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Campbell Soup Co. (CPB)

Q4 2021 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Ludi, and I'll be your conference operator today. At this time, I would like to welcome everyone to the Campbell Soup Fourth Quarter and Full Year Fiscal 2021 Earnings Conference Call. Today's call is being recorded. All participants will be in a listen-only mode until the formal question-and-answer portion of the call. [Operator Instructions] Thank you.

With that, I would like to hand the conference over to your host, Ms. Rebecca Gardy. Ms. Gardy, you may begin your conference.

Rebecca Gardy

Vice President-Investor Relations, Campbell Soup Co.

Good morning, and welcome to Campbell's fourth quarter and full year fiscal 2021 earnings conference call. I am Rebecca Gardy, Head of Investor Relations at Campbell Soup Company. Joining me today are Mark Clouse, Campbell's President and Chief Executive Officer; and Mick Beekhuizen, Campbell's Chief Financial Officer.

Today's remarks have been pre-recorded. Once we conclude the prepared remarks, we will transition to a live webcast Q&A session. The slide deck and today's earnings press release have been posted to the Investor Relations section on our website, campbellsoupcompany.com. Following the conclusion of the Q&A session, a replay of the webcast will be available at the same location, followed by a transcript of the call within 24 hours.

On our call today, we will make forward-looking statements, which reflect our current expectations. These statements rely on assumptions and estimates, which could be inaccurate and are subject to risk. Please refer to slide 3 or our SEC filings for a list of factors that could cause our actual results to vary materially from those anticipated in forward-looking statements. Because we use non-GAAP measures, we have provided a

reconciliation of each of these measures to the most directly comparable GAAP measure in the appendix of this presentation.

On slide 4, you will see today's agenda. Mark will share his overall thoughts on our fourth quarter and full-year performance as well in-market performance by division. Mick will discuss the financial results of the quarter and the year in more detail, and then provide our guidance for the full year fiscal 2022.

And with that, I'm pleased to turn the call over to Mark.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

Thanks, Rebecca. Good morning, everyone. Thank you for joining us today. In fiscal 2021, the pandemic continued to present challenges across North America, but I am so proud of how our teams, particularly our frontline and supply chain teams, adapted and rallied to keep each other safe and meet the sustained demand for our products. On behalf of the entire Campbell's leadership team, I am deeply grateful for their dedication, and we continue to make their safety and wellbeing paramount as they work to meet the needs of our customers, consumers and our communities.

As difficult and complex as this time has been, it has also been an extraordinary period for Campbell, and we've made clear, meaningful progress advancing our strategic plan. We've evolved into a different company, one that is stronger, more agile, and with growing more relevant brands that are better positioned for the future.

For the full year, I'm pleased to report that Campbell's organic net sales were comparable to fiscal 2020 and grew 3% on a two-year compounded annual growth basis, driven by both divisions reflecting strong in-market performance. In fact, three-quarters of our portfolio grew or held market share for the year, reflecting our continued momentum.

Adjusted EBIT lagged fiscal 2020 as we lapped dramatic scale and efficiency from a year ago and navigated a much higher inflationary environment this year. However, on a two-year CAGR, adjusted EBIT grew 5% and adjusted EPS grew 14% as we de-levered and improved our balance sheet.

Turning to slide 7, full-year organic net sales were comparable to prior year, which included a positive fourth quarter finish to 2021 in light of last year's remarkably strong performance. If you recall, our first half fiscal 2021 was driven by strong elevated in-market performance as we continued to gain share and made steady progress on supply to restore the shelf. The third quarter reflected the challenging comparisons to the prior year as we cycled the demand surge that accompanied the onset of the COVID-19 pandemic and navigated several headwinds, including increased inflation and executional pressures in our Snacks division.

In the fourth quarter, we delivered solid results ahead of our expectations across all three key metrics: net sales, adjusted EBIT, and adjusted EPS, and addressed the executional pressures we experienced last quarter. Organic net sales declined 4% as we lapped 12% growth in the prior year and delivered 4% growth on a two-year CAGR basis. Our fourth quarter performance accelerated relative to third quarter, driven by strong in-market results, particularly in US soup and Goldfish and the continued recovery of our foodservice business.

In Snacks, we delivered sequential operating margin improvement of 270 basis points versus the third quarter despite the continued industry-wide supply chain challenges. An important barometer of the health of our brand portfolio is our in-market performance. For the full year, 75% of our brands grew or held share versus the prior year, and the majority of our brands in our 13 core categories grew ahead of pre-COVID levels.

To note, repeat rates on our brands in all core categories are ahead on a two-year basis. Total company in-market consumption was minus 1% compared to fiscal 2020 on a 52-week basis. Importantly, compared to the fiscal 2019 period, consumption grew 10%, driven equally by strength in both our Meals & Beverages and Snacks divisions as we continue to make material advances in attracting and retaining consumers, especially the critical millennial cohort.

Turning to our division performance on slide 9, let me begin with Meals & Beverages. Our fourth quarter organic net sales decline of 9% and in-market performance of minus 2% reflects cycling the partial inventory recovery and elevated consumption levels in the prior-year quarter. Compared to the fourth quarter of fiscal 2020, we continued to grow share in Swanson broth, condensed soup, Prego, ready-to-serve soup, and Pacific Foods. On a two-year basis, we delivered strong consumption growth of 13% against organic net sales growth of 10%, narrowing the gap as our foodservice business continued to be stabilize.

On US soup, we delivered another quarter of record share growth of nearly 2 points, with gains in all segments. This included gains from Swanson broth, condensed soup, Well Yes!, and Slow Kettle driven by the continued recovery in our total points of distribution or TPDs. Our share of TPDs grew for the fourth consecutive quarter this year. US soup two-year dollar sales growth of 16% in the fourth quarter exceeded the growth in total shelf-stable meals and was just slightly behind total edible growth in that same time period.

Household penetration and repeat rates remain elevated compared to pre-COVID levels. Condensed soup increased dollar share for the 10th consecutive quarter, with the largest driver of share growth coming from condensed eating varieties as we nearly restored the full range of offerings to the shelf. As our ability to supply improved, we were also pleased to see household gains in ready-to-serve versus the prior year as a result of the shelf recovery and favorable at-home consumption behaviors, particularly for lunch occasions.

Ready-to-serve in-market consumption grew an impressive 21% on a two-year basis led by Chunky, Slow Kettle, and the successful relaunch of Well Yes!.

Pacific Foods continues to strengthen its position as the number one organic soup brand, with the fourth quarter marking seven straight quarters of share gains in measured channels. We expanded distribution and have recovered the majority of our supply, while bringing in more millennials to the category than any other soup or broth brand.

On Swanson broth, we increased our share by 3.7 points, our highest quarter of share growth in over three years, driven by our investment in supply recovery. This is important as it demonstrates the strength of the brand as we recovered lost share to lower-price players as our supply improved.

Prego delivered its best year of dollar share gains in four years and maintained the number one share position for 27 consecutive months. The brand grew in-market consumption on a two-year basis and delivered 5% growth over the prior year. Household penetration was elevated versus fiscal 2019 in every quarter and grew 1 point in the fourth quarter.

Overall, the Meals & Beverages division delivered strong in-market performance against difficult comparisons to the prior year and achieved share gains in key categories, particularly with millennials.

On slide 11, we are excited to share with you a glimpse into our Meals & Beverages innovation plans for fiscal 2022. Our new items focus on new occasions and relevant wellness trends. Expanding on the relaunch of our

better-for-you Well Yes! brand is the launch of Well Yes! Power Bowls with five unique varieties for both lunch and snack occasions. We have also expanded our successful Slow Kettle Crunch innovation with four varieties of Campbell's Red and White Crunch, including our iconic classic tomato soup with Goldfish toppings.

On our Pacific Foods business, we are launching additional plant-based products, including creamy oat milk soups and creamy plant-based protein broths. Finally, if you haven't tried the new Chunky Spicy Chicken Noodle, it's fantastic and brings variety to the critical at-home lunch occasion.

In addition to our relevant and consumer-driven innovation, another element of our winning soup strategy is a refresh of our Campbell's condensed soup. We are contemporizing the brand to better match our growing millennial consumer base, while improving the product and its shopability as we continue to support our positioning as the starting point for delicious meals.

We also have continued our journey of simplifying our ingredient lines and improving quality. It's always tricky when looking to evolve such an iconic design and product, but our new graphics and improved ingredient lines strike the right balance and have been met with a very positive customer and consumer response.

Let's now turn to Snacks. This quarter was the second-highest 13-week quarter of net sales for the Snacks division since the Snyder's-Lance acquisition. Organic net sales grew 1% over the prior-year quarter and 7% on a two-year basis. In-market performance declined only 1% year-over-year, but grew 11% on a two-year basis.

Turning to our Snacks power brands, which continue to fuel performance with in-market consumption growth of 2% this fiscal year and 15% on a two-year basis, driven by double-digit consumption growth in the majority of our brands. Compared to the prior year, we grew share on many of our power brands, most notably Cape Cod Potato Chips, Snack Factory Pretzel Crisps, Goldfish Crackers, and Late July Snacks. Compared to pre-COVID levels, household penetration remains elevated and repeat rates are higher on all power brands.

Turning to Goldfish, we delivered sustained share growth, increasing for a second quarter in a row by more than 1 point compared to this time last year. On a one- and two-year basis, Goldfish delivered strong results, including double-digit consumption growth, increased household penetration and higher repeat rates. This solid performance on Goldfish was due in part to the successful launch of limited-edition edition Goldfish Frank's RedHot crackers. Additionally, the reinstatement of promotions, improved performance on multi-packs, and an effective marketing campaign contributed to our strong results. We are excited to continue to introduce on-trend limited editions on Goldfish, with the launch this week of [ph] Goldfish Jalapeño Popper (00:13:17) and plans for additional innovation later this fiscal year.

Entering the fourth quarter amid rising inflation, labor shortages and some executional pressures, we better focused our agenda in the Snacks division, driving operational excellence and allocating additional resources throughout the supply chain network. We are very pleased with the speed and progress we have made to address the executional pressures we experienced in the third quarter. We head into fiscal 2022 with a stronger foundation and confidence we can continue our significant transformation on this important business.

On slide 17, we do expect a challenging environment in fiscal 2022 as COVID persists and inflation and labor availability remain highly volatile. However, we also anticipate our effective pricing actions, supply chain productivity programs, and cost savings initiatives to be significant offsets, resulting in an improvement in the second half of the fiscal year relative to the prior year and exiting fiscal 2022 with momentum as we continue to make progress on our strategic plan. Mick will provide more details on our fiscal 2022 outlook and assumptions in a moment.

With that, let me turn it over to Mick to discuss our fourth quarter and full-year results in more detail.

Mick J. Beekhuizen

Chief Financial Officer & Executive Vice President, Campbell Soup Co.

Thanks, Mark. Good morning, everyone.

Turning to slide 19, for the fourth quarter, organic net sales, which excludes the impact from the additional week and the impact of the sale of the Plum baby food and snacks business declined 4% as we cycled both the elevated demand in food purchases for at-home consumption and a partial retailer inventory recovery in the prior year.

Compared to the fourth quarter of fiscal 2019, which we view to be more meaningful given the COVID-19 impact to prior year, organic net sales increased 4% on a two-year CAGR.

Adjusted EBIT decreased 13% compared to prior year to \$267 million, driven by lower sales volume, including the impact of the additional week in the prior-year quarter and a lower adjusted gross margin partially offset by lower adjusted marketing and selling expenses and lower adjusted administrative expenses. Our adjusted EBIT margin was 14.3% compared to 14.6% in the prior year.

Adjusted EPS from continuing operations decreased \$0.08 or 13% versus prior year to \$0.55 per share, partially driven by the estimated \$0.04 contribution from the additional week in fiscal 2020.

For the full year, organic net sales, which excludes the impact from the additional week, divestitures, and the impact of currency were comparable to the prior year and grew 3% compared to fiscal 2019 on a two-year CAGR basis. Compared to prior year, Meals & Beverages organic net sales decreased 1% driven by declines in foodservice partially offset by growth in V8 beverages.

In Snacks, organic net sales were flat as gains in our salty snacks portfolio including Late July snacks and Snack Factory Pretzel Crisps and in Goldfish Crackers were offset by declines in Lance sandwich crackers and in partner brands within the Snyder's-Lance portfolio.

Full-year adjusted EBIT decreased 3% versus the prior year to \$1.4 billion. The decline reflected a lower adjusted gross margin and lower sales volume, including the impact of prior-year's additional week, partially offset by lower adjusted marketing and selling expenses and higher adjusted other income. Our marketing and selling expenses represented 9.6% of net sales compared to 10.9% last year.

Full-year 2021 adjusted EBIT margin was 16.6% compared to 16.7% in the prior year. Full-year adjusted EPS from continuing operations increased 1% to \$2.98 per share.

On the next slide, I'll break down our net sales performance for the fourth quarter. Organic net sales decreased 4% during the quarter, lapping an increase of 12% in the prior year quarter when the demand for at-home consumption remained elevated and retailers partially recovered on inventory. The organic net sales decline was driven by a 5-point headwind due to volume declines, partially offset by favorable price and sales allowances and lower promotional spending, which each drove a 1-point gain in the quarter.

The impact of one less week in the quarter subtracted 7 points and the recent sale of Plum subtracted 1 point. All-in, our reported net sales declined 11% from the prior year, stronger than anticipated as in-market demand remained elevated.

Turning to slide 22, our fourth quarter adjusted gross margin decreased by 420 basis points from 35.6% last year to 31.4% this year, which was generally consistent with our expectations.

Next, an operating leverage had a negative impact of approximately 70 basis points and 40 basis points, respectively, on gross margin as we continue to transition from last year's elevated demand. Net pricing drove 100-basis-point improvement due to lower levels of promotional spending in the quarter as well as favorable price and sales allowances, which do not yet reflect the price increases effective first quarter of fiscal 2022.

Inflation and other factors had a negative impact of 640 basis points with slightly more than half of the decline driven by cost inflation as overall input prices on the rate basis increased by approximately 5%. The remaining impact was driven by higher other supply chain costs largely due to last year's manufacturing cost efficiencies related to higher production levels to service the elevated demand as well as lower mark-to-market gain on outstanding commodity hedges, partially offset by lower COVID-19-related costs.

Our ongoing supply chain productivity program contributed 150 basis points to gross margin, partially offsetting these inflationary headwinds. Our cost-savings program, which is incremental to our ongoing supply chain productivity program, added 80 basis points to our gross margin.

Moving on to other operating items, adjusted marketing and selling expenses decreased \$91 million or 34% in the quarter on a year-over-year basis. This decrease was driven by lower advertising and consumer promotion expense, lower selling expenses, and lower marketing overhead costs. A&C declined 52%, reflecting our elevated pandemic-driven level of investment in the prior year to attract and retain new households. However, A&C was comparable to the fourth quarter of fiscal 2019. Overall, our adjusted marketing and selling expenses represented 9.3% of net sales during the quarter, a 330-basis point decrease compared to last year.

Adjusted administrative expenses decreased \$30 million or 18%, with approximately one-half of the decrease driven by the estimated impact of the additional week in the prior-year quarter. The balance of the decrease reflected lower general administrative costs, higher charitable contributions in the prior year, and benefits associated with our cost savings initiatives, partially offset by higher IT costs. Adjusted administrative expenses represented 7.4% of net sales during the quarter, a 60-basis-point decrease compared to last year.

Moving to the next slide, we have continued to successfully deliver against our multi-year enterprise cost-savings initiatives. This quarter, we achieved \$25 million in incremental year-over-year savings, which came in ahead of our expectations, resulting in full-year savings of \$80 million with the majority of the savings from the Snyder's-Lance integration. We remain on track to deliver our cumulative savings target of \$850 million by the end of fiscal 2022.

On slide 25, we are providing a total company adjusted EBIT bridge to summarize the key drivers of performance this quarter. As previously mentioned, adjusted EBIT declined by 13% as the net sales decline including the impact of the additional week in the prior-year quarter and the 420-basis-point gross margin contraction resulted in a \$84 million and \$77 million EBIT headwind, respectively.

Partially offsetting this was lower adjusted marketing and selling expenses, contributing 330 basis points to adjusted EBIT margin and lower adjusted administrative and R&D expenses contributing 50 basis points. The

estimated impact to EBIT from the additional week in fiscal 2020 was \$22 million. Overall, our adjusted EBIT margin decreased year-over-year by only 30 basis points to 14.3%.

The following chart breaks down our adjusted EPS change between our operating performance and below-the-line items. A \$0.10 impact of lower adjusted EBIT and a \$0.01 impact of higher adjusted taxes partially offset by a \$0.03 favorable impact from lower interest expense resulted in better-than-expected adjusted EPS of \$0.55, down \$0.08 from \$0.63 per share in the prior year; of which an estimated \$0.04 was driven by the additional week in fiscal 2020.

In Meals & Beverages, declines across US retail products including US soup, Prego pasta sauces, and Pace Mexican sauces led to a 9% decrease in fourth quarter organic net sales compared to the prior year. The decline was driven by volume decreases in US retail due to last year's partial retail inventory recovery and increased demand of food purchases for at-home consumption in the prior-year quarter. However, versus the comparable period in fiscal 2019, organic net sales increased 10%. In the fourth quarter of fiscal 2021, sales of US soups decreased 21%, 7 points of which were driven by the additional week in the prior year, while at the same time cycling a 52% increase in the prior-year quarter.

Operating earnings for Meals & Beverages decreased 30% to \$129 million. The decrease was primarily due to sales volume declines, including the additional week, and a lower gross margin partially offset by lower marketing and selling expenses as well as lower administrative expenses. The lower gross margin resulted from higher other supply chain costs, net of lower COVID-19-related costs, higher cost inflation, including higher freight costs and ingredient and packaging inflation, and unfavorable product mix partially offset by the benefits of supply chain productivity improvements.

Overall, within our Meals & Beverage (sic) [Meals & Beverages] (00:25:21) division, fourth quarter operating margin decreased year-over-year by 290 basis points to 15.2%.

Within Snacks, organic net sales increased 1% to \$1 billion, driven by volume gains in Goldfish Crackers and our salty snacks portfolio, including Snack Factory Pretzel Crisps, Snyder's of Hanover Pretzels, and Cape Cod Potato Chips, partially offset by declines in partner brands and fresh bakery. Favorable price and sales allowances and lower promotional spending also contributed to sales growth. Compared to the fourth quarter of fiscal 2019, Snacks organic net sales grew 7%.

Operating earnings for Snacks increased 7% for the quarter, driven by lower marketing and selling expenses, partially offset by sales volume declines including the impact of the additional week and a lower gross margin. The lower gross margin resulted from higher cost inflation and other supply chain costs, net of lower COVID-19-related costs, partially offset by the benefit of cost savings initiatives, supply chain productivity improvement, favorable price and sales allowances and lower promotional spending.

Overall, within our Snacks division, fourth quarter operating margin increased year-over-year by 170 basis points to 14.2%.

I'll now turn to cash flow and liquidity. Fiscal 2021 cash flow from operations decreased from \$1.4 billion in the prior year to \$1 billion, primarily due to changes in working capital, mostly from a significant increase in accounts payable in the prior year and lower accrued liabilities in the current year.

Our year-to-date cash for investing activities was reflective of the cash outlay for capital expenditures of \$275 million, which was slightly lower than the prior year driven by discontinued operations and the net proceeds from

the sale of Plum. Our year-to-date cash outflows for financing activities were \$1.7 billion, reflecting cash outlays due to dividends paid of \$439 million as we continue to focus on delivering meaningful return of cash to our shareholders. Additionally, we reduced our debt by \$1.2 billion.

We ended the year with cash and cash equivalents of \$69 million. In June, the board authorized a \$250 million anti-dilutive share repurchase program to offset the impact of dilution from shares issued under our stock compensation programs. As you saw in today's press release, we reinstated our strategic share repurchase program with a \$500 million program replacing the suspended \$1.5 billion program, which has been canceled. The company expects to fund the repurchases out of its existing cash flow generation.

Turning to slide 30, as covered in our press release, we're providing guidance for full-year fiscal 2022. We expect continued uncertainty around the duration and effects of the pandemic on industry-wide supply chain networks, resulting in accelerating inflationary pressures and a constrained labor market. We expect to partially mitigate these headwinds with well-executed pricing and planned productivity initiatives as well as our cost savings program.

First half margins, particularly in the first quarter, will continue to be impacted by transitional headwinds cycling prior year's elevated sales and scale efficiencies with comparisons easing in the second half of the fiscal year. We expect organic net sales to be minus 1% to plus 1%, adjusted EBIT of minus 8% to minus 5%, and adjusted EPS of minus 8% to minus 4% versus the fiscal 2021 results.

Fiscal 2021 results include a \$0.12 benefit for mark-to-market gains on outstanding commodity hedges and an approximate \$0.02 adjusted EPS contribution from Plum. For additional context on mark-to-market, please refer to today's Form 8-K. Importantly, when considering these items, the upper end of our fiscal 2022 adjusted EPS range is in line with fiscal 2021 performance.

As you see on slide 31, we expect core inflation for the year to be high-single digits with a more pronounced impact in the second half of fiscal 2022, which we plan to address with price increases and trade optimization, supply chain productivity improvements, and cost savings initiatives and a continued focus on discretionary spending across the organization.

Moving to additional assumptions, we expect ongoing supply chain productivity gains of approximately 2% to 3% for the year, excluding the benefit of our cost savings program. As previously mentioned, we expect continued progress on our cost savings program and expect to deliver an incremental \$45 million in fiscal 2022, keeping us on track to deliver \$850 million by the end of the fiscal year.

Additionally, we expect net interest expense of \$190 million to \$195 million and an adjusted effective tax rate of approximately 24%, which is largely in line with fiscal 2021.

While cognizant of our current operating environment, we expect to continue to invest in the business, targeting capital expenditures of approximately \$330 million, which includes carryover projects from fiscal 2021.

Additionally, we expect a net of adjusted administrative expenses and adjusted other income to increase as a percentage of net sales, reflecting the planned information technology investments and related costs and the cycling of lower administrative items in the prior year. All-in, we expect year-over-year operating margin improvement in the second half of the year.

Overall, as Mark said, we had a positive finish to the year. We are truly grateful to our teams and for their continued dedication and commitment as we head into fiscal 2022.

And with that, let me turn it over to Mark.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

Thanks, Mick. In closing, we feel good about how we landed fiscal 2021 amidst a difficult environment. We expect fiscal 2022 will be a complicated transitional year, but I'm confident that with our strong in-market momentum and the progress that we've made, we will successfully navigate through it. I look forward to sharing our view on how we intend to unlock the full growth and value potential of this fantastic company going forward at our Investor Day on December 14.

With that, we'll now turn it over to the operator to take your questions. Thank you.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Andrew Lazar of Barclays. Your line is open.

Andrew Lazar

Analyst, Barclays Capital, Inc.

Q

Great. Thanks very much for the question. I was hoping that we could get into maybe some of the key assumptions underpinning the full-year EPS range for fiscal 2022 in terms of assumptions around retention of new households, gross margin and SG&A, marketing spend in particular, really to just better assess the level of confidence and conservatism in the full-year forecast, particularly in light of the expected challenging 1Q and the higher inflation anticipated in the second half that could mute the second half recovery.

And I really ask this because I still get the feel from many investors sort of conversations that sort of the broader food group is maybe still not fully factoring in the full challenges ahead in guidance. So thank you.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Sure, yeah, so thanks, Andrew. That's a full question. So let me try to piece out a couple of different elements in there. First, why don't we talk a little bit about the basis of the assumptions for our guidance and how we're thinking about it? So first, let's talk a little bit about top line. I think – and part of the composition of the year is going to be a little bit of a tale of two of halves, because I do foresee a first half that's going to feel a little bit more like what we've been experiencing in the fourth quarter, while seeing sequential improvement as pricing comes into play, which is obviously a significant contributor as we go forward.

And then, in the back half, even though we do expect really driven on the back of packaging inflation as it relates to steel in particular as our contract turns on the calendar year. But even with that in mind, we're expecting improvement in the back half and overall momentum as we exit the year.

So I think when you think about top line next year, I do think that we see terrific momentum on our business today. We accelerated that momentum in Q4. We expect to continue to see positive in-market performance as we move forward. We are going to lap a pretty significant inventory replenishment that occurred primarily in the first quarter, but through into the second quarter, but I think the underlying health of the business we expect to continue to be positive. And, of course, sadly with COVID resurgence, I think some of the consumer dynamics that supported demand is likely going to be with us for a while longer.

I also am and continue to be very encouraged by the retention of households and really the sustainment of repeat levels that's very broad-based across our portfolio. Obviously, soup is one that we're watching very closely. And again, I don't think we've ever had, or at least not in recent history, a sustained period of progress so broadly across that part of our business. And with what we're bringing relative to innovation and other elements, we're feeling very good about that.

I do think a governor a little bit on this and a recognition of a little bit of then, well, why is your guidance the way it is, is because we also have to be mindful of what is a very significant pressure on labor that we're experiencing right now. And as I talked about that a little bit in the last quarter, I think we've seen that sustain through the fourth quarter and expect to still be wrestling with that, although I think we're taking some terrific actions and we're seeing some progress in some areas, arguably one of the toughest moments certainly that I've seen as it relates to labor. We're running about 2 times our normal vacancy rate, and as a translation into what that means, think about it as around somewhere in the neighborhood of 6% of our positions that are open either vacant or absent, and that is making it tougher to fully meet the demand.

So I think you sense or feel a little bit of that balance in our top line projections for the year. And I'll say this a couple of times, but if you go top of the range to bottom of the range, it kind of reflects how we do in that area, and so that's how we've thought about the top line.

When you get to margin, it's more distinctively a first half/second half discussion where really primarily in the first half but really more so even in the first quarter as we see pricing come into fruition, of course, inflation now as we leave the [ph] covered (00:37:57) positions of 2021 into 2022, we definitely are seeing higher inflation, but also feeling very good about the traction we're getting relative to the pricing actions that we put in place.

We've got good, strong productivity that we think will certainly help mitigate that as well. But certainly you're going to be in that transitional quarter of pricing coming in with higher inflation, and then as pricing is fully in place, we expect that to stabilize. As we did note, as steel prices have gone up significantly, we are expecting a tick-up in inflation in the back half. Not enough to offset the progress in the other areas and the comparable numbers that we're going to be lapping, but generally a little bit more mitigation, and that's – although we've got good programs, I think we've got a good plan for it. That's a pretty significant driver as we look through the balance of the year.

And then what we've been calling transitional costs which, again, in the fourth quarter were fairly consistent with what we saw in the third quarter, we expect that to be consistent in the first quarter and then begin to mitigate as we move forward from there.

So I do think as the year unfolds, I feel like we are assuming that as we both lap as well as see some relief in a couple of areas, while we get pricing fully in place, I think we have a fairly balanced approach. And not unlike what I was talking about around top line, I think the high-end and the low-end of the ranges of guidance are a little bit reflective of what variability could occur relative to where we're seeing inflation or coverage of that inflation to give you a sense of how we've thought about the year. And then, of course, as you drop to EPS, a little less difference between where EPS and EBIT is relative to what we see happening below the line.

So that – I don't know from a macro basis that's kind of the way we're thinking about the pieces. Maybe worth just going back to you to see if you've got any specific element you want to dive into a little bit more. I know this is a big question for the day, though.

Andrew Lazar

Analyst, Barclays Capital, Inc.

Q

Yeah, no, very helpful overall perspective. I appreciate it. I guess, really it's just more on marketing spend.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Oh, yeah.

Andrew Lazar

Analyst, Barclays Capital, Inc.

Q

It's certainly worth a lot of questions this morning.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Sure, sure.

Andrew Lazar

Analyst, Barclays Capital, Inc.

Q

Just to get a sense of how you see that playing out for the year.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah, so let me hit that one head-on, and maybe a good way to start with that is to give you a little bit of an explanation on Q4, because I know as you unpack the numbers – and again, I think we've foreshadowed this. But it's important to remember that in fourth quarter of 2020, we were in a position where we had a significant opportunity to double-down and invest in a more significant way, which, by the way, I'm very glad that we did because as I've said before, I think it did two things, gave us some momentum as we were solidifying relationships with a lot of new consumers, especially millennials, but it also gave us a great opportunity to learn and figure out what was working, what wasn't working, which helped us really dial into the most efficient or the highest returning spends.

As you flip the page to Q4 of 2021, you see a significant drop in marketing and selling. But underpinning that, what you have is essentially advertising and marketing that are at about the same level as Q4 2019. And as you've seen our results behind it – and, again, arguably always a little bit of a lag, but as you see our results relative to it, I think I feel great about the investment levels overall that we have.

And as you think about going into next year, I do think you may see a little bit of movement between the quarters. But overall from a marketing spend, I think we're at a good level. We may have a little bit of incremental investment in a couple of areas as we're adding innovation and working through the balance of the year, but it'll be a relatively stable investment year. We're not expecting marketing to be a source of opportunity to offset

inflation at all, right? We feel good about the levels we're at, and we want to make sure that we continue to refine the effectiveness of it, but we're committed to spending behind the businesses.

I think the last thing in the world we'd want to do is slow down the momentum that we're seeing in market, because it's certainly been for us a bit of an unprecedented period of really broad-based market share expansion and growth in key businesses. And so we know long term coming out of this thing that's what's going to matter most. And so we're going to be very guarded on it, even though I recognize on paper Q4 needs a little bit of context, but relative to how we're thinking about it going forward, we're expecting very stable investment.

Andrew Lazar

Analyst, Barclays Capital, Inc.

Q

Great. Thank you so much.

Operator: Your next question is from the line of Bryan Spillane from Bank of America. Your line is now open.

Bryan D. Spillane

Analyst, BofA Securities, Inc.

Q

Good morning, everyone.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Hey, Bryan.

Bryan D. Spillane

Analyst, BofA Securities, Inc.

Q

I just wanted to ask a follow-up on inflation. And I guess, just two points to cover. One, the high-single-digit, is that gross inflation or is that net of productivity? That's the first one.

Mick J. Beekhuizen

Chief Financial Officer & Executive Vice President, Campbell Soup Co.

A

That's gross, Bryan.

Bryan D. Spillane

Analyst, BofA Securities, Inc.

Q

Okay. Thanks. And then, the second one, just in terms of – trying to understand, we get a lot of questions about just how much that high-single-digit inflation expectation is – more or less locked in and how much is variable, right? Meaning it could swing up or down depending on conditions.

And I guess, one of the things that we've been hearing consistently through the month of August is we've touched base with companies is there's a lot of volatility in freight, even if you've got contracts. Sometimes it's not even – the truck doesn't even show up, let alone paying higher for the contract. So it seems like there's just a lot of volatility there. And then, anything resin-based, whether it's snack bags, bag liners, resin cups. And Ida probably complicates that a little bit, just given what it's doing to the refining complex. So anyway, just any context there in terms of...

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

Sure.

A

Bryan D. Spillane

Analyst, BofA Securities, Inc.

How much is fixed and how much could be variable? Thanks.

Q

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

I'll let Mick walk through kind of our coverage position and then I'll give you a little bit of qualitative view of it. I totally understand the question. And there's a little bit of mix here, I would say, of certainty and pragmatic forecast positions as we look at anticipating some variables that aren't necessarily locked down, but that I think we have a good sense of where we'll likely be.

A

Mick J. Beekhuizen

Chief Financial Officer & Executive Vice President, Campbell Soup Co.

Yeah. So if you look at it from a ingredient and pack perspective, at this point in time in the year, we are covered about two-thirds. So for the fiscal year next year, which is very typical and probably a little bit more front-end loaded coverage and then throughout the year you have a little bit more exposure, but about I would say two-thirds right now.

A

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

Yeah, and I'd say of that remaining third, as you know, we do have a pretty significant piece of this, which is relative to our cans as it relates to steel prices. And so what we're doing there is using a – and that gets really locked in more at the turn of the calendar year, although I do think we have a much clearer picture of where we are and are working through that as we sit here today.

A

But we've got an economic forecast that I think is generally consistent with where prices are today. You are right, resin is another area that we've seen some tick-up in cost as well, but I think we've covered that. And again, as we navigate through the balance of the year, I think you should expect us to continue to use the full tool bag to cover that, whether it's some combination of promotion and trade spending, some price pack architecture that we've worked on as well as the likelihood that there may be some places where we're coming back with a second wave of pricing designed to match very clearly in a very transparent way where we have some of these more explicit costs.

Now, I would say I think that will be much more surgical and specific than the pricing that we already have in place. But I do think as we look at the outlook, we see a mix of those variables in our plan to help us cover that.

Bryan D. Spillane

Analyst, BofA Securities, Inc.

Okay. Great. So just – so on the two-thirds/one-third, would that include logistics and freight as well?

Q

Mick J. Beekhuizen

Chief Financial Officer & Executive Vice President, Campbell Soup Co.

A

No, that's more related to the raw and packaging side of things. And then, we have a pretty decent chunk of our freights and logistics covered as well at this point in time with contracts that we've put in place.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah, it's definitely been volatile, you're right. In particular, I think we've seen more variability in areas like ocean freight, which was – had been a bit more stable and I think that's adding some volatility. But I think as we've – remember, you're also beginning to – as you go into 2022 begin to lap some of the volatility we were experiencing in fiscal 2021. And so your comparables do get a little bit easier as the year unfolds. But as we said, as we think about some of these transitional costs in the first half, that's partly why we see a little bit more of that headwind in the beginning of the year as we've tried to be prudent in making the appropriate estimate as it relates to where those costs are going to come in based on how we're seeing them today.

Bryan D. Spillane

Analyst, BofA Securities, Inc.

Q

Okay. Great. Thanks, Mark. Thanks, Mick.

Operator: Your next question is from the line of Ken Goldman from JPMorgan. Your line is now open.

Ken Goldman

Analyst, JPMorgan Securities LLC

Q

Thank you so much. Mark, last quarter when you were asked about pricing, you said a number of things. But one thing was that you were, I think, being thoughtful, strategic about reflecting critical price thresholds. I think you said the last thing you want is to shut down growth in share.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Right.

Ken Goldman

Analyst, JPMorgan Securities LLC

Q

And I think some people came away from that with the idea that you want to have some pricing but a little bit of a balanced approach. I'm just curious if your thoughts on that have evolved at all, right? Maybe you've seen elasticity a little bit lower than you [indiscernible] (00:49:00)...

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah

Ken Goldman

Analyst, JPMorgan Securities LLC

Q

...expected across food at home, maybe a little bit more inflation. So I'm just trying to get a sense, are you willing to be a little bit more aggressive on pricing just given some of the changes you've seen in the last few months, or do you still want to take that balanced approach to things?

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah, it's a great question. I think the first thing I would say is we definitely have been encouraged by what we're seeing early on as it relates to elasticity. And I think just the – perhaps the broad-based nature of the inflation is supporting perhaps a little lower than historical levels as it relates to what the elasticities are.

I also think that the strength of our brands right now and the momentum relative to businesses – a great example is our Swanson business, which, as we've returned supply into the marketplace, as you might remember, over the last year or so we'd lost a lot of share to lower-cost players, which I think for me was going to be an important test for that brand as we came back in the supply. And we've done extremely well on recovering the share that we had surrendered. And so I do think perhaps my view of where the boundaries are have expanded.

However, I do think there still are some boundaries. And so I think although it's giving us perhaps permission to reflect and continue to do the best job we can in juggling the pressure relative to inflation with wanting to protect the franchises and the brands longer term, I think we've got more room. And I think that although there will be some places where I think we still want to make the right smart trade-off for the long-term health, there's no question that I am feeling more confident in our ability to carry pricing than I might have initially as we were talking in the third quarter.

Ken Goldman

Analyst, JPMorgan Securities LLC

Q

Okay. Great. I'll let it go there. Thank you.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yep.

Operator: Your next question is from the line of Michael Lavery from Piper Sandler. Your line is now open.

Michael S. Lavery

Analyst, Piper Sandler & Co.

Q

I just want to drill into the third of the COGS that's exposed and specifically just understand where steel costs fit in. I know you touched on that's not finalized yet given just the calendared nature of that contract. Can you give me any sense of what assumptions you've made around it? And I assume the timing of finalizing those terms is consistent with prior years. But I don't think the magnitude of increase in the spot rates we're seeing is really similar.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah, yeah.

Michael S. Lavery

Analyst, Piper Sandler & Co.

Q

So just can you help us understand your planning position there?

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. We're doing a lot more of what I would say iterative collaboration with suppliers to understand more in real-time what they're seeing, so that we can plan appropriately. And so that implies is that as we've seen the increase occur, our outlook or our reflection on costs for the year includes that.

So we're not assuming some big relief on steel prices as we go through the year. I do think what we're going to want to do is probably work with suppliers to make sure that we're able to accommodate variability that may be occurring throughout the year. But I think from a planning standpoint, we've taken what I think is probably balanced to conservative in our position, but, of course, I think the volatility around in particular that cost has been quite significant as you know. But I think no one's banking on a reversal of that in the current forecast that we've got.

Michael S. Lavery

Analyst, Piper Sandler & Co.

Q

Okay. That's helpful. And just a quick follow-up on that. So it sounds like maybe in a way that's a bit unprecedented. You may have a much more flexible or variable contract and recognizing that sounds like it's still not finalized. Would we be right to think that that could go up or down?

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

It's a good – so I would just say, we're having, as you would expect, pretty meaningful conversations on that right now. And I think, again, philosophically, my perspective on this is predictability is really the priority. And so I would want to be careful and balanced in our ability to have certainty versus banking on something going a better direction.

So generally speaking, I'm going to want to know what we're dealing with. But I also think you're right. It is certainly somewhat of an unprecedented window. And so how do you think about where there are floors and ceilings to certain things may be a conversation that we continue to have. Hopefully that helps. But a little bit of a work-in-progress. But I think for now, assuming not a major change, I think, is probably a pretty prudent position.

Michael S. Lavery

Analyst, Piper Sandler & Co.

Q

Okay. Thanks so much.

Operator: Your next question is from the line of Robert Moskow from Credit Suisse. Your line is now open.

Robert Moskow

Analyst, Credit Suisse Securities (USA) LLC

Q

Hi. Thanks.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Hey, Rob.

Robert Moskow

Analyst, Credit Suisse Securities (USA) LLC

Q

Hi. Forgive me if I missed this, but have you said how much you think your pricing is going to be up in fiscal 2022? And is it also going to be back-half loaded? I'm just trying to do back-of-the-envelope math, because it looks like your internal inflation could be up as much as 10% in the back half of your year, which would mean your pricing would need to be up 5% or 6%.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah.

Robert Moskow

Analyst, Credit Suisse Securities (USA) LLC

Q

Am I in the right ballpark?

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yep. So you're in the right ballpark. I'd say a little bit lower as it relates to full-year and back-half inflation. And then on pricing, I think, as you take all of the variables into account, as we've said before, we're probably somewhere in the middle single-digits, in that area. Again, that obviously incorporates a variety of tools. But that's a pretty good assumption relative to where we are.

Robert Moskow

Analyst, Credit Suisse Securities (USA) LLC

Q

Okay. And my follow-up is that would imply a volume decline of the same amount. So how did you go about just determining what that volume decline would look like, and how do you factor in the possibility anyway that there will be declining food-at-home consumption as well?

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. I think we've looked at the – it is a set of variables that are in there. Again, we talked a little bit earlier about elasticities and a little bit of a growing confidence as it relates to our ability to navigate pricing perhaps without seeing some of the historical levels that would translate necessarily into the 5%.

I think you're working a little bit of a couple of different puzzle pieces together. One, we continue to imagine that we'll be investing. We're [ph] adding (00:57:10) innovation. We are on the flipside lapping some inventory replenishment that we saw in the beginning of last year. But I think the net of it is we do expect that to be – to result in a relatively flat year for top line. And that's reflected in our ranges.

And again, if we – remember, in the backdrop of all this, too, Rob, is a little bit of the labor situation and how we are going to be able to meet the level of demand and our ability to navigate that. I think we're a lot smarter, a lot more experienced in that now than we were perhaps a year-and-a-half ago when the journey began. But at the same time, again, I would say consistent with many of my peers, the labor challenges that we're seeing are certainly tougher than I ever remember. And I think the combination of those variables is how we're getting to the outlook.

But I don't think we're leaning out on any of those assumptions. So I think we've been fairly, like I said, pragmatic or balanced in our view. But I think there's going to be puts and takes. And so although I think you may see pressure downward as it relates to pricing, I think there is likely going to continue to be a catalyst for growth and progress as well. And, remember, some of our businesses, especially like our Snacks businesses have been pretty steady contributors of growth even through a little bit of the ups and downs as we've been navigating the pandemic. So I think there's going to be a mix of variables. But I think where we've kind of pegged this is probably about right.

Robert Moskow

Analyst, Credit Suisse Securities (USA) LLC

Q

Okay. Thank you so much.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yep. Thanks, Rob.

Operator: Your next question is from the line of David Palmer from Evercore. Your line is now open.

David Palmer

Analyst, Evercore ISI

Q

Just a follow-up to that question from Rob, pricing net of inflation through the year, how should that trend? It sounds like the second half is higher in inflation. Is pricing going to track with that or perhaps be accelerating more through the year such the relationship gets better for gross margins? And I have a quick follow-up.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. So the way I would think about plotting that course is gaining traction through Q1. So taking a little bit of time to get that fully reflected well in place as we go through Q2. I do think you'll see efforts for us to balance the step-up, if you will, in inflation as we get to the back half. But I do think you may see a little bit more pressure there. But remember, you've got several tailwinds as you're getting to the back half of the year. So I think the ability to still show that sequential progress in margins as we get to the back half of the year, even with those assumptions relative to inflation, I think, still will be positive.

David Palmer

Analyst, Evercore ISI

Q

And then, just a follow-up on biscuits and snacks, the roughly 13.5% segment margin, it seems like there would be some reasons for that to get better over time independent from this cost absorption year lapping the supply chain for one, plus all the improvements that you've been making. Could you perhaps help us squint and look through the inflation cycle and think about what could be happening there from a segment perspective basis on margins? Thanks.

Mark A. Clouse

President, Chief Executive Officer & Director, Campbell Soup Co.

A

Yeah. So that will be a prime topic of discussion when I see you guys in December. But here's what I can tell you. I continue to believe very strongly in the potential for us to improve margins on Snacks and for us to continue to

close or reduce the gap between where we are today and where we see ourselves relative to Snacks margin averages.

I think as time goes on, we continue to get better clarity and better understanding of the building blocks and the variables that will help us get there. And at the same time, I just would say that as you're looking at the here and now, if you think about where we started the journey to where we find ourselves, there's probably somewhere around 150 basis points of margin that I would call just transitional costs that are dampening some of the productivity and savings that we've been generating over the last several years.

Part of it is planned investment, so part of the offsets to the productivity has been – or the value capture has been planned investments in both the infrastructure and in marketing in some cases. But I think beyond that, we're probably looking at about 150, like I said, basis points that are dampening the baseline.

And then as we project forward, I think what you're going to see is a combination of building blocks that will help us build off of that adjusted base. And hopefully, in December, I'll be able to give you greater confidence in what those look like. I know we've been kind of dripping that out for several quarters now, but it'll be good to get to the December period. And I think I felt like it was important to keep playing through a little bit of this short-term transitional pressure as we get ready for that conversation. But hopefully that gives you a little bit of a sense of how we're looking at it and then how we're thinking about the future.

David Palmer

Analyst, Evercore ISI



That's great. Thank you.

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

Rebecca Gardy

Vice President-Investor Relations, Campbell Soup Co.

Great. Thank you. The IR team is available for follow-up discussions. And thank you for your time and interest in Campbell Soup Company.

Operator: And with that, this concludes today's conference call. Thank you for attending. You may now disconnect.

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