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CPB - Q3 2016 Campbell Soup Co Earnings Call

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OVERVIEW:

Co. reported 3Q16 as-reported net sales of $1.87b and adjusted EPS of $0.65. FY16 sales guidance remains unchanged at minus 1% to 0% and expects adjusted EPS to be $2.93-3.00.

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PRESENTATION

Operator

Good, ladies and gentlemen, and welcome to the Campbell Soup third-quarter 2016 earnings conference call.

(Operator Instructions)

As a reminder, today's conference call is being recorded. I would now like to turn the conference over to Mr. Ken Gosnell, Vice President of Investor Relations. Please go ahead, sir.

Ken Gosnell - *Campbell Soup Company - VP, IR*

Thank you, Candace. Good morning everyone. Welcome to the third-quarter earnings call for Campbell Soup's 2016.

With me here in New Jersey are Denise Morrison, President and CEO; Anthony DiSilvestro, CFO; and Blake MacMinn, Senior Manager of Investor Relations.

As usual we've created slides to accompany our presentation. You will find the slides posted on our website this morning at investor.campbellsoupcompany.com. This call is open to the media who participate in a listen-only mode.

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 2 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 these measures to the most directly comparable GAAP measure which is included in our appendix. One final item, before we begin our discussion of the quarter I'd like to cordially invite our sell side analysts and institutional investors to our Annual Investor Day at Campbell's World Headquarters.

RSVPs are required. All others are invited to join by webcast. This year's event will be held the afternoon of Wednesday, July 20.

We will include updates on our plans and key initiatives for the three operating divisions. We will also have time for interacting with our management team. More details to follow on this.

With that, let me turn it over to Denise.

Denise Morrison - *Campbell Soup Company - President & CEO*

Thank you, Ken. Good morning, everyone, and welcome to our third-quarter earnings call. Today, I'll share my perspective on our performance in the quarter and year to date.

As many of you are aware the consumer environment continues to be challenging in many of the markets where we have operations. In the US, consumer spending remains cautious. Shoppers are making more frequent trips than a year ago but they are purchasing less per trip.

As a result, consumer takeaway of total food and beverage has softened compared to both short- and longer-term comparisons. This has exerted top-line pressure on both retailers and manufacturers.

In other parts of the world economic conditions remain volatile. In the third quarter, our organic sales declined 2% which was below our expectations. Key factors that led to the decline include softer-than-expected soup category performance, weakness in V8 beverages and product shortages in our Bolthouse Farms carrot business.

I continue to be pleased with our adjusted gross margin expansion driven by supply chain productivity programs despite the negative impact of the weather on our Bolthouse Farms carrot business. Both our sales and the cost of carrots were adversely impacted by the poor growing conditions in California.

Cold, rainy weather from mid-December through mid-March reduced carrot yields across the industry. The decreased crop yield had a significant impact on our gross margin performance in the quarter. Both Anthony and I will discuss this later in the call.

Third-quarter adjusted EBIT declined but was better than we expected, reflecting improved gross margin performance. The decline in adjusted EBIT was due to higher levels of planned spending including the increased marketing investments as well as higher incentive compensation cost and investments in long-term innovation. We expected that our adjusted EBIT performance would taper in the second half as we realized the benefits of our cost savings earlier, cycled improved gross margin from a year ago and implemented our plans to increase marketing investment in the second half.

Now let me share my view on our segment performance for the quarter. Let's start with our largest division, Americas Simple Meals and Beverages. As a reminder we are managing this division for moderate growth consistent with the categories in which we operate and for margin expansion.

Organic sales declined by 2% in the quarter, predominantly driven by US soup and V8 beverages. Our ready-to-serve soup business was challenged by a number of the same factors we discussed last quarter: the mild winter weather which affected the entire category, the volume impact of our pricing actions and marketing execution on the Chunky brand.

We are realistic about these issues and have plans to address those things within our control for the next soup season. Namely, we intend to do a better job of driving demand, particularly for Chunky ready-to-serve soups. We will have a more robust marketing plan that fully leverages our NFL sponsorship.

We also recognize that we need to bring more excitement to the category and we have new on-trend product innovations planned for fiscal 2017. We will discuss these plans in greater detail at our Investor Day in July.

There were several bright spots within soup and Simple Meals. Sales of Swanson broth, Slow Kettle and Campbell's organic soup all grew. Also Campbell's condensed soup gained share.

Beyond soup, Prego continues to perform well, driven by strong merchandising and growth in white sauces. We also began shipping Prego Farmers Market, our new premium Italian sauce with a clean label. Additionally, we drove double-digit sales gains in Plum.

V8 beverages continue to struggle with sales declines in V8 Red, V-Fusion and V8 Splash. There was, however, some good news, particularly in the performance of V8 Veggie Blend and V8 +Energy.

In the short term, we've taken steps to address the performance of V8 Red and have increased both TV and digital advertising specific to the V8 Red brand. In the past, we've had success with advertising that reminds consumers of the benefits of V8. We're also building on the successful launch of V8 Veggie Blend with new varieties and expanding our V8 +Energy carbonated beverages into the grocery channel.

We recognize that these short-term actions are not the complete solution. That said, V8 is a great brand and we believe we have a solid platform to build upon going forward. We're in the process of finalizing our strategy and we'll discuss our longer-term plans to get this business back on track at Investor Day.

Overall, we feel good about how the Americas division is performing against its portfolio role year to date, especially its continued margin expansion. Clearly, we have some work to do in several key categories to generate demand for our products. We get it and we're on it.

Turning to Global Biscuits and Snacks, this division unifies our Pepperidge Farm, Arnott's and Kelsen businesses and its portfolio role is to manage growth while improving margins in both developed and developing markets. Pepperidge Farm delivered modest sales growth while we experienced some challenges in our Australia and China businesses.

The two main drivers of the sales decline were Kelsen in China and Arnott's sweet biscuits in Australia. First, China. Despite strong merchandising support and our improved marketing efforts heading into Chinese new year, sales were below expectations. We experienced short-term distribution challenges and faced strong competitive activity.

Let me explain. At the beginning of the fiscal year we made changes to our business model, adding salespeople and changing distributors. This new go-to-market model is designed to improve execution while enabling us to increase distribution into multiple cities in China over time.

However, our new distribution system did not have the same reach as in the past. In spite of the challenges we faced Kelsen consumer takeaway and share increased in our priority markets.

Going forward, we will need to supplement and expand our distributor network to increase our geographic reach. We're confident that we will get there and continue to believe in the long-term prospects for Kelsen in this important market.

In Asia-Pacific, excluding currency, sales of Arnott's biscuits were comparable to the prior year with growth in Indonesia offset by declines in Australia and New Zealand. In Australia we faced competitive pressure in the sweet biscuit category and experienced lower consumer takeaway on special varieties of Arnott's Tim Tam biscuits which had a negative impact on sales. On the plus side our savory biscuit business performed well and we're encouraged by the launch of our new and improved Arnott's shapes crackers.

While small our developing markets in Southeast Asia performed well. Excluding the impact of currency, we grew sales in both Indonesia and Malaysia double digits. As expected, the economic situation in Indonesia started to improve in the quarter.

Turning to North America, Pepperidge Farm cookies and crackers continued to perform well, driven mainly by Goldfish Crackers. Sales declined slightly in our fresh bakery business as we faced increased competition in the quarter.

Moving on to Campbell Fresh. C-Fresh is anchored by Bolthouse Farms and also includes Garden Fresh Gourmet and our refrigerated soup business. This division's portfolio role is to accelerate sales growth and expand into new package fresh categories.

The CPG portion of this business is the full force growth engine of the division. Reported segment sales increased 6% in the quarter. Excluding the impact of the Garden Fresh Gourmet acquisition sales declined 4%.

In the quarter, Bolthouse Farms was a tale of two cities. Solid performance in our CPG premium juice and salad dressing business was more than offset by significant declines in our farm business which consists of carrots and carrot ingredients.

As I mentioned earlier the carrot supply across the industry was negatively impacted by the adverse weather in California. This led to product shortages and product allocation to customers as we were unable to meet market demand. As a result, our carrot sales were down double digits in the quarter.

This weather pattern is irregular. As we looked back, the Bolthouse Farms carrot business experienced similar weather conditions in the winter of 2010 to 2011. Since then we've significantly diversified our winter crop into multiple growing regions in California, Arizona and Georgia.

Today we're much better equipped to respond and have reduced our recovery time. We're currently back in full supply with customers and don't anticipate any material sales impact going forward as we're now in the prime growing season in California.

Turning to the CPG side of Bolthouse Farms we're pleased with the 8% sales growth we delivered in the quarter. As expected, this growth was driven by distribution gains in our spring innovation. We added 14 new items across ultra and super premium beverages as well as salad dressings which increased double digits.

We're also pleased with the performance of 1915 by Bolthouse Farms, our ultra premium cold-pressed organic juice line. We achieved 50% ACV in less than 12 months, enabled by our investment in expanded capacity. Due to the success of our spring innovation sell-in we are well-positioned for the fourth quarter as we look ahead to fiscal 2017.

A quick word on our Garden Fresh Gourmet acquisition. From an integration standpoint, we continue to make progress on bringing the business into the Bolthouse Farms operations platform and we've expanded fresh salsa distribution. We remain very optimistic about the potential of this brand.

Before wrapping up, I'd like to share my thoughts on our year-to-date performance. Year to date, organic sales are down slightly 1% in what continues to be a very challenging consumer environment. We're clear eyed about the factors impacting our top line and the actions we need to take to address them.

We can and we must do better on driving profitable net sales growth. Looking ahead to the fourth quarter and next fiscal year, we expect to grow organic sales. Our year-to-date adjusted EBIT increase of plus 15% reflects our improved gross margin performance and the benefits of our $300 million cost-savings initiatives including our move to zero-based budgeting.

As we focus on finishing the fiscal year, I feel good about the progress we're making, how we've performed year to date and our outlook for the full year. This is reflected in our updated guidance which Anthony will discuss shortly.

We've made many important changes to Campbell: completely redesigning organization, setting up the Company by category versus geography and assigning each division a clear portfolio role. We continue to remain focused on strengthening our core business and expanding into faster growing spaces as we unleash the power of our purpose, real food that matters for life's moments.

Overall we're now better positioned to execute our strategies, invest in the areas of our business that hold the greatest profitable growth potential and increase shareholder value. We're proud of the progress we've made but we know we have more to do.

Now I will turn the call over to our Chief Financial Officer Anthony DiSilvestro.

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

Thanks, Denise, and good morning. Before getting into the details I wanted to give you my perspective on the third quarter. Organic sales in the quarter were below our expectations, reflecting softness in US soup, V8 beverages and the weather-related crop yield issue which negatively impacted our carrot sales and earnings.

We continue to make progress on adjusted gross margin. It improved by 40 basis points, better than expected, benefiting from our supply chain performance and moderating cost inflation despite the weather-related yield issue on carrots. The carrot issue negatively impacted sales by approximately $14 million and our adjusted gross margin by approximately 50 basis points or $0.02 per share.

We continue to make good progress on our cost savings initiative which delivered approximately $30 million savings in the third quarter with these savings impacting multiple P&L lines bringing the year to date total to $110 million. Program to date we are now at $195 million in cost savings.

With one quarter to go we are updating our guidance. We are holding the sales range, narrowing the adjusted EBIT range and raising the adjusted EPS range to reflect our current outlook for adjusted EBIT and a lower adjusted tax rate.

Now I will take you through the detailed results and guidance. For the third quarter, net sales on an as-reported basis declined 2% to $1.87 billion. Excluding currency and the impact of the Garden Fresh Gourmet acquisition organic net sales also declined 2% driven by lower volume.

Net price realization was comparable to the prior year with higher selling prices offset by increased trade promotions. Adjusted EBIT decreased 5% to $312 million, reflecting higher advertising and consumer promotion expenses, higher administrative expenses and lower volumes, partly offset by a higher gross margin percentage. Adjusted EPS decreased 2% to $0.65.

For the nine-month period net sales on an as-reported basis were down 2% while organic sales decreased 1% compared to the prior year. Adjusted EBIT of $1.214 billion and adjusted EPS of $2.48 both increased by 15%. Year-to-date earnings growth is being driven by our improved gross margin performance and benefits from our cost savings initiatives.

Breaking down our sales performance for the quarter, reported net sales and organic sales both declined 2% as the 1 point negative impact of currency translation was offset by the 1 point benefit from the acquisition of Garden Fresh Gourmet. Within organic sales, volume and mix subtracted 2 points which was primarily driven by declines in V8 beverages and soup within the Americas Simple Meals and Beverages segment as well as the lost carrot sales in Campbell Fresh. Higher selling prices contributed 1 point of sales growth while higher promotional spending subtracted 1 point.

Our adjusted gross margin percentage increased by 40 basis points to 37%, exceeding our expectations on overall supply chain performance despite the weather-related carrot issue. Cost inflation and other factors had a negative margin impact of 1.6 points, driven primarily by cost inflation which as a rate increased by approximately 1% and the increasing carrot cost previously discussed.

In aggregate our net price realization reduced adjusted gross margin by 20 basis points as higher promotional spending in the quarter to support US soups, Global Biscuits and Snacks and Bolthouse Farms beverages was mostly offset by list pricing actions previously taken across several businesses. Mix was slightly favorable, adding 10 basis points. Lastly, our supply chain productivity programs, which are incremental to our three-year cost savings program, contributed 210 basis points of margin improvement in the quarter.

Adjusted marketing and selling expenses increased 5% in the quarter, primarily due to higher advertising and consumer promotion expense. Advertising and consumer promotion expense increased 8% in the quarter, driven primarily by increases in Pepperidge Farm and V8 beverages. Adjusted administrative expenses increased 4%, primarily due to higher incentive compensation cost, inflation, increased cost to support long-term innovation and the acquisition of Garden Fresh Gourmet, partly offset by the benefits from cost savings initiatives.

For additional perspective on our performance, this chart breaks down our EPS change between our operating performance and below-the-line items. As you can see adjusted EPS decreased $0.01 compared with the prior year from $0.66 to $0.65 per share.

On a currency neutral basis, declines in adjusted EBIT had $0.03 negative impact on EPS. The impact from share repurchases under our strategic share repurchase program reduced our share count slightly but had no impact on EPS for the quarter. And net interest expense was comparable to prior-year levels.

Our adjusted tax rate for the quarter was 28.5%, down 3.1 points versus the prior year, primarily due to lower-than-expected taxes on foreign earnings, partly offset by the geographic mix of our earnings with a higher proportion of income in the US. The lower tax rate benefited EPS by $0.03. Currency had a $0.01 negative impact on EPS in the quarter, completing the bridge to $0.65 per share.

Now turning to our segment results. In Americas Simple Meals and Beverages organic sales decreased 2% to $999 million, driven by declines in soup and V8 beverages, partly offset by gains in Prego pasta sauces and Plum products. Operating earnings increased 1%, reflecting a higher gross margin percentage, driven by productivity improvement, partly offset by lower volumes and increased advertising expenses.

In total, US soup sales declined 5%, driven by category declines which as Denise mentioned were primarily impacted by warmer weather compared to the year-ago quarter, the impact from our pricing actions and marketing execution issues on Chunky. Although our pricing actions had a negative impact on volumes they have contributed to improved profitability.

Within US soup, RTS declined 13% and condensed declined 4%, partly offset by a 10% gain in Swanson broth. Estimated changes in retailer inventory levels did not meaningfully impact sales in the quarter. As we previously stated we will not be providing this subcategory sales performance beyond this fiscal year.

Here's a look at US wet soup category performance in our share results as measured by IRI. For the 52-week period ending May 1, 2016, the category as a whole declined 2.4%. Our sales and measured channels declined 3.5% with weakness in ready-to-serve and condensed soups partly offset by strength in broth.

Campbell had a 59% marketshare, a decline of 70 basis points. Private label grew share by 20 basis points finishing at 13%. All other branded players collectively had a share of 29%, up 50 basis points, reflecting share gains by smaller brands.

In Global Biscuits and Snacks, organic sales decreased 1% with declines in Kelsen partly offset by gains in Pepperidge Farm, Goldfish Crackers and soups and beverages in Australia. Excluding the negative impact of currency translation, sales of Arnott's biscuits were comparable to the prior year with gains in Indonesia offset by declines in sweet biscuit varieties in Australia. Operating earnings decreased 8%, primarily driven by higher incentive compensation costs and the negative impact of currency translation.

In the Campbell Fresh segment organic sales decreased 4% with declines in carrots partly offset by gains in Bolthouse Farms premium refrigerated beverages and salad dressings. Not included in organic results is our recent acquisition, Garden Fresh Gourmet, which contributed 10 points of sales growth to the segment.

Operating earnings declined 28%, driven by the higher carrot cost. Excluding the negative impact from the carrot issue and the acquisition, operating earnings for C-Fresh in the quarter would have increased significantly compared to the prior year. Despite the negative impact in the quarter year-to-date operating margins in C-Fresh have increased by 1 percentage point.

We had strong cash flow performance for the first nine months.

Cash from operations increased by $212 million to $1.183 billion driven by higher cash earnings and lower working capital requirements, especially in the area of inventory. Capital expenditures decreased $17 million to $225 million.

We continue to forecast CapEx of approximately $350 million for fiscal 2016. We paid dividends totaling $294 million, reflecting our current quarterly dividend rate of $0.312 per share. In aggregate, we repurchased $118 million of shares in the first nine months, $75 million of which were under our strategic share repurchase program.

The balance of the repurchases were made to offset dilution from equity-based compensation. Net debt declined by approximately $250 million as positive net cash flow generated by the business more than offset the impact of the $232 million acquisition of Garden Fresh Gourmet in the fourth quarter of 2015.

Now I'll review our 2016 outlook. Our sales guidance remains unchanged at minus 1% to 0% including a 1 point benefit from the acquisition of Garden Fresh Gourmet and a 2 point negative impact from currency translation. We are narrowing the range for adjusted EBIT which we now expect to grow 11% to 13%.

The year-over-year growth reflects the benefit of improved gross margin performance and the benefits from our cost-saving initiatives. We expect adjusted gross margin for the year to expand by approximately 175 to 200 basis points. We're increasing the adjusted EPS growth range to 11% to 13% or $2.93 to $3.00 per share, in line with EBIT growth.

Reflecting lower taxes on foreign earnings, we now expect the full-year adjusted tax rate to be approximately 32%. Against our cost savings program and consistent with our prior forecast we expect to deliver incremental savings in the range of $120 million to $140 million in 2016. Our 2018 annual savings target remains unchanged at $300 million.

That concludes my remarks. And now I will turn it back to Ken for the Q&A.

Ken Gosnell - *Campbell Soup Company - VP, IR*

Thanks, Anthony. We will now start our Q&A session.

Since we have limited time and out of fairness to other callers please ask only one question at a time. Okay, Candace.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) David Driscoll, Citi.

David Driscoll - *Citi Research - Analyst*

Great, thank you and good morning everyone. I just wanted to ask a question about the cost savings program. And I think the original expectation was to take half of the savings from the program and reinvest back in the business.

I think you guys have said a number of times that the savings is just coming faster than you originally anticipated, so maybe you're not at the pacing of putting a full half in. So is it right to think kind of going forward that the bulk of the 2017 savings should get reinvested back into the business, Denise, and this would number one, give you the fuel to reinvigorate the top line and then number two, would just kind of marry-up to that big picture comment about 50% reinvestment? Can you just comment on that?

Denise Morrison - *Campbell Soup Company - President & CEO*

Yes, the cost savings program is giving us the financial flexibility to reinvest back in the business to jumpstart top-line growth. We're being very choiceful about these investments and they are predominantly going after new product launches, such as you started to see in the third quarter our C-Fresh innovation, new Shapes in Australia, Prego Farmers Market and we're introducing a Plum Organic baby formula. And we will continue to support business products into next year and announce some more at our Investor Day.

A lot of the money is going to make sure that we have support of our key brands in line with the portfolio roles in each division. One thing that is new is we are channeling some of these dollars into longer-term innovation so that we make sure we have a robust pipeline in a state of readiness.

And then finally we're reinvesting it to build capabilities in things that we see coming into the industry such as digital and advanced analytics. So our intention is definitely to reinvest some of this money to drive top-line growth.

David Driscoll - *Citi Research - Analyst*

Just one follow-up. Did the pacing of the cost savings change at all, Anthony? Is it still, is your forecast for you the year still the same?

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

Yes, David. So in the last quarter we talked about $120 million to $140 million incremental for that for this year. We're at about $110 million year to date, so I've got a little bit to go. But we are certainly well ahead of our initial expectation both in the total amount and the timing.

And I think if I can get to the essence of your earlier question, with the target going up to $300 million and a significant amount of savings still to be achieved in fiscal 2017 and 2018 we will work and continue to target our long-term targets in terms of sales EBIT and EPS growth in fiscal 2017.

David Driscoll - *Citi Research - Analyst*

Thank you very much.

Operator

Andrew Lazar, Barclays

Andrew Lazar - *Barclays Capital - Analyst*

Good morning, everybody. I think the gross margin guidance for the year was I think up 175 basis points as of last quarter and Anthony you said now 175 to 200 for the year.

So I'm just trying to get a sense of what the key sort of change there was. I know volume in the quarter wasn't necessarily where you wanted it, so I'm trying to get a sense of what's driving that upside. Thank you.

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

Sure, Andrew, it is primarily coming out of our supply chain which just continues to operate extremely well. If you look across a number of metrics there all of our plant efficiencies are up, the plants are running more effectively than they did last year. And we continue to see significant savings in the area of transportation and warehousing and just to give you a couple of KPIs, our inter-plant shipments are down versus a year ago.

The amount of times we reach into the spot market for freight purchases is basically at zero compared to a significant amount last year. Our truck weights are up this year versus last year. Our miles traveled are down versus year ago and all of these things are just yielding really good results coming out of the supply chain and continue to exceed our expectations.

Andrew Lazar - *Barclays Capital - Analyst*

Great, thank you.

Operator

Bryan Spillane, Bank of America.

Evan Morris - *BofA Merrill Lynch - Analyst*

It's actually Evan on for Bryan. Just following on David's question just about reinvesting back, I guess I'm still struggling here. So promotional spending was up in the quarter, marketing was up in the quarter but organic sales were down.

I guess Denise you started out your prepared comments talking about the challenging operating environment. So I guess I'm still unsure how the planned reinvestment is going to drive the top line and I guess starting in 4Q. So within the context of the operating environment why should we expect sales to return and how I guess starting as early as the fourth quarter?

Denise Morrison - *Campbell Soup Company - President & CEO*

It seems like it's an equation but it isn't, because the places where we experienced the sales decline were not necessarily the places where we invested the A&C and the T. So let me explain. I talked about the sales decline being due to three factors: one being predominantly RTS soup, the second being V8 beverages and the third the unfortunate situation we had in carrots with the shortage of organic carrots.

The investments that we made was on different things. So we invested A&C, advertising and consumer, in our Global Biscuits and Snacks business against Shapes in Australia which worked, Tim Tams in Australia which didn't work and our cookies and bakery business in Goldfish and Pepperidge Farm which did work. We invested advertising and consumer in V8 but we focused it on the Veggie Blends and that works but what we realized is that we had to put more emphasis going forward on V8 Red and we are course correcting there.

We also spent predominantly promotion spending on our Campbell Fresh new product launches. And that is going incredibly well. And then finally, we spent money against Prego and Simple Meals which also had a very good quarter.

So we do believe in the investment of A&C in this business. And with trade spending it was up against the Arnott's business that I just talked about, Goldfish and C-Fresh new products. On a year-to-date basis trade spending is down 5% and about 0.3 points versus year ago on a rate basis.

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

Just to add to add, there's a couple of issues that we believe are temporal in the quarter and a bit unusual. One is certainly the impact of the carrot yield issue which impacted our sales by almost a point negatively and also the category declines in soup as Denise mentioned earlier impacted by the warmer weather.

If you exclude those two items sales would have been flat compared to a year ago. So we think a couple of things happening in this quarter and going to repeat themselves.

Evan Morris - *BofA Merrill Lynch - Analyst*

That's helpful. So it sounds like some of the things were more category specific. And as you are thinking about the challenging operating environment, particularly in the US, are you seeing just broader levels of promotional activity?

Do you expect that going forward or again is just really where your spending is really more category-specific behind some of these brands? They need a little help?

Denise Morrison - *Campbell Soup Company - President & CEO*

We are in a situation in the industry, particularly in center store categories, where growth is hard-won and it's very competitive. And we expect that to continue.

Operator

Rob Moskow, Credit Suisse.

Rob Moskow - *Credit Suisse - Analyst*

Hi, thank you very much. One question is on the fourth-quarter implied guidance. It's a very wide range, Anthony.

I wanted to know why so wide, what are the factors that could go either way. Second are you giving fiscal 2017 and 2018 guidance today? I thought I heard you say that you expect to be on your long-term algorithm, maybe I misunderstood. Thanks.

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

Yes, so just to clarify that I said we aspire to achieve our long-term target in fiscal 2017. We will give more specific guidance when we get to our fourth-quarter call.

In terms of the implied range, it does obviously have a $0.07 delta in the fourth quarter. I think for perspective, and we've had a bit of challenge forecasting our year as you know taking the guidance up a couple of times already, we've just gone through massive change here at the Company, probably the largest transformational change in the Company's history in terms of reorganizing into three divisions, addressing spans and layers and voluntary headcount reduction, involuntary headcount reduction, the adoption of zero-based budgeting and changing many of the policies we have at the Company, changing our operating model and forming an integrated global services function. And given the amount of change it's just been really difficult or more difficult than usual to forecast.

So we're just giving ourselves a little bit of latitude here in the fourth quarter in terms of where we're going to come out. Some of the variability will likely be in gross margin. That 25 basis point range can take you from the top of the EPS range to the bottom.

Cost savings could be a little bit variable. We feel pretty confident we'll see some organic growth at the top line.

Operator

Chris Growe, Stifel.

Chris Growe - *Stifel Nicolaus - Analyst*

Hi, good morning. I just wanted to ask a question in relation to the marketshare declines in soup. And I know we've talked about soup generally and you have talked about soup generally, and some of the challenges particularly in ready-to-serve.

But condensed was down as well and that's the part I was surprised by. And I guess in relation to that I'm just trying to understand when you think about the incremental marketing, and for example in this quarter in promotional spending, and as you look ahead is it designed to try and narrow that marketshare gap in soup? Is it something you're trying to work against here in the short run and we could see some improvement in early next soup season?

Denise Morrison - *Campbell Soup Company - President & CEO*

Yes, as I look at it, for the quarter condensed was down but on a year-to-date basis condensed is actually up in share. Broth was up 10% for the quarter and pretty flat but gaining consumption and gaining share.

Our issue, really, is RTS. And I look at myself in the mirror on this one, it was bad execution on Chunky. We had lack of compelling advertising.

We didn't leverage our partnership well with the NFL. We had a label issue in the first quarter which cost us sales.

And the good news is that these are all execution issues within our control and we are actively addressing them. So I believe that if we keep supporting this core business and we get our act together on Chunky we'll be in pretty good shape going forward.

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

Just to add to that, one of the things we did in RTS is we made a pretty significant move on our promoted price points which we hadn't done in over a decade and we felt that it was really important for the category and for our profitability to make that move. We knew it would have a negative impact on volume. We're seeing that come through and we knew it would have a negative impact on our share performance and again we are seeing that come through as well.

Denise Morrison - *Campbell Soup Company - President & CEO*

I think also, too, you'll start to see more of a steady stream of innovation in the core soup category.

Chris Growe - *Stifel Nicolaus - Analyst*

Just on that point, Anthony, in terms of the raising price points, is that something you can sustain or is competition not allowing for that in ready-to-serve?

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

We intend to sustain that.

Chris Growe - *Stifel Nicolaus - Analyst*

Okay, thank you.

Operator

Ken Goldman, JPMorgan.

Ken Goldman - *JPMorgan - Analyst*

Hi, good morning everyone. Anthony, you said that excluding I guess the carrot and weather-generated soup issues sales would have been flat this quarter. I get it, that makes sense.

But it still implies like a two-year stack number of minus 1%. So I guess when I'm looking at your four-quarter guidance are you looking for, and just to confirm and if you said this already I apologize, but just to confirm are you looking for it seems to me like at least positive, 2%-ish roughly on an organic basis against what will be kind of a positive come.

So I'm just curious A, is my math right on that? And B, just go back on some of the questions that people have asked already, doesn't that sort of imply a little bit of a sequential improvement in run rate organic growth excluding some of the items you talked about?

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

Sure. Let me give you a little more detail on the facts. So before I get to the organic just building up to the sales in the fourth quarter, so year-to-date currency has been minus 2 points, in the fourth quarter it's going to be more modest, likely a minus 1.

The other thing is the impact on Garden Fresh Gourmet in our fourth quarter which is seasonally low it will probably have closer to a 2 point positive impact than a 1 point positive impact. So net-net that's a positive 1 and if we can do plus 1 in organic that gets it to a plus 2.

So that's kind of what we're thinking about. So it doesn't have to be a 2 organic, just has to be a 1 to get to the bottom end of that range.

Denise Morrison - *Campbell Soup Company - President & CEO*

And we have the benefit of some new products that we just started shipping in the quarter.

Ken Goldman - *JPMorgan - Analyst*

That's very helpful. Thank you, guys.

Operator

Jason English, Goldman Sachs.

Jason English - *Goldman Sachs - Analyst*

Hey, good morning folks. Real quick clarification question, Denise, I think you said trade spend is down around 5% year to date but when we look at the promotional lines in terms of sales drivers it's neutral year to date. So what else is driving the offset to trade spend reductions?

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

I don't remember you saying that. I think in dollar terms trade spend is fairly comparable to prior year. And I think on a rate basis, let me look that up real quick here, relatively flat on a total Company on a rate basis.

Jason English - *Goldman Sachs - Analyst*

Okay, then let's delve a little bit deeper in there. I know you guys set up a revenue management team early this year. It's probably still early innings but there was an objective coming in to be able to find some opportunities, some efficiencies there and reverse what's been sort of a long-term trend of promotions being a drag on sales.

Where do we stand? You sort of had progress out of the gate, we've kind of unwound some of that progress. Have you found sort of your efforts on that front to be futile or as we think forward is there still opportunity and can we expect to see it start to bear fruit as we go into next year?

Denise Morrison - *Campbell Soup Company - President & CEO*

We look at trade as part of net price realization. And to that end, with our creation of the integrated global services we have beefed up our revenue management group and are working on advancing our analytics to be able to do a couple of things: first of all, make sure that we are optimizing our pricing; second, make sure that we are maximizing the return on our trade investment as we continue to work through programs on our brands with customers.

If we do see opportunities to be more effective and efficient, we will do so. I'm as much for working with the numerator as the denominator.

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

Let me just add to that. We are seeing benefits from our revenue management initiative. It led to the pricing actions we took on soup last year.

It led to the changes in promoted price points. It led to the pricing on Prego. It led to some of the pricing in some of our other businesses around the world and we will continue to focus on it going forward.

I think just one more comment in terms of the quarter. A lot of what you're seeing in the quarter is a result of timing. A lot of the cost savings came in the first half and we had re-phased some of the marketing out of the first half and into the second half, so I think it's probably appropriate to judge us on our year-to-date results which we feel really good about.

Jason English - *Goldman Sachs - Analyst*

Makes sense. Thanks a lot. I will pass it on.

Operator

John Baumgartner, Wells Fargo.

John Baumgartner - *Wells Fargo Securities, LLC - Analyst*

Good morning, thanks for the question. Denise, I'd like to ask about promo spend in baking and snacking.

It's been a segment where you had reduced promo during the first half of the year and it looks as though you reversed course this quarter. How much of this is really just a comparison issue against the pacing of last year versus maybe relative to deeper change of course going forward?

Denise Morrison - *Campbell Soup Company - President & CEO*

Well, I think that promotion spend is really important. In the baking and snacking area we've been -- in the United States we've been really focused on a couple of brands, one being Goldfish which has performed very well, and the other being Milano. I do think that there will be a cadence that's worked throughout the year, but promotion is an important part of the mix for that particular business for impulse sales.

John Baumgartner - *Wells Fargo Securities, LLC - Analyst*

Okay, and then just in terms of the volume prospects there, you were lapping some pretty hard comps earlier this year. But how do you think about the base Pepperidge business going into fiscal 2017 and kind of on the competitor front as well?

Denise Morrison - *Campbell Soup Company - President & CEO*

I'm not sure I understand the question. Could you clarify?

John Baumgartner - *Wells Fargo Securities, LLC - Analyst*

Yes, in terms of the volume prospects for the segment going forward, I think you had lapped some pretty hard comps in the first half of this year with depressed volumes. But as you get into easier comps back half of this year, some of the innovation rolling out in Goldfish, how are you feeling about the volume prospects in the business as you move into fiscal 2017?

Denise Morrison - *Campbell Soup Company - President & CEO*

And you are talking specifically about Baking and Snacking?

John Baumgartner - *Wells Fargo Securities, LLC - Analyst*

Yes.

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

Pepperidge Farm.

Denise Morrison - *Campbell Soup Company - President & CEO*

Pepperidge Farm. Oh, I think that you'll get a glimpse of their plans in July, but it's shaping up to be a pretty strong plan. We will continue to work on, like I said, on Goldfish and also on the cookie business as well. I don't know what else I can say about that at this point.

John Baumgartner - *Wells Fargo Securities, LLC - Analyst*

Thank you.

Operator

Michael Lavery, CLSA.

Michael Lavery - *CLSA - Analyst*

Good morning. I just was hoping I'd get a little more color on the top line and some of your outlook there. You mentioned just in general the cautious consumer spending and soft trends. But can you dissect that a little bit, because certainly there's categories and companies that have very strong top-line growth and there's minimum wage increases and low-end wages that are on the upswing.

And so is that more big food or center store specific or do you think that's a macro issue? And then related to that on pricing, obviously Wal-Mart had very strong numbers driven by price investments and presumably they're funding a good bit of that. But are seeing pushback on pricing from the trade and are you able to get pricing through or how do you see the outlook there?

Denise Morrison - *Campbell Soup Company - President & CEO*

Well, we're seeing in terms of performance in the marketplace, the shelf stable businesses we're tracking them -- the shelf stable businesses are pretty mixed with more robust sales growth in the Simple Meals area and then there are a number of categories who are below the average. And so refrigerated is doing a lot better so the fresh business and frozen more categories are down than up.

And so we have done an analysis on trips and like I said there's more frequent trips being made versus a year ago but shoppers are buying less overall units. And that seems to be across all of the categories.

So we are noticing that behavior. We don't really talk about specific customers but I think in general we've been able to execute our pricing in the marketplace.

Michael Lavery - *CLSA - Analyst*

I didn't expect color on Wal-Mart in particular, but just pushback from the trade in general, you're seeing that pricing outlook environment looks constant?

Denise Morrison - *Campbell Soup Company - President & CEO*

Well it's just been such a long time since we've increased prices on our products that we were able to establish them in the marketplace. And we're still promoting the products and working with the customer of their plans.

Michael Lavery - *CLSA - Analyst*

And when you say across categories are you referring to grocery specifically or do you get a read through things like channel shifting say even to Amazon or other nontraditional channels?

Denise Morrison - *Campbell Soup Company - President & CEO*

Yes, we track about 38 categories in Simple Meals and across the center store refrigerated and also in frozen so that we can get an idea for the cadence of the industry and how we're performing within that cadence.

Michael Lavery - *CLSA - Analyst*

But that's where? In grocery?

Denise Morrison - *Campbell Soup Company - President & CEO*

Yes, well it would be MULO.

Michael Lavery - *CLSA - Analyst*

Okay, thanks a lot.

Operator

Alexia Howard, Bernstein.

Alexia Howard - *Bernstein - Analyst*

Good morning, everyone. So can I just ask I guess two questions. It seems to me there are some smaller challenger brands that are doing quite well in soups at the moment, if I think about Imagine obviously from a much smaller base or even in the refrigerated section Panera's (inaudible) soup.

How is that informing your innovation pipeline? And also how is that affecting your relationship with the retailer where you've mentioned analytics a couple of times improving, is there a sense that the retailers might be starting to tone down the category captain role in favor of just using analytical algorithms to set the shelf space now that these smaller brands do seem to be where the growth is?

Denise Morrison - *Campbell Soup Company - President & CEO*

It's absolutely true and I think it's absolutely true in a lot of categories that smaller challenger brands are growing faster off of a smaller base. And in the soup category there are a couple that are growing faster again but they are much smaller.

We also have some smaller parts of the soup business that are growing faster. So for example, Slow Kettle was up 9% in the quarter and is up 50% year to date in consumption and also Campbell Organic is of 41% in the quarter and then a relatively new brand to the category, this would be two examples.

And there's a couple of others as well. And our refrigerated soup continues to perform as expected, up 2%. So we are seeing it and we believe that we need to participate in that.

Alexia Howard - *Bernstein - Analyst*

And then on the category captain role?

Denise Morrison - *Campbell Soup Company - President & CEO*

I'm sorry, I didn't understand what you mean by the role.

Alexia Howard - *Bernstein - Analyst*

The idea that the traditional category captain role that you've obviously played in soups might be being replaced by just more analysis of the scanner data, particularly by the retailers I mean. And maybe the retailers are less dependent on you. How is that playing out?

Denise Morrison - *Campbell Soup Company - President & CEO*

We have just about 59% marketshare in the soup category. We believe that we have to play in all segments and we are doing so and we are working with retailers on the best way to manage the whole category. So that has not changed.

Alexia Howard - *Bernstein - Analyst*

Okay, thank you very much. I will pass it on.

Operator

Matthew Grainger, Morgan Stanley.

Matthew Grainger - *Morgan Stanley - Analyst*

Hi, good morning everybody. Denise and Anthony, I just wanted to ask about the M&A landscape. I know this comes up a lot, but you've always talked about being open to acquisitions but approaching it generally with strategic and financial discipline.

So I guess with that as the starting point, can you just give us an update on the scale of opportunities that you're thinking about, whether the focus is more on bolt-ons and higher growth adjacencies or whether you'd be open to larger, more transformational things that allow you to more aggressively use the balance sheet now that you've delevered a bit?

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

As we've said before we have a very disciplined approach to M&A. Anything we do obviously needs to be strategically compelling and has to be financially attractive. And I'd say we're open to both, both the idea of smaller bolt-on acquisitions that build upon our platform, for example, in Campbell Fresh or to expand geographically in Biscuits and Snacks.

The overall list is relatively short. We continue to work it and develop relationships with companies around the world and in the US.

On the other hand, we do have the financial flexibility to do something a bit larger. So I think it depends more on the attractiveness of the opportunity first and foremost from a strategic and a financial perspective and again open to varying sizes.

Matthew Grainger - *Morgan Stanley - Analyst*

Okay. And are there any constraints that we should keep in mind just in terms of leverage or willingness to use equity?

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

So you don't have a specific limit in mind? I think the Bolthouse Farms acquisition is a good example where we took the debt to EBITDA up between a little over 3.5 times and paid that down pretty quick. So again we have quite a bit of financial flexibility and would use it for the right opportunity.

Matthew Grainger - *Morgan Stanley - Analyst*

Thank you, Anthony.

Operator

Jonathan Feeney, Athlos Research.

Jonathan Feeney - *Athlos Research - Analyst*

Thanks very much. I just had a question on the interplay between pricing and volume in Americas Simple Meals.

When you looked over the past two years it looks like pricing is up about 2.5 points while volume is down about 7.5. That's just for this third quarter, just stack the past two years. And I'm wondering, I know costs are down a fair amount in that time and so I understand you've done a great job holding share in those categories, we're mainly talking soup here, but what role do you think higher pricing across the category is having in hurting the volumes in soup?

I know you maybe had some weather but on a two-year basis that's not really been the case, some weather this year. And going forward now that costs are rising a little bit more, is that going to change your philosophy in thinking about how you'd balance price and volume in Americas Simple Meals? Thanks very much.

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

I will start. I would say on the cost side you said they are rising a little bit more. We're seeing moderating cost inflation at least in the back half of this year and probably into the next year and that takes a little bit of pressure off the pricing algorithm.

Our objective is to expand gross margins through a combination of net pricing and productivity in excess of cost inflation. So as cost inflation moderates that gives us a little more flexibility. There's no question that if you look back over the last couple of years we have moved up some of our net pricing both list and promoted in an effort to improve the profitability of the soup business and in fact we've done that quite successfully.

Now that does have a short-term impact on volume. Longer term we like to think that in the broad basket of things that will drive consumer demand, things like product quality and innovation and robust marketing, are all part of that algorithm to drive volume growth over the long term.

Jonathan Feeney - *Athlos Research - Analyst*

Okay, just to clarify, you're saying costs are up over the past two years in Americas Simple Meals?

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

Looking backwards or looking forwards?

Jonathan Feeney - *Athlos Research - Analyst*

Versus fiscal 2014, looking right now, you're saying costs, input costs are up over that period of time for you?

Anthony DiSilvestro - *Campbell Soup Company - SVP & CFO*

Yes.

Jonathan Feeney - *Athlos Research - Analyst*

Okay, I will follow up off-line about that. Thank you.

Operator

This concludes our question-and-answer session for today. I'd like to turn the conference back over to Mr. Gosnell for closing remarks.

Ken Gosnell - *Campbell Soup Company - VP, IR*

Thanks, Candace. We thank everyone for joining our third-quarter earnings call and webcast.

A full replay will be available about two hours after the call concludes by going online or calling 1-703-925-2533. The access code is 1670608.

You have until June 3 at midnight at which point we move our earning calls strictly to the website, investor.campbellsoupcompany.com under news and events. If you have any further questions, please call me, Ken Gosnell, 856-342-6081. If you are a reporter with questions please call Carla Burigatto, Director of External communications at 856-342-3737.

This concludes today's program. Thank you.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program and you may all disconnect. Have a great day, everyone.
