning's call, a webcast replay will be posted to our investor website and archived for one year.

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Before we get started this morning, 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. Non-GAAP figures adjust for the impact of an adverse arbitration ruling of approximately $70 million reflected in operating expense. These non-GAAP measures include adjusted operating income, adjusted operating margin, adjusted selling, general and administrative expenses, and adjusted diluted net earnings per share. Discussion on non-GAAP information is detailed in our press release, which can be accessed from our corporate or investor website.

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. In an increasingly dynamic and competitive environment, we grew volume across all our segments, delivered adjusted diluted net earnings per share in line with last year and made further progress addressing the near-term challenges impacting the business during the quarter. This progress included reducing inventory, continuing to build momentum in the Planters snack nuts business and driving adjusted operating margin improvement compared to last year.

Reducing inventory to more historical levels remains a top priority for the company. Our actions to rectify the inefficiencies caused by elevated inventory are working, demonstrated by a sequential reduction in dollars of both finished goods and total inventory. The value of finished goods inventory ended the quarter at its lowest level since this same time last year, representing meaningful improvement. We expect further declines in the fourth quarter and also plan to achieve our days sales in inventory target by the end of the year.

We also drove improvement in our Planters business, supported by another quarter of higher shipments and positive results in consumption data. For the quarter, Retail shipments of Planters snack nuts and CORN NUTS varieties were up 5% and 24% respectively. Retail data shows dollar consumption and share improving sequentially for the last 52, 26 and 13-week periods. Volume trends remain encouraging as well, with above-category performance over the last six months, and more recent data shows Planters volume and dollar shares have inflected into positive territory.

The launch of our innovative flavored cashews is meeting expectations, and we are seeing strong acceptance from our customers. While early, our flavored cashews are over-indexing with younger consumers, as we see the benefits of leveraging our brand equity to drive excitement for the category. We are supporting the launch with social and digital activities, as well as a national TV ad campaign. And we recently launched an LTO for the fall season, Apple Cider Donut flavored cashews, which we expect to drive incremental volume and attention for the category.

Momentum continues to build in our snack nuts business, as we benefit from regained distribution, investments in innovation and effective promotional support. We continue to do our part as the category leader to support the Planters and CORN NUTS brands to drive growth for our business, the snack nuts category and for our customers. Lastly, we continue to make progress in improving our margin structure, with adjusted operating margin slightly ahead of last year. Margins benefited from demand for our premium items in Foodservice and

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growth from the Retail SPAM and Black Label bacon portfolios, areas we have invested in heavily over the past three years.

We also more than overcame the positive mix impact from strong SKIPPY sales and turkey markets last year, as well as a 15% increase in advertising investments to support our brands during the third quarter. We expect our highest operating margins of the year in the fourth quarter, aided by a seasonally strong sales mix and savings from a series of projects aimed at reducing cost and complexity throughout our system.

Our third quarter results reflect the strength of our leading brands and the value of our balanced business model. Investments into our brands and continued improvement across our supply chain have generated positive performance in the marketplace. Volume growth for the quarter was broad-based, driven by a recovery in turkey, elevated demand for many of our Foodservice items, and growth from leading Retail brands, including SPAM, Black Label, Planters and Hormel pepperoni.

On an adjusted basis, diluted net earnings per share for the quarter was $0.40, even to last year. Compared to our outlook heading into the quarter, we absorbed unexpected earnings headwinds of $0.02 to $0.03 resulting from much weaker results in our International segment and supply chain disruption caused by a third-party logistics provider shutdown.

Looking to our segments, our Foodservice segment delivered balanced volume gains and another quarter of segment profit growth. Volume for the quarter increased, driven by growth in our affiliated businesses and strong demand in many branded categories, including pizza toppings, premium bacon and breakfast sausage, and premium prepared proteins. Brands such as Café H, Fire Braised, Fontanini, Old Smokehouse and Bacon 1 delivered volume gains compared to the prior year.

Net sales declined 3% due to lower market-driven pricing. For context, the average selling price per pound decreased 5% compared to last year, resulting from input cost deflation. As anticipated, our Foodservice business leveraged its differentiated capabilities to drive double-digit segment profit growth, led by better volumes and improved mix. Our team continues to successfully manage pricing and cost dynamics. They continue to actively engage with operators through our direct selling model, and they continue to innovate to address key operational issues such as labor, prep time and complexity.

Industry data from Technomic is also supportive of growth for our business, with operator sentiment steady, industry employment improving and dollar sales increasing. Inflation in the channel has also slowed for the fourth consecutive month. We expect a strong finish to the year from this team, driven by growth from premium items, further recovery in turkey, and as the team leverages its capabilities in the K-12 and college and university channels this fall.

In our Retail segment, we grew volume in key categories and saw a recovery across the turkey portfolio. For the quarter, we delivered volume growth in four of our six Retail verticals, and those verticals were value-added meats, bacon, snacking and entertaining, and emerging brands. Volume and net sales improved for the value-added meats vertical, primarily due to higher turkey volumes. The team is heavily focused on regaining distribution of our value-added Jennie-O products and managing turkey supply through the current recovery period and upcoming holiday season.

The bacon vertical again delivered excellent results due to elevated demand for Black Label items and favorable input costs for most of the quarter. Over the last 52 weeks, Black Label bacon has grown share and household penetration by 1 point each. Our strategy to offer a wide variety of both raw and pre-cooked items in the

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marketplace has been successful, as we grow our business in the large and highly relevant bacon category. Our team is executing our brand strategy while maneuvering through the market volatility we are currently experiencing.

Volume gains for the snacking and entertaining vertical were led by Planters snack nuts, CORN NUTS corn kernels, Hormel pepperoni and Hormel Gatherings Party Trays. In addition to improvement for the Planters snack nuts business, our pepperoni and Hormel Gatherings businesses are healthy, demonstrated by household penetration gains for these brands during the quarter. We expect holiday demand and promotional support to drive a strong end of the year for the Planters, Hormel Gatherings and Columbus brands.

Our Applegate business posted another quarter of volume and net sales growth, led by our frozen line of breaded chicken and breakfast sausage. Many products also outpaced category dollar sales growth during the quarter, including breaded chicken, breakfast sausage, bacon and hot dogs. The team also introduced Applegate Naturals frittata bites, the industry's first and only Certified Humane frozen egg bites. In the fourth quarter, we expect to benefit from expanded distribution for the Applegate brand and from new capacity to support our popular line of frozen breakfast sausage.

Net sales of global flavors items were comparable to last year, while pricing actions, operational gains and favorable input costs on avocados drove equity and earnings improvement for our MegaMex business. The Herdez brand remains relevant with consumers, outpacing category growth for dollar and volume sales in the salsa, taco sauce, hot sauce, refrigerated guacamole and refrigerated salsa categories. Convenient meals and proteins net sales declined as higher sales to SPAM varieties and Hormel chili were more than offset by the difficult comparison from high levels of demand for SKIPPY spreads last year.

We continued to gain distribution on both innovative and core items during the quarter, which helped alleviate some of this pressure. In the fourth quarter, we have numerous programs in place to engage consumers at the store level and online with reminders of the value offered by our products. These efforts are expected to help offset the impact of elasticities and as consumers utilize their pantry supplies. We also secured additional capacity for SKIPPY peanut butter, which should help meet the elevated levels of demand we continue to see.

Segment profit for the Retail segment declined due to unfavorable mix and increased brand investments, partially offset by the impact from pricing actions across the portfolio, improved bacon volumes, and higher equity in earnings from MegaMex. Our Retail business is benefiting from market share gains, innovation, new distribution, higher fill rates in key categories, and effective advertising and brand support. However, there remains volume pressure in many categories across the store. Strong execution this fall and holiday season will be key to delivering our outlook.

Our International segment remained challenged during the third quarter and the inflection we expected in this business did not materialize. Segment profit declined significantly due to unfavorable pork and turkey commodity markets, softness in China and lower branded export demand. Commodity fresh pork and turkey volumes were strong during the quarter, though depressed pricing led to weaker mix, especially on turkey items.

The commodity environment is expected to remain unfavorable for the balance of the year due to high inventories of freezer stocks in key export markets. In China, Foodservice sales improved sequentially throughout the quarter, growing 14% compared to last year. However, Retail sales remained soft as we lapped difficult comparisons to last year and as consumer demand in the Retail channel slowed considerably. Near-term, we expect our Foodservice business in China to grow, which should help to offset continued softness in the Retail channel.

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Lower Retail sales are anticipated to have a negative impact on China's profitability for the remainder of the year. As we've reiterated over the past few quarters, our strategies to grow our global brands, multinational businesses in China and Brazil, and partnerships around the world are sound. Our International team is confident that these situational dynamics will abate, allowing for our teams to resume delivering accelerated growth.

Turning to our outlook, we remain focused on driving volume and earnings growth, as well as delivering on our commitments to improve our business. The operating environment domestically and abroad continues to be dynamic, and we anticipate consumers and operators to remain highly intentional in their spending. Our broad portfolio of products and diversified channel exposure position us well in this regard.

As we close the year, we expect a strong finish from our Foodservice segment, incremental savings from a series of projects aimed at reducing costs and complexity throughout our system, and further synergies from our implementation of GoFWD. Additionally, we expect continued softness in our International segment and earnings pressure from heightened competition at Retail. We are assuming increased promotional activity this fall in the Retail channel, as consumer demand moderates to more historical levels and as industry-wide supply chains continue to improve.

We also expect an impact from resumed student loan payments, which could pressure overall consumer spending in the US. Taking these factors and our performance to-date into account, we are providing fourth quarter guidance and an updated outlook for fiscal 2023. For the fourth quarter, we expect modest volume growth, which assumes growth from the Foodservice segment, continued recovery in turkey and improved fill rates in key categories.

Fourth quarter net sales are expected to be between $3.1 billion and $3.6 billion, reflecting our current assumptions for raw material input costs in the fourth quarter. Full year net sales are expected to be down 4% to flat. We expect fourth quarter diluted net earnings per share to be down from last year, which accounts for continued weakness in the International segment and lower Retail segment results. Full year diluted net earnings per share are expected to be $1.51 to $1.57 and adjusted diluted net earnings per share are expected to be $1.61 to $1.67.

We believe our continued investments into our brands, disciplined financial strategy and balanced approach across our businesses position us well for future growth as we close a challenging 2023. At our upcoming Investor Day, we plan to provide an update on our fourth quarter assumptions and outlook and further detail on how our investments and transformational efforts as a global branded food company are expected to drive earnings growth in the future. We look forward to hosting many of you in person at our mid-October event.

At this time, I will turn the call over to Jacinth Smiley to discuss detailed financial information related to the third quarter and additional color on key drivers to our outlook.

Jacinth C. Smiley

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

Thank you, Jim, and good morning, everyone. During the third quarter, we delivered volume growth across all of our segments and net sales of $3 billion. Our businesses benefited from higher turkey supplies and continued improvement across our supply chain. Third quarter gross profit was $498 million. Gross margins for the third quarter increased compared to last year and improved 30 basis points sequentially compared to the second quarter.

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SG&A expenses increased compared to last year due to a $70 million accrual resulting from an unexpected unfavorable arbitration ruling. Adjusted SG&A expenses were in line with last year. Advertising investments were $43 million during the quarter, up 15% compared to last year, as we supported our leading brands in the marketplace. We expect full year advertising expenses to increase compared to the prior year. Equity in earnings of affiliates for the third quarter increased compared to last year due to higher results from MegaMex.

Operating income for the third quarter was $217 million and adjusted operating income was $287 million, 1% lower than last year. As Jim noted in his remarks, operating income was negatively impacted by supply chain disruption caused by a third-party logistics provider shutdown. Our teams did an excellent job diverting products through other distribution centers during this brief period, though we absorbed an impact from shortages, incremental logistic costs and elevated levels of distressed inventory.

The effective tax rate for the quarter was 21.7% compared to 24.5% last year. The lower effective tax rate was primarily due to favorable adjustments related to our fiscal 2022 federal tax return filing. The effective tax rate for fiscal 2023 is still expected to be 21% to 23%. The net result of all these factors was diluted net earnings per share of $0.30 and adjusted diluted net earnings per share of $0.40, which was comparable to last year.

We generated strong cash flow compared to last year. Operating cash flow during the quarter was $317 million, up 70%. This improvement was driven by favorable working capital adjustments. We paid our 380th consecutive quarterly dividend effective August 15 at an annual rate of $1.10 per share. This completes the 95th year of uninterrupted dividend payments to our shareholders. Capital expenditures in the third quarter were $78 million compared to $61 million last year. We're targeting $280 million in capital projects as we prioritize investments in growth, innovation, cost savings, automation, and maintenance.

We have updated our net sales and diluted net earnings per share outlook for the year. As a reminder, our diluted net earnings per share outlook reflects an adverse arbitration ruling of $0.10 per share. We said last quarter that growth in the back half would be partially dependent on the recovery in our International segment. While this dynamic has not played out as anticipated, the near-term drivers for our business continue to be successful execution against our plans for the Planters snack nuts business; improvement across the supply chain, including delivering on our internal cost reduction goals; year-over-year favorability in commodity and freight markets; and a recovery in turkey volumes.

In addition to the innovation, promotional and advertising support for the Planters business that are expected to positively impact the fourth quarter, we have several workstreams underway to drive further improvement in future periods. These workstreams encompass all aspects of the value chain and place a heavy emphasis on enhancing mix and expanding margins. The Planters business remains key to our long-term growth as a company, and we will continue to invest in and resource the business accordingly.

Performance across our supply chain continues to improve, demonstrated by another quarter of higher fill rates, progress on our commitment to lower inventory, and execution on our cost reduction targets. Our team has committed to several projects aimed at reducing cost and complexity to improve our margin structure. In the fourth quarter, we expect to realize incremental freight and indirect supply savings and benefits from our above historical run rate on our legacy cost mitigation efforts.

Longer term, we are committed to advancing the supply chain workstream of Project Orion and a series of multiyear projects aimed at unlocking earnings growth. We plan to provide more detail on these large-scale strategic projects at our Investor Day in October. We have seen market stabilization across many inputs, though key pork raw material commodity markets were volatile throughout the third quarter. The USDA composite cutout

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increased more than 40% sequentially during the quarter, primarily driven by strength in the belly, loin, and ham primals.

To start the fourth quarter, pork costs have begun to moderate seasonally, and we expect lower pork input costs compared to the prior year. We began to see a volume recovery in turkey during the third quarter, and we expect to see higher year-over-year turkey volumes in the fourth quarter. To further support our recovery, we have invested in incremental advertising to drive consumer awareness and engagement in the Retail channel. We're beginning to see signs of these actions paying off, especially for the important lean ground category.

Turkey markets continued to move lower in the third quarter as a result of increased supply, which is pressuring prices across our channels. Pricing is down considerably on commodity items and for breast meat entering the Foodservice and deli channels. Importantly, we're producing a full assortment of turkey items and our teams are selling with confidence in the Retail, Foodservice and International markets. This bodes well for the long-term outlook for turkey, which remains an important part of our balanced portfolio.

In closing, I want to specifically acknowledge our production professionals across the organization for their continued focus on safety. Their dedication is critical to the success of our company and the primary reason we remain on track for one of our safest years ever. Safety-first is a cultural belief. It's non-negotiable and represents an integral part of our company's fabric. We are proud of our track record and the work done each day to maintain our standard of excellence. Thank you to all our team members who uphold our safety-first culture.

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

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Your first question comes from Ben Theurer from Barclays. Please go ahead.

Benjamin M. Theurer

Analyst, Barclays Capital Casa de Bolsa SA de CV

Q

Yeah. Good morning and thanks for taking my question. So, Jim, I'd like to just follow up a little bit on the cadence of the year, the changes in outlook, and wanted to get your thoughts how to put things into perspective. So, if we go back, first quarter, obviously, there was a lot of like still the inventory issues, too much production, you had to work this through. You took a big hit and you kind of laid the ground as how the rest of the year was expected to be. Second quarter, very much in line with everything what you've talked about, and it feels like the third quarter started to kind of get sidetracked again.

And obviously, with your implied guidance, and you've mentioned you expect EPS in the fourth quarter to be down year-over-year, that's very different from the commentary we got just about three months ago when you actually expected in the fourth quarter to see most of growth. So, can you help us understand what in particular it was that drove that significant turn over the last couple of weeks from being on track to being maybe not so much on track and then to actually be off track again, and what you, as a management team, can do to get back into the right direction?

James P. Snee

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

A

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Yeah. Good morning, Ben. It's a really, really good question. So, we've done, obviously, a lot of thinking about that, and there are some things that are uniquely different in the conversation that we had at the end of Q1 and the conversation we're having today. If we take a step back to the Q1 call, really what we were talking about were more internal dynamics when we talked about and identified those near-term challenges in Q1. And as a reminder, as you said, it was our inventory situation, the performance of Planters, and then the cost margin implications and work that we had to do there.

And you fast forward six months from that timeframe and really, really good progress against all of those near-term challenges, and we feel really good about the work that the team has done. But as we sit here today, the conversation is different, and the conversation is driven more by what's happening in markets, some of the competitive activity and really overall consumer dynamics. And so, those are very uniquely different conversations. More specifically, as we've thought about the fourth quarter, and I think it's important to get that out there, what has changed for us. Well, our Foodservice business hasn't changed. We expect that business to remain well-positioned, continue to deliver growth, continue segment profit growth in Q4 on higher volumes.

Our International business, I think what's changed there is that it is weaker than we anticipated the last time that we talked. We had talked about an inflection point in China, and we haven't seen that, especially on our Retail business. We've talked about some elasticities in our International SPAM business, primarily in the Philippines. That's a sizable legacy market, and we've seen significant pricing activity over the last several years. But with that came some higher than expected elasticities. The team has already done some work to really drive consumer demand. We're seeing a rebound in offtake. And so, there is a really good plan in place for a recovery there.

We've also talked about some of the commodity headwinds at International [audio gap] (00:35:10). And so, what we anticipated there is weaker than we thought. And just in total, how do you overcome that, I mentioned the work that we're doing on SPAM. The China piece, the macroeconomic issues, there's a lot of moving pieces there. And so, we're continuing to work on Retail with innovation, new distribution, but we need to see that accelerate. Our Foodservice business continues to do well. We're aligned with some multinational business there that continues to perform.

And then, when you get to the Retail segment, I mean, that's the part of the business, Ben, that's a bit more nuanced. And it's good to have this conversation, because as a reminder, in Q4 of 2022, we had a really strong turkey performance in the fourth quarter of 2022. And a lot of that benefit was allocated to Retail in our restated financials. That being said, I mean, we expected to be able to overcome that, and that's how we looked at the business for the balance of the year. However, we're seeing some heightened challenges across the channel. I think we can see what categories have done in general. Promotions are higher as volumes remain soft across a lot of the categories, a lot of the aisles.

Our team continues to do work. We're holding our shares in the marketplace. The execution at the sales level is actually really, really good. But we know that that's going to continue to be an area that's challenged. The area where we've seen the most change really is our expectations for turkey. And as we said last quarter, we didn't expect this to be a flip-the-switch event and that it was going to take some time. We did expect it to happen faster. It's been a little slower than we expected. And so, that's really where probably the biggest change has occurred for us. And I do want to say though, if we take the turkey out of our volume figures, there's still really good underlying volume growth on a consolidated basis.

But what changed is our lean ground turkey business. We've talked about really just getting back into business. We knew that we had to sacrifice a lot of distribution during AI, and it didn't come back as quickly as we thought. Now, what I will tell you is some of our recent results are really showing the benefits of investments that we've

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made to drive consumer engagement. So, we are seeing improvement. Lots of work to do, but lots of opportunity for growth.

And then, the other part for us is we did expect a really strong finish to the year on our whole turkey business. And we started out strong, but most recently, we've seen some unique market dynamics and customer behavior that's really impacting both volume and pricing. Now, that's a work in progress. We're still working through this as we speak. And then, the last part that's newer news is we've had some really, really hot weather here in the Midwest at the end – middle to end of August and expected again this weekend. So, we have unfortunately lost some birds. That will have an impact on our business in the fourth quarter. And so, I know it's a long-winded answer. But I think it's necessary to really put into context what's changed for us.

But as we look past all of that, when you say what can you do to overcome that or change that, I mentioned the work that we're doing and the performance of our brands to hold shares in the marketplace. Our Planters business is definitely going in the right direction, regaining distribution; some fantastic innovation that's in the marketplace; really capitalizing on investments that we've made; being able to secure some additional SKIPPY capacity because that demand remains really strong; continued benefit from our supply chain as our fill rates continue to improve. So, there is a lot to be encouraged about. But your question is a good one, and hopefully, that gives you some better context as to the differences in our business, but also the differences in the conversations that we've had.

Benjamin M. Theurer
Analyst, Barclays Capital Casa de Bolsa SA de CV

Q

That was a very complete one, Jim. Thank you very much. And in the interest of time, I'll pass it on and skip on the follow-up. Thank you very much for the detailed response.

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Great. Thanks, Ben.

Operator: Your next question comes from Peter Galbo from Bank of America. Please go ahead.

Peter T. Galbo
Analyst, BofA Securities, Inc.

Q

Hey, Jim. Good morning. Thanks for all the thoughts.

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Good morning.

Peter T. Galbo
Analyst, BofA Securities, Inc.

Q

I guess just as maybe a follow-up to Ben's question or to put a finer point on it, one of the big questions we are getting this morning is just within the range of outcomes in 4Q and in your guidance, it still seems like there is a fairly wide range, a $500 million range on revenues at least. So, just I guess within the context of that, you talked about all of the headwinds. But I guess what could go right that would push you maybe towards the higher end of that versus the lower end of that? I think it might be helpful.

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James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. It's a great question. And really the biggest thing, and we've seen it very recently in terms of the market performance, is we've had significant volatility in two very important inputs. You think about what's happened in the belly market, the run-up and now the softening in the market. We have seen strength in [ph] 72% (00:41:25) lean trim. So, there's been a lot of volatility there. And then, probably the detailed answer that I gave a little while ago is how does turkey come back and at what rate. And then, the other thing is – so, you got the market conditions, but we've had pretty strong volume as well. So, I think when you put those two things together, it's important for us just to have that range.

Peter T. Galbo
Analyst, BofA Securities, Inc.

Q

Got it. Okay. No, that's helpful. And you touched on this a little bit, Jim. But I think in the context of bellies, and this may have been in the prepared remarks as well, can you just give us a sense of what you're seeing maybe in real-time there? The July move was outsized even relative to seasonality. I'm sure maybe Prop 12 played a role in that. But just you saw that run up a decent amount. It's come back a bit. Just what are you seeing in real-time given it does impact a meaningful part of the business?

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. I mean, I guess what we're seeing in real-time is what you're seeing in the marketplace and that it does have an impact in terms of how we are pricing the product. And as you know, as markets run up, you're always lagging a little bit further behind. And then, as markets come down, you're catching up that way too, but you probably see a little bit of expansion. And so, the volatility is the thing that really, as you know, leads to the unpredictability in what we're talking about.

Peter T. Galbo
Analyst, BofA Securities, Inc.

Q

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

Operator: Your next question comes from Ben Bienvenu from Stephens. Please go ahead.

Ben Bienvenu
Analyst, Stephens, Inc.

Q

Hey. Thanks. Good morning.

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Good morning.

Ben Bienvenu
Analyst, Stephens, Inc.

Q

So, I want to – if you would discuss these drivers that are negatively impacting 4Q results that have kind of evidenced themselves intra-quarter during the third quarter, what is your view at the moment on the duration of these impacts? So, thinking about more challenged exports, increased promotional activity at Retail and then

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weaker China results, I would think that those would have more duration in the fourth quarter. But how would you expect these things to play out based on what you've seen in the past?

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. Ben, that's a good question. And that's really what we're focused on is we know we've got some of these near-term challenges in Q4. A couple of things that we talked about that are really, we think, immediate or more closer in improvements. So, when we talk about the SPAM business in International, we're seeing that improved offtake. And so, we expect that business to be better in Q1. We talked about the lean ground turkey business. And so, that really is just that continued acceleration, and we've seen recent improvement in that business. So, that's only going to continue to get better. We're in the middle of the whole bird thing, and that'll shake out here between the end of Q4 and early Q1, given the timing of the holidays.

The competitive dynamics in the domestic Retail business outside of what we've talked about, I think our team is doing a really good job in terms of marketplace execution. We are now seeing some cost favorability trends. I think our innovation pipeline that we're seeing is really robust. So, there is a lot to like outside of some of the things that we've talked about. The part that is still a wildcard is the macro issues in China. Obviously, we've said earlier we thought there'd be an inflection point, and we were wrong. So, we're going to continue to do our work there in terms of driving distribution, the focus on innovation, getting our Foodservice business to continue to grow. And so, we are optimistic about what the future holds. But clearly, we've got some of these short-term challenges that we're addressing.

Ben Bienvenu
Analyst, Stephens, Inc.

Q

Okay, fair enough. On thinking about the Jennie-O business, there's a number of puts and takes. The International business segment seems to be negatively impacted by it, while some of the other segments are positively impacted by it. When you think about the runway over the next 6 to 12 months, we have declining turkey prices, but meaningfully stronger volumes as you regain distribution and the flock comes back – your production comes back. You should also be rotating into considerably lower feed prices over the next year. So, what would you expect the net benefit or detriment of all of those various factors to be as we look out over the duration of this next 6 to 12 months?

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. I think you're – the things that you're talking about are the things that are going to drive that business into 2024. And again, when we talk about the nuances of the turkey business, and this is going to get a little bit in the weeds here, Ben. But when we think about how maybe our lean ground business didn't accelerate as quickly as we thought, while there was some turkey that International had to sell and those market conditions were depressed. And so, as our lean ground business regains distribution and accelerates, there'll be less of that commodity type sale that they'll have to endure. And so, that's a positive for us.

You're right on the feed costs. I mean, we expect that to be favorable as we head into 2024, and breast meat prices should be more in line with more historical levels. So, we haven't done the math yet to say how is that going to shake out in total. But I think the bottom line, and we said this a couple of times throughout the year, is that turkey is an important part of this portfolio. When we think about it from a Foodservice perspective and we have it in our Retail portfolio, it's good to have turkey back. And for us to be able to operate in a more normalized environment over time, I mean, that's really where we're at our best and that's what we want to get to.

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Ben Bienvenu
Analyst, Stephens, Inc.

Q

Okay. Thank you, Jim. Thanks for taking my questions.

Operator: Your next question comes from Rupesh Parikh from Oppenheimer. Please go ahead.

Rupesh Parikh
Analyst, Oppenheimer & Co., Inc.

Q

Good morning and thanks for taking my question. I know it's a little early, but just curious if you can give any puts and takes as you guys look to FY 2024. And would you expect at this point to return to growth next year?

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. Good morning, Rupesh. I think we'll probably tag team this one a bit, because I think as we look into 2024, it applies to – everyone's going to have a point of view. I do think it's important to go back to some of those internal dynamics that we addressed early on in the year and that we are in a better spot on those near-term challenges or we'll call them key priorities. When we think about the state of the Planters business today, the work that we've done on inventory, the margin improvement that we've seen, and there's more work to come in that area, but we've done some really nice work.

And then, really leveraging more of the GoFWD benefits in year two, right. Year one is always feeling things out a bit, but we know that there will be more benefit in year two. But Ben mentioned feed costs. We do expect feed costs to be a tailwind as we head into 2024, further leveraging and capitalizing on those investments that we've made, and then we've also talked about the recovery in volume – turkey volume. And so, having that volume at more normalized market conditions is a good thing.

The offsets, obviously, we talked about China, the China economy, what happens there, what does inflation do with labor as a big component of that. So, we feel really good about the core business, the things that we can control. It's the things that are always out there that are outside your control that can be some potential headwinds. But by and large, continued strength in Foodservice. Retail, continue to be competitive, but we expect to hold shares in our categories. I've mentioned already strong innovation pipeline, that's really exciting. And then, International should improve off a, I mean, obviously, a significantly lower base. And so...

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

A

Yeah.

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

...Jacinth, Deanna, I'll let you add your two cents worth.

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

A

Yeah, certainly. Good morning, Rupesh. Jim has talked about a lot of the headwinds and some of the tailwinds here and things that we're working through from a market and customer/consumer standpoint. There are a lot of other things we're also doing in parallel here as we think about getting back to the margin structure that we have

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talked about before. And so, we're heavily focused from a project standpoint working through how do we get our portfolio more healthy.

And so, there are a couple of projects I'll just throw out here that we'll talk more about in Investor Day. As we think about portfolio segmentation and optimization, continuing on with Project Orion, as we think about our supply chain and the effectiveness there, and building out the right infrastructure to support this business as we continue to evolve and modernize. And just also thinking through advancing on different areas from an end-to-end planning standpoint, and continuing the transformation and getting the cost out of our system internally from a effectiveness and efficiency standpoint. So, there is a lot of work going on in parallel. As we deal with the tactical to operate the business, we're also thinking about long-term growth and setting this business up, as I said, to continue to return to a margin structure and expanding margins from where we are today.

Rupesh Parikh
Analyst, Oppenheimer & Co., Inc.
Q

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

Deanna T. Brady
Executive Vice President-Retail, Hormel Foods Corp.
A

Rupesh, this is...

Rupesh Parikh
Analyst, Oppenheimer & Co., Inc.
Q

Oh, sorry, go ahead.

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.
A

Go ahead, Deanna.

Deanna T. Brady
Executive Vice President-Retail, Hormel Foods Corp.
A

Rupesh, this is Deanna. I just wanted to tag team on that from a supply chain standpoint, from a Retail standpoint, we've been not only managing to the current environment, but continue to stay focused on standing up GoFWD and what that looks like and really starting to see the benefit. As you think about – GoFWD was to align our structure to our strategy, and if we think of one of our company strategies of snacking and entertaining, the team has been really a cross-functional team dedicated to modernizing the Planters business as an example. The team has made significant progress, and we're seeing that play out.

A few things that we've done as we pull our resources around Planters. In particular, we've pulled up our innovation pipeline. We're currently in market with three new flavors of cashews. We've quickly come to market with advertising to support that new launch called Surrender to the Cashew, and we're having great response both from our retailers and our consumers. Additionally, the team has looked at capital expenses and modernizations that we need in the plants to align with the consumer and packaging, as well as a really robust innovation pipeline that's coming at us.

And then, from a sales execution against Planters, again, as a benefit of GoFWD, thinking hard about regaining distribution, we did a price pack architecture study in the first half of the year, and the team's out working with our retailers to help them think about the category itself [ph] and the set. And that (00:54:11) price pack architecture

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work is helping us have really fruitful, insightful and analytical conversations with our retailers about how we grow together and how we can both meet the consumer with products that are going to be relevant and provide category growth.

Rupesh Parikh
Analyst, Oppenheimer & Co., Inc.

Q

Great. Thank you for all the color and best of luck.

Operator: Your next question comes from Tom Palmer from JPMorgan. Please go ahead.

Thomas Palmer
Analyst, JPMorgan Securities LLC

Q

Good morning. Thanks for the question.

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Good morning.

Thomas Palmer
Analyst, JPMorgan Securities LLC

Q

I think in the past, what we have seen with the whole turkey business is falling commodity prices don't always flow through the Retail business immediately just given how supply contracts are structured. You made a comment about unique market dynamics and customer behavior for whole birds. I just wanted to unpack what's happening. Is the net of this that whole bird prices are coming down at Retail maybe faster than we typically see or did you mean something else by that?

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

No. That's correct, Tom. I mean, I think at this point in the year, you'd see some higher bookings. But as the market has declined, I think there is a bit more of a wait-and-see mentality. And so, that's really what we're talking about when we're saying that there's some unique market dynamics.

Thomas Palmer
Analyst, JPMorgan Securities LLC

Q

Okay. Thanks for that. And then...

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah.

Thomas Palmer
Analyst, JPMorgan Securities LLC

Q

...just on the competitive environment at Retail and your comment about the promotional activity, just categories stepping up, are these – I guess, first, like what are the categories where you're seeing that competition and promotional activity most intense? And then, how would you describe kind of the start of that activity? Is it you're

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running it to drive share in certain categories or is the promotion step-up on your side more in response to what you're seeing from competitors?

Deanna T. Brady
Executive Vice President-Retail, Hormel Foods Corp.
A

So, this is Deanna. Thanks for the question. This isn't new for us, although it's new probably over the last couple of years, as companies have pulled back on promotions just because of supply and high demand. So, this isn't new for us. And having promotional activity as well as a balance with our baseline business is really normal, but it hasn't been normal in the last few years. So, as we reenter promotional activity, we have the opportunity to really think about it strategically and to leverage our revenue growth management team and price pack architecture work to really inform and sit down with the retailers to say, how do we do this, that's really positive for both of us, and how do we ensure that we're meeting the consumer and that we're reminding the consumer about our products, the value that they provide, as well as keep them coming in the store either in-store or online.

And so, we're thinking about both our digital activation, our in-store activation. And it really goes beyond just a promotion or a price point. We need to make sure that we have advertising in place as well. We need to make sure that we have innovation. So, I point again to the Planters example where we have innovation coupled with advertising and promotion in place, and it's working. From other categories, we're really, again, as we reenter promotional, trying to do it as smart as we can. I point to bacon. We've had a lot of good activity and growth in bacon this past year. We've had a cadence of promotional activity, a cadence of advertising, as well as we've got innovation coming in the bacon category that we're really excited about in 2024.

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.
A

And Tom, at an even higher level – Deanna gave you a great answer. When we said heightened competition at Retail, I mean, I think it's fair to say that we are seeing demand normalizing to some more historical levels. [ph] Edible sales (00:58:23) flat versus last year. Units have declined since 2019. So, as you've got that and supply chains have somewhat normalized, that – I'm not going to say everywhere there's capacity, but there's probably some additional capacity in the industry. And as fill rates get better, there's work to make sure that you're filling that up. So, it's that at a higher level, and then to some of the specific activities that we're working on, that Deanna talked about, that's really what we meant when we say heightened competition at Retail.

Thomas Palmer
Analyst, JPMorgan Securities LLC
Q

Okay. Thank you for the details.

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.
A

Yeah.

Operator: [Operator Instructions] Your next question comes from Adam Samuelson from Goldman Sachs. Please go ahead.

Adam Samuelson
Analyst, Goldman Sachs & Co. LLC
Q

Yes. Thank you. Good morning, everyone.

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James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Good morning.

Adam Samuelson
Analyst, Goldman Sachs & Co. LLC

Q

I guess the first question is trying to maybe clarify on tying the turkey comments specifically. I think previously – and I know Jennie-O is not a reported segment as such anymore. But previously, you had framed turkey profitability in fiscal 2023 as being roughly flat year-on-year. Is it fair to say that that's a decent chunk of the outlook cut today is attributable to turkey, and so that is going to be down a decent amount year-on-year even with the volume recovery from HPAI?

James P. Snee
Chairman, President & Chief Executive Officer, Hormel Foods Corp.

A

Yeah. I think that's fair to say, Adam, is to be slightly down year-over-year, and that's really due to some of these Q4 issues that we've talked about.

Adam Samuelson
Analyst, Goldman Sachs & Co. LLC

Q

Okay. And I guess just to the Q4 point, I mean, the full year range, you've got one quarter left, the sales range widened relative to your prior guidance. Yet, the EPS range narrowed. And I appreciate that maybe there was a pretty wide EPS range previously. But can you just help us understand kind of the puts and takes around, is it just the uncertainty on some of the commodity pork cuts and some of the turkey whole bird pricing, [ph] so that much (01:00:56) uncertainty on volume? And why wouldn't that revenue volatility kind of manifest in a wider EPS range? I'm just trying to make sure I understand kind of how the outlook has been recalibrated.

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

A

Yeah. So, good morning, Adam. I'd say for all the reasons that Jim talked about in terms of just the dynamic that we're seeing here and just the volatility, that is exactly why we have the ranges that we have as we sit here at the moment.

Adam Samuelson
Analyst, Goldman Sachs & Co. LLC

Q

Okay. But that's – certainly on revenue, but why would that change in revenue not fall to the earnings line? And why would it fall – why would there be more volatility previously on the range of outcomes on earnings and less on revenue today? Just with one quarter left in the year, I'm just – maybe it's a recalibration of...

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

A

Yeah. All mix, right, all mix-driven. You think about the mix between, right – even from a commodity standpoint and where markets are priced, it really depends on what that mix looks like. I mean, you could have a drag on the top line, where you have really strong volume hitting your top line, and just depending on where markets are, it doesn't necessarily fall through on your margin line.

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Adam Samuelson

Analyst, Goldman Sachs & Co. LLC

Q

Okay. All right. I'll take it offline. Thank you.

Operator: There are no further questions at this time. I will turn the call back over to Jim Snee, CEO, for closing remarks.

James P. Snee

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

Yes. Thank you. 2023 has certainly been a challenging year, but we continue to make great progress addressing the near-term challenges. Our continued investment into our brands, our disciplined financial strategy, our continued balanced approach across our business, all position us very well for future growth. My sincere thanks to all the hard work being done by the Hormel team to set us up for future success, and I want to thank all of you for joining us this morning and hope that you all have a safe Labor Day weekend.

Operator: Ladies and gentlemen, this concludes your conference call for today. We thank you for joining, and you may now disconnect your lines. Thank you.

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