THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

CPB - Q2 2017 Campbell Soup Co Earnings Call

EVENT DATE/TIME: FEBRUARY 17, 2017 / 2:00PM GMT

OVERVIEW:

Co. reported 2Q17 as-reported net sales of $2.171b and adjusted EPS of $0.91. Expects 2017 sales to grow by zero to 1%.

THOMSON REUTERS

CORPORATE PARTICIPANTS

Ken Gosnell *Campbell Soup Company - VP Finance Strategy & IR*

Denise Morrison *Campbell Soup Company - President, CEO*

Anthony DiSilvestro *Campbell Soup Company - SVP, CFO*

CONFERENCE CALL PARTICIPANTS

Ken Goldman *JPMorgan - Analyst*

Chris Growe *Stifel Nicolaus - Analyst*

Bryan Spillane *BofA Merrill Lynch - Analyst*

Andrew Lazar *Barclays Capital - Analyst*

Robert Moskow *Credit Suisse - Analyst*

Cornell Burnette *Citi Research - Analyst*

Alexia Howard *Bernstein - Analyst*

Michael Lavery *CLSA Limited - Analyst*

Rob Dickerson *Deutsche Bank - Analyst*

PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Campbell Soup second-quarter 2017 earnings call. (Operator Instructions). As a reminder, this conference call is being recorded.

I would now like to turn the conference over to Ken Gosnell, Vice President, Finance Strategy and Investor Relations. Please go ahead.

Ken Gosnell - *Campbell Soup Company - VP Finance Strategy & IR*

Thank you, Candace. Good morning, everyone. Welcome to the second-quarter earnings call for Campbell Soup's fiscal 2017. With me here in New Jersey are Denise Morrison, President and CEO, and Anthony DiSilvestro, CFO.

As usual, we've created slides to accompany our earnings 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 listen-only mode.

Today, we'll 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 two 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 would like to cordially invite our interested shareholders, investors, and members of the media, and consumers to listen to and view our investor presentation at CAGNY, which will be video webcast live on Wednesday, February 22, at 10:30 a.m. from Boca Raton. A replay of the video and copies of the materials will also be available afterward on our website. If you are attending the event, there will be a Campbell's-sponsored luncheon immediately after our presentation.

And 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 second-quarter earnings call. Today, I'll share my perspective on our performance in the quarter and provide my view on our progress across each of our three divisions. Anthony will follow with a detailed financial review.

Let's be real. I am not satisfied with our overall sales performance in the quarter. Organic sales declined 2%, with the most prominent declines in Campbell Fresh and V-8 shelf-stable beverages. Additionally, in the Campbell Fresh segment we recorded non-cash impairment charges related to the carrot and carrot ingredient and Garden Fresh Gourmet reporting units. Anthony will walk you through additional details during his comments.

There were some bright spots in the quarter, such as growth in US soup, simple meals, Pepperidge Farm snacks, and fresh soup. Our adjusted gross margin increased 70 basis points, all of which was achieved by Americas Simple Meals and Beverages. Another positive result was the overdelivery of our cost-savings initiatives. As we announced this morning, we now expect to achieve our cost-savings target a year ahead of schedule.

Based on the success of the program to date and the identification of additional savings opportunities, we're raising our cost-savings target from $300 million by the end of fiscal 2018 to $450 million by the end of fiscal 2020.

Looking at the first half, organic sales declined 1%, adjusted EBIT was comparable to a year ago, and adjusted earnings per share increased 5%. With the exception of improved sales performance in second half of the year -- excuse me, the expectation of improved sales performance in the second half of the year, we reaffirmed our full-year guidance this morning.

Now, let me offer my perspective on the performance of each of our three divisions in the quarter. Let's start with the Campbell Fresh division. The CPG segment of C Fresh includes Bolthouse Farms beverages and salad dressings; Garden Fresh gourmet salsa, hummus, dips, and chips; and fresh soups. The Farms portion of the portfolio includes carrots and carrot ingredients.

The division's performance was below our expectations this quarter. C Fresh is an important strategic business for Campbell's and we remain confident in the growth potential of the packaged fresh category as consumer preferences continue to shift towards fresher and healthier foods. In fact, nearly 80% of consumers, including younger ones, are trying to eat more fresh foods. These consumers not only believe that fresh foods are cleaner, healthier, and less processed, but that they also taste better.

We acquired two packaged fresh businesses, Bolthouse Farms and Garden Fresh Gourmet, with brands that resonate with consumers as a way to develop a long-term growth platform in packaged fresh CPG. The perimeter categories in which we compete are still growing significantly faster than the traditional center store. While category growth rates have slowed somewhat, we still believe we can build a profitable growth business leveraging these brands, capabilities, and our scale.

However, our performance over the last year in fresh has been disappointing. The reasons vary by business, which I'll explain in more detail in a minute. We've made a number of changes to address this. Most notably, we replaced the leadership team and appointed a long-time Campbell executive, Ed Carolan, as the President of C Fresh in November. I'm confident in this new seasoned leadership team, which includes Campbell executives, some newcomers to the Company, and key members of the Bolthouse Farms team, who possess CPG and agriculture experience, as well as insight into both the operations and the entrepreneurial culture of the organization.

It's taking longer than we originally expected to regain carrot customers following last year's quality and customer service issues and to rebuild capacity following the Protein PLUS beverage recall. As a result, we no longer expect C Fresh to grow this fiscal year.

Over the last quarter, our new team has conducted an extensive strategic review to assess the potential of this business going forward. This has helped us update our expectations about future growth based on the fresh categories in which we compete, and it's leading to a sharpened strategy.

As a result of this work and our current-year performance, we've lowered our expectations for both long-term sales and earnings.

We've learned some tough lessons over the last several quarters and we're applying them. As a first step, we've started to integrate the supply chain to re-engineer the Fresh operating model. We're building a stronger foundation under the Campbell Fresh business, leveraging Campbell's scale and expertise, realizing synergies, and building capacity and capabilities in order to return it to profitable growth.

Let me now take each piece of the business individually and explain. Let's start with Farms and specifically the carrot business. After experiencing quality issues last year due to execution and poor weather conditions in California, we've restored our carrot quality. We've demonstrated this improved quality to customers and are working hard to earn back the lost business over time. Our previous assumptions were too aggressive and regaining share is turning out to be more difficult than planned.

In the current quarter, our carrot business faced additional challenges, again related to the weather. In California, rainfall in December and January was significantly higher than normal. This hampered our ability to harvest fields and lowered our yields on the carrots we did harvest. This negatively impacted both sales and earnings in the quarter.

Now let's turn to beverages. Last June, we voluntarily recalled our Protein PLUS beverages for quality reasons. At that time, we had a 47% market share of the protein segment and Protein PLUS was one of our strongest performing SKUs.

The good news is that consumers are seeking out protein products and our Protein PLUS consumer is a loyal shopper. As previously discussed, we implemented enhanced processes to improve the quality standards, resulting in fabulous product quality, albeit at reduced runtimes. Since then, we've steadily improved, but have not returned to pre-recall production levels.

We've added an additional beverage line in our Bakersfield plant that we expect to be fully operational in April. As we discussed last quarter, we're seeking additional ways to increase capacity. We've had challenges in finding copackers that meet our quality standards, but we've recently qualified a copacker and expect to be significantly expanding our capacity by the summer.

We're able to fulfill shelf stock and service levels back to the high 90s. In addition, we're seeing increases in velocity each period as we regain distribution. While we're selling everything we make, we have insufficient capacity to fulfill merchandising demand across the full range of our beverages. Our plan is to relaunch Protein PLUS merchandising in the fourth quarter of fiscal 2017, when we expect to have sufficient supply.

Due to our continued capacity constraints, we don't expect our beverage business to return to growth until the fourth quarter.

Meanwhile, we remain focused on driving innovation across the Bolthouse Farms CPG range, including dressings, spreads, and super-premium and ultra-premium beverages. We recently extended our salad dressing line with a range of four new organic varieties. We also launched a test of Bolthouse Farms MAIO, a new line of refrigerated yogurt-based spreads made with clean ingredients and fewer calories than mayonnaise. Later this year, we plan to expand our line of 1915 by Bolthouse Farms organic cold-pressed juice and launch Bolthouse Farms Plant Protein Milk, a higher protein alternative to almond milk. Customer response to this new product has been very positive.

Now, turning to Garden Fresh Gourmet. As a reminder, the business has four product groups, salsa, which is over half of the business; hummus; dips and chips; and fresh soup. The business offers a combination of branded and private-label products.

The traits that made Garden Fresh Gourmet an attractive acquisition target, a small, authentic brand with a compelling story, have also presented some obstacles. When we acquired it in June 2015, Garden Fresh Gourmet was a small operation with approximately $100 million in revenue and very little infrastructure. The integration into the Bolthouse Farms fresh platform proved to be challenging. The truth is we expected more, faster, in multiple areas of this business, including financial systems, information technology, and supply-chain integration, as well as increased marketplace distribution.

Let me explain the issues we've encountered and what we're doing to fix them. Garden Fresh Gourmet branded salsa is growing strongly in consumption and we've regained a major customer beginning January 2017. Private-label salsa is below expectations, due to lost distribution with two customers. We've recently regained one of these customers and active negotiations are underway with the second.

Throughout its short history, Garden Fresh Gourmet salsa was largely a Midwestern brand. Our plan called for the rapid distribution expansion of branded salsa beyond the Midwest. However, it became apparent that we did not have the differentiated recipes and taste profiles that would be accepted by consumers in other parts of the country.

We now have the recipes to pursue expanded distribution. In January, we launched branded Garden Fresh Gourmet salsa in new packaging with new regional recipes. We're focused on key distribution and velocity-building initiatives. For example, in January we gained national distribution for new branded organic salsa with a major customer.

Today, our ACV distribution of Garden Fresh branded salsa is only 37%, so we have a lot of runway to match the 70% ACV levels of our other C Fresh CPG brands. We're optimistic that we can get there with delicious high-quality ingredients, product and packaging innovation, improved marketing and sales support, and expansion into organic and regional flavors.

I do want to take a moment to highlight a positive result in the division. We've made significant gains in our fresh soup business, which continues to grow at high single digits, driven by both private-label and branded soup. We've recently introduced a new Garden Fresh Gourmet soup, which has been well received by customers, and initial velocity is encouraging. We're also testing Souplicity, a new artisanal cold-pressed soup.

We continue to expect to grow the Garden Fresh Gourmet business profitably, but it will take longer than we originally planned.

Overall, we've learned several important lessons from these two packaged fresh acquisitions and we're applying them going forward. First, establishing a leadership team with diverse skills and experience early on is critical. Our new team combines the talents and capabilities of Campbell and Bolthouse leaders. They're actively integrating C-Fresh into Campbell and taking advantage of our full suite of resources. We're now blending the best of small, while also benefiting from the best of big.

Second, fresh food is more perishable and therefore more fragile. At Campbell, we're obsessed with safety and quality. We put safety above all else, because if we don't, nothing else matters. Meeting Campbell's quality standards in C-Fresh required significant investment and the right resources.

Third, there is no roof over the carrot fields. We've experienced everything from severe drought to record rainfall. This business has been much more volatile than expected. We've set up more diversified growing regions, but we have more to do to strengthen our agricultural operations.

Fourth, the Fresh supply chain presents an opportunity for productivity improvement and optimization. We believe we can and will drive margin improvement in these businesses over time.

Finally, we have both the ability and the desire to build strong brands and drive growth in response to increasing consumer demand for fresh foods.

To recap, we are facing some challenges in C Fresh beyond what we originally realized. Our new leadership team is making progress and addressing them. To be clear, we remain committed to the packaged fresh category and to M&A in the fresh space as we build this growth platform.

Now let's turn to Global Biscuits and Snacks. As a reminder, this division includes our Pepperidge Farm, Arnott's, and Kelsen businesses. The organic sales decline in the division was mainly a result of the performance of Kelsen and our decision to forgo some less profitable business with a large US customer. Additionally, the depreciation of the Chinese RMB negatively impacted our sales in China.

Stepping back and looking at the underlying trends in Kelsen China, we feel good about our execution during the important Chinese New Year period. As we've discussed previously, we've been working to expand our distribution capabilities in China and we've been adding new subdistributors to extend our reach. Our sell-in for Chinese New Year went according to plan and promotion displays were consistently strong across all store formats. We're still awaiting consumer takeaway.

Turning to the US, Pepperidge Farm delivered modest sales growth behind the continued strong performance of Goldfish crackers, as well as cookies, especially the Milano brand. Goldfish growth benefited from channel gains leveraging multiple pack sizes and innovative new products. Goldfish made with organic wheat is also attracting new millennial families to the brand. However, our fresh bakery sales declined as a result of intensified competitive activity, especially in the sandwich bread category.

As a reminder, we're cycling double-digit operating earnings growth this quarter and we expect a strong back half as this division delivers both sales and margin growth.

Looking ahead, we're focused on driving continued growth in Goldfish and increasing innovation in cookies, especially the upcoming launch of our new Farmhouse line in April. These cookies leverage Pepperidge Farm's baking heritage and deliver against our real food philosophy with great taste and simple ingredients. We'll also continue to build the national rollout of Tim Tam Biscuits in the US, following its recent launch in January.

Rounding out the portfolio is our largest division, Americas Simple Meals and Beverages. I'm encouraged by the sales gains in soup and simple meals; however, this was offset by the lackluster performance of V-8 shelf-stable beverages. I continue to be pleased with the Americas gross margin expansion, driven by the performance of our supply-chain team. Once again, the division delivered strong operating earnings growth of plus 8%.

Our US soup business grew in the quarter. I'm especially pleased with our ready-to-serve brands. Sales increased double digits in ready to serve. Chunky continued to lead the way, behind our improved execution and strong integrated marketing that fully leveraged our NFL sponsorship. We're also delighted with the launch of our new Well Yes! clean label soup, which hit shelves in December. Retailer acceptance has been exceptional, with ACV already around 75% and most customers taking all nine varieties.

We activated our marketing plans in January and initial consumer response has been positive. It's early days, but we feel good about our overall execution and how we got out of the starting blocks with this brand.

Sales declines in our broth business were the result of increased competitive activity, mainly from private-label offerings. As discussed last quarter, we had strong holiday merchandising plans for our broth business, and we were pleased with the execution of that program. However, we did not achieve the consumer takeaway that we expected, as a result of an extremely competitive holiday period.

In the short term, we will be sharpening our promotional activity and marketing message to drive improved performance in the back half of the year, while we continue to develop longer-term plans to improve our competitiveness and differentiation in this important category.

Looking ahead on US Soup, we have robust marketing plans in the third quarter and we continue to expect to deliver modest growth in soup this fiscal year.

The shelf-stable beverage category remains sluggish and our portfolio continues to be challenged. As I've previously stated, V8 will not grow this year. Let me reframe the conversation to provide a little more context. In the quarter, consumption grew in two-thirds of our business, V8 100% Vegetable Juice, Veggie Blends, and our V8 +Energy franchise. All of them are on trend and leverage our heritage in vegetable nutrition. Importantly, we continued to see improved consumption trends in V8 100% Vegetable Juice following our increased marketing support.

The remaining one-third of the portfolio, consisting of V8 V-Fusion and V8 Splash, is declining, partly due to category-wide consumer concerns about sugar. Despite the overall sales declines, the business continues to focus on productivity initiatives, which are contributing to the overall gross margin expansion in the division.

Big picture, the Americas Simple Meals and Beverages division continues to be on track to deliver modest sales growth and margin expansion.

In closing, I want to stress again that I am not satisfied with our overall sales results this quarter. I own it, and we have plans in place to improve our performance in the second half, deliver our cost savings, invest back in our business, and deliver our full-year guidance.

It's really important to keep sight of the long-term progress we've made in transforming this Company in a difficult operating environment, our continued gross margin expansion, how we've strengthened our core business while expanding into faster-growing spaces, the investments we're making in real food as a result of our purpose, how we've diversified our portfolio with innovation and acquisitions, and the leaner, more agile, and more cost-effective Company we've become as a result of our successful cost-savings initiatives. I look forward to seeing many of you next week at CAGNY where we will focus on Campbell's long-term strategic growth platforms.

Now let me turn the call over to our Chief Financial Officer, Anthony DiSilvestro.

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

Thanks, Denise, and good morning.

Before reviewing our results, I wanted to give you my perspective on the quarter. We are disappointed with our sales performance. Declines in C-Fresh and V8 were the primary drivers. On the positive side, we grew US Soup sales, and Pepperidge Farms snacks had a strong quarter. Sales results were below our expectations, primarily due to C Fresh as the recovery on beverages and carrots is taking longer than previously anticipated, with the additional impact of heavy rains in the quarter, which had a 40 basis-point negative impact on adjusted gross margin.

Sales and earnings in Garden Fresh Gourmet also declined, and as Denise mentioned, we recorded non-cash impairment charges totaling $0.58 per share in our GAAP results related to our Campbell Fresh segment.

Despite the negative impact from C-Fresh, I'm pleased with our overall adjusted gross margin performance, which was up 70 basis points. We're increasing our cost-savings estimate for 2017 to $85 million, which will put us at our targeted $300 million by the end of fiscal 2017, a year earlier than anticipated.

Based on the overall success of the program and the identification of additional savings opportunities, we are increasing our cost-savings target to $450 million by the end of fiscal 2020.

While adjusted EPS increased to $0.91 in the quarter, we recognize that the increase is due to a decline in our adjusted tax rate. We're also lapping a very strong second quarter last year, in which adjusted EPS increased 23%.

Lastly, with the increased cost savings and lower cost inflation offsetting incremental marketing investment and lower earnings in C-Fresh, we are reaffirming our fiscal 2017 guidance.

Now, I'll review our results in more detail. For the second quarter, net sales on an as-reported basis declined by 1% to $2.171 billion. Excluding the favorable impact of currency translation, organic net sales declined 2%, driven by lower volume and higher promotional spending. And as I said earlier, the majority of this decline is driven by lower volumes in Campbell Fresh and our V8 juice business.

Adjusted EBIT declined 1% to $417 million, reflecting the impact of lower sales and higher marketing and selling expenses, partly offset by a higher adjusted gross margin percentage. Benefiting from a lower tax rate, adjusted EPS increased 5% or $0.04 to $0.91 per share. For the first half, as reported and organic net sales both declined by 1% compared to the prior year. Adjusted EBIT was comparable to prior year and adjusted EPS of $1.92 was up 5%.

Breaking down our sales performance for the quarter, organic sales declined 2%, driven by a one-point decline from volume and mix driven primarily by Campbell Fresh and a one-point decline from higher promotional spending. In Americas Simple Meals and Beverages, promotional spending rates were up on Swanson Broth, V8, and in Canada to hold promoted prices following our list price increase. Promotional spending is also up in our Arnott's business in the Asia-Pacific region. Although it rounds to zero on the chart, we did have a slightly positive impact from currency translation, principally the Australian dollar, bringing the change in our as-reported sales to minus 1%.

Our adjusted gross margin increased 70 basis points in the quarter. First, cost inflation and other factors had a negative impact of 80 basis points. On a rate basis, cost inflation was about 1%, and in Campbell Fresh, increased costs reflect the impact of heavy rains on carrot yields, lower beverage operating efficiencies, and the overall impact of lower volumes. These negative drivers were partly offset by the benefits from our cost-savings initiatives.

Increased promotional spending had a negative impact of 60 basis points, reflecting the drivers I previously discussed. List price increases had a slightly positive impact of 10 basis points, driven primarily by list price actions taken by our retail business in Canada. Mix was slightly favorable, adding 20 basis points, reflecting the sales declines in our lower-margin C-Fresh segment.

Lastly, our supply-chain productivity programs, which are incremental to our cost-savings programs, contributed 180 basis points of margin improvement in the quarter. All in, our gross margin percentage increased 70 basis points to 38%.

Adjusted marketing and selling expenses increased 5% in the quarter, primarily due to higher advertising and consumer promotion expenses as we reinvest in our brand. The increase in advertising was primarily driven by our investment to support the launch of Well Yes! soups and higher levels of support on V8 juices and Prego pasta sauce. Adjusted administrative expenses declined 3%, reflecting lower incentive compensation compared to the year-ago quarter, partly offset by higher benefit-related costs and investment in long-term innovations.

For additional perspective on our performance, this chart breaks down our EPS change between our operating performance and below-the-line items. Adjusted EPS increased $0.04, from $0.87 in the prior-year quarter to $0.91 per share in the current quarter. On a currency-neutral basis, decreases in adjusted EBIT had a $0.02 impact on EPS. Share repurchases lowered our share count, adding $0.01 benefit.

Our adjusted tax rate for the quarter decreased by 3.8 points to 27.8%, contributing $0.05 to EPS growth. We benefited from a favorable timing impact related to the impairment charge. This will reverse in the second half and bring us to our forecasted full-year adjusted tax rate, which remains at approximately 32%. Interest was comparable to prior year as the impact of higher rates was offset by a lower debt level. Currency translation also had no impact on EPS, completing the bridge to $0.91 per share.

Now, turning to our segment results. In Americas Simple Meals and Beverages, organic sales fell 1% to $1.231 billion, as declines in V8 beverages were mostly offset by gains in soups, Prego pasta sauces, and Plum products.

Sales of US soups increased 1%, reflecting double-digit gains in ready-to-serve soups, driven by growth in Chunky and the launch of Well Yes! mostly offset by declines in broth and condensed soups. The strong performance in Chunky reflects our improved execution, including better advertising and successful new items. The launch of Well Yes! is progressing well, with strong customer acceptance and supported with a robust marketing plan.

Operating earnings increased 8%, driven by a higher gross margin percentage which benefited from supply-chain productivity improvements, partly offset by increased advertising and consumer promotion expenses.

Here's a look at US wet soup category performance and our share results, as measured by IRI. For the 52-week period ending January 29, 2017, the category as a whole declined 1.2%. Our sales in measured channels declined 1%. Campbell had a 58.8% market share for the 52-week period, with a share gain of 10 basis points. Private label grew share by 70 basis points, finishing at 13.5%. All other branded players collectively had a share of about 28%, declining 80 basis points.

In Global Biscuits and Snacks, organic sales decreased 1%, driven by declines in Kelsen in the US and Arnott's Biscuits, partly offset by gains in Pepperidge Farm. Pepperidge Farm sales increased as growth in crackers, primarily Goldfish, and cookies was partly offset by declines in fresh bakery and frozen products. Operating earnings declined 4% to $135 million, reflecting a lower growth margin percentage as higher promotional spending and supply-chain costs were partly offset by productivity improvements.

In the Campbell Fresh segment, organic sales declined 8%, driven by lower sales of carrots, Bolthouse Farms beverages, and Garden Fresh Gourmet, partly offset by gains in refrigerated soups. Operating earnings declined by $24 million to a loss of $3 million, reflecting higher carrot and beverage production costs, as well as from lower sales volumes.

As Denise mentioned, the recovery from both the market-share losses on carrots and the beverage capacity constraints will take longer than originally anticipated.

The performance of Garden Fresh Gourmet is also short of expectations. We now expect that, for the full year, segment sales and earnings will decline in 2017.

The performance of Campbell Fresh is below our previous expectations. We have a new management team in place and it undertook a strategic review, which informed our future plans and expectations for growth. Based on current performance and lower forecasted sales and earnings growth, we recognized non-cash impairment charges of $0.45 per share on the carrot and ingredients business and $0.13 per share on Garden Fresh Gourmet. The other two reporting units in this segment, Bolthouse Farms CPG, which includes beverages and salad dressings, and the fresh soup unit, were not affected.

Cash flow from operations was $667 million, compared to $754 million generated in the first half of last year. The lower level of cash flow generated reflects higher working capital requirements, primarily driven by changes in accrued liabilities related to taxes and incentive compensation. Capital expenditures declined $34 million to $119 million. We have lowered our CapEx forecast by $25 million to approximately $325 million for fiscal 2017. The reduction is primarily related to the timing of projects in global biscuits and snacks.

We paid dividends totaling $207 million, reflecting our increased quarterly dividend rate of $0.35 per share. In aggregate, we repurchased $234 million of shares, $200 million of which were under our strategic share repurchase program as we've increased our level of share repurchases. The balance was made to offset dilution from equity-based compensation.

Net debt declined by $357 million compared to year-ago levels, as cash from operations over the last four quarters was well in excess of capital expenditures, dividends, and share repurchases.

We are very pleased with the progress made on our cost-savings program. With our new forecast for incremental savings of $85 million in 2017, we now expect to reach our $300 million target by the end of this fiscal year. We have generated savings by reducing layers of management and increasing spans of control. We have changed our operating model by creating an integrated global services organization and we are implementing a comprehensive zero-based budgeting process, which is delivering savings across many simple and more complex cost categories.

While our current initiatives will generate in excess of $300 million in savings, we believe there are additional areas of opportunity which in aggregate will get us to our new target of $450 million. First, we will look for opportunities to further optimize our supply-chain network, primarily in North America. Second, we will continue to evolve our operating model to drive efficiencies and to focus resources on our most significant growth opportunities. And lastly, we will more fully integrate our recent acquisitions to generate cost synergies and improve our effectiveness by leveraging both our enterprise scale and capabilities.

Now, I'll review our 2017 guidance, which remains unchanged from what we first announced last September. We expect sales to grow by zero to 1%, adjusted EBIT to grow by 1% to 4%, and adjusted EPS to grow by 2% to 5%. This guidance assumes, based on current exchange rates, that the impact from currency translation will be nominal. On our cost-savings program, we now project full-year savings of approximately $85 million, compared to our prior forecast of $50 million.

Additional cost savings and lower-than-expected cost inflation, about 1.5% compared to the prior forecast of about 2%, are offsetting incremental investments in marketing and the softness in Campbell Fresh. We expect our adjusted gross margin percentage to end the year at about 38%, almost a point better than last year.

Our EPS guidance reflects an effective tax rate of approximately 32%, which is unchanged, and the favorable impact of anticipated share repurchases over the course of the year. In terms of timing, we expect the majority of our year to go earnings growth to come in the fourth quarter.

That concludes my remarks, and now I'll turn it back to Ken for the Q&A.

Ken Gosnell - *Campbell Soup Company - VP Finance Strategy & IR*

Okay. Thanks, Anthony. We will now start our Q&A session. Since we have limited time, out of fairness to the other callers, please ask only one question at a time. Okay, Candace?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Ken Goldman, JPMorgan.

Ken Goldman - *JPMorgan - Analyst*

One of your competitors in biscuits obviously made a fairly major announcement last week. Does that announcement in any way, in terms of distribution, make you rethink your distribution or is it sort of full steam ahead? Pepperidge has an incredible, obviously, DSD system set up. Just curious if that made you guys go back and rethink things in any way or if it's too early to tell. Any help there would be very appreciated.

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

I'll take that one. Thanks, Ken. We're very pleased with the performance of Pepperidge Farm, particularly in the snacks business, some really good growth. And our distribution system, DSD distribution system, is different in that it is a network of independent contractors, so that's really how we've assessed it.

Ken Goldman - *JPMorgan - Analyst*

Right. So is the takeaway, then, that because it's different and because you're pleased with it, we on the outside should interpret it as it's unlikely to see major changes at any point in the near term?

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

Yes. We're continuing to run our play.

Operator

Chris Growe, Stifel.

Chris Growe - *Stifel Nicolaus - Analyst*

I just wanted to ask you, in relation to the soup business, you had -- the Well Yes! soup product looks to be doing quite well and you had some pipeline fill in the quarter. Did that have an effect on soup sales in the quarter? And if I can ask related to that, with the Well Yes! launch, did we see marketing spending go up in relation to that product in the quarter? And should we expect that going forward in the second half of the year?

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

Yes, a couple of things, so it's a good question. The impact of Well Yes! on soup sales in the quarter was about two points, so it did have a benefit to our net sales number. And as you can imagine, most of that is obviously in retail inventory. Some did pull through, but not a lot.

But as we look at the total inventory on soup, there has been some reduction in other areas, so when you put it all together, changes in retail or inventories in soup did not have an impact on our overall soup sales results in the quarter, but there was some puts and takes in there.

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

We're very happy with the introduction of Well Yes! There were -- great retail support, 75% ACV distribution, displays everywhere, but we won't get a read on the consumer takeaway, really, until this quarter.

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

To your second question, this is going to be supported with a fairly comprehensive and robust marketing program, so you can expect, obviously, an increase in marketing behind this in the third quarter.

Operator

Bryan Spillane, Bank of America.

Bryan Spillane - *BofA Merrill Lynch - Analyst*

I guess just a question about the prospective cost savings going forward, and I guess as you are thinking about balancing how much reinvestment versus how much you'll use to support earnings growth, not trying to get you to be specific in terms of earnings targets in the out year, but can you sort of maybe give us some color in terms of how you might be thinking about that balance going forward with this new savings versus maybe the way you approached the $300 million you've achieved so far?

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

I think, Bryan, the way to think about it is against the incremental $150 million, probably about half will go back in terms of reinvestment.

So we've talked about this support before. We need to increase the support behind some of our key brands. We need to continue to support new product launches, like we're doing with Well Yes! and Prego's Farmer's Market and Tim Tams in the US and Goldfish with the organic wheat, so we need to continue to do that. We'll continue to invest behind our real food initiatives, removing artificial colors and ingredients, removing BPA for our can liners. We'll also continue to invest in longer-term innovation, things like Habit and the Acre venture funds, and we'll look to make investments to improve our capabilities in areas like digital and e-commerce. So we have a fairly well-balanced plan in terms of what to do with those cost savings.

Operator

Andrew Lazar, Barclays.

Andrew Lazar - *Barclays Capital - Analyst*

A quick question on C Fresh, as your commentary was -- it seems you are going to be further integrating that division to take advantage, I guess, of the broader scale and scope and capabilities of the larger Campbell organization. I guess my question is we've all seen, I think, a lot of examples over time, whether it be the Kashis of the world where the larger company sort of brings the smaller, more entrepreneurial growthier entity in a bigger way into more of the mainstream organization, and I guess we've seen a number of examples where that's led maybe those more entrepreneurial businesses to maybe lose some of that progressive nutrition swagger or some of what made them special and growthier in the first place.

So I guess I'm just trying to get a sense. It's a little broad, but I guess how do you guard against taking advantage of what the organization can bring to that and not lose what it is that you bought in those businesses to begin with?

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

Andrew, it is the key question, and when I talk about getting the best of small and the best of big, I'm really serious about -- what we have done is really delineated those parts of the business that really need to be separate and differentiated for the consumer and the customer. And that's all of the marketing and the R&D and insights.

We have this model that we've used very successfully with our Plum Organics baby food business. By keeping those parts of the business separate, that maintains that entrepreneurial culture; however being able to leverage the scale of Campbell's, particularly in areas of the supply chain and in operations, where we have resources that can be used to make them much more effective and efficient and, even more important, achieve scale, because these are typically smaller companies that need the chassis to increase scale in the marketplace.

So we've done this very successfully with Plum and Kelsen. We have not done it with the Campbell Fresh business, and so the situation that we found ourselves in in the last year, we've been able to insert Campbell executives on the leadership team, working in conjunction with Bolthouse Farms executives, to maintain that best of small and best of big. So we're really optimistic and we're finding some really great opportunities to put a stronger foundation under the business.

Operator

Robert Moskow, Credit Suisse.

Robert Moskow - *Credit Suisse - Analyst*

I noticed on the opening remarks that you mentioned competitive pressure more often than usual, I would think. It was definitely in fresh bakery and in broth. And my view going into this year was that the food companies would cut costs and focus on price realization and try to avoid deep discounting. Do you see any of that kind of price discipline changing around you in your categories or do you think it's just kind of a pretty typical year in terms of promotional activity?

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

I think the activity definitely varies by category, and what we've seen in the fresh bakery business is competition in the area of sandwich bread and swirl bread. We've recently reformulated our swirl bread and we're out there now with a much improved product, so that was a very specific situation. In the fresh bakery business, our buns and rolls business continues to rock. So we believe we are all over the issue there.

And then in broth, it was really more of a proliferation of private label during the holiday that produced more price competition, and we have responded with increased marketing and actual trade spending to hold our own in that category. So those were two very specific things that we faced.

Robert Moskow - *Credit Suisse - Analyst*

Can I ask a follow-up to Ken Goldman's question, actually? I think what he was kind of getting at is, have you ever considered a model where you go to direct-to-customer shipments to warehouses, rather than DSD? Not so much using -- whether you are using dependent routes. Is that a big savings or is it even possible in Pepperidge Farm?

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

We've been pleased with the DSD system, the independent contractors, what they bring to the business in terms of selling and merchandising and delivery. It's a quality product, it's perishable, so breakage could be an issue. I think when you consider all of it, we're pleased with our DSD system.

Operator

David Driscoll, Citi.

Cornell Burnette - *Citi Research - Analyst*

Good morning. This is Cornell Burnette in with a few questions for David. I just wanted to start off here with -- in ready-to-serve soup. One of your major competitors made the announcement that they would be reducing capacity. I wanted to get your outlook on what that meant for the category over the long term, and specifically does that give you an opportunity, perhaps, to margin up and be maybe less aggressive with promotions and move prices in a higher direction?

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

We're very focused on our soup business. We're particularly pleased with the performance of ready-to-serve soup, whether that the Chunky or the introductory of new Well Yes!. I think you need to ask the other guy.

Cornell Burnette - *Citi Research - Analyst*

Okay. And then on the C Fresh business, just I know you gave a number of puts and takes of kind of what's going on there this year and some of the things that you're trying to do to get the business back on track. Will some of these headwinds, especially in carrots and the issues surrounding the harvest, kind of linger into perhaps F18 as well?

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

So we've talked about the issues facing us in F17 and the expectations that the business will decline. We do expect it to turn a bit in the fourth quarter. As we look ahead to F18, we expect to return to growth on this business both top- and bottom line.

Operator

Alexia Howard, Bernstein.

Alexia Howard - *Bernstein - Analyst*

I guess a quick question on the commodity cost outlook here. Obviously, you have a slightly different mix of input costs. How are things looking? And if the commodity cost environment is getting a little tougher, do you think you will be able to pass that on in pricing?

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

So I can comment on the commodity cost environment. So as we look at the full year, we originally thought cost inflation would be around 2% and now we're thinking it's closer to 1.5%, so we've seen some favorability relative to our expectations in a couple of areas that are causing that. One is wheat, dairy, resins related to you plastic packaging, as well as poultry. So overall, we see a bit of a benefit versus our original expectations.

But we are seeing a swing, first half to back half. It was fairly benign when you look at the core ingredients, packaging, and energy, and that's starting to tick up in the second half, and there's a couple of areas in particular that we are seeing. One is dairy. The first half of the year, we were wrapping the avian flu thing, so that's going to go back more to a normal situation. Vegetable oil is kicking up in the second half and we're beginning to see increases in steel cans as well. I don't know if you follow the steel market, but prices are up fairly significantly on steel. So, we've got an overall year with being OK, but we're seeing increasing headwinds in the back half.

In terms of pricing, I would say we're not ready to talk about any specific pricing actions, but we're right in the midst of starting to formulate our plans for next year and I'm sure we'll take this into account.

Operator

Michael Lavery, CLSA.

Michael Lavery - *CLSA Limited - Analyst*

Just back on C Fresh, you said you had a strategic review, and obviously that's had some changes in your outlook and everything else. Did that also include a review of just your interest in that business long term? Are you evaluating some potential alternatives in terms of whether you might even still be interested in having an agricultural business, or is that a given? And then, just on the branding, you said you'd want to step up those efforts. Could you give a little better color on some of what that might be?

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

Sure. The strategic review that the new team undertook looked at, once again, the potential for this business and we verified the consumer trends towards fresh and health and well-being, the fact that these categories are still growing significantly faster than center-store categories, particularly in the categories that we compete in, so we feel really good about this space strategically.

We've had some execution issues this year and some weather issues in the agricultural part. That's been unfortunate, but that does not sway us from our long-term strategic vision to really build a fresh food platform for Campbell's. And I think the role of the carrots in the business is the authenticity. It's on trend with consumers' desire for fresh produce. Carrots have had a tough go with drought and with heavy rains and some execution issues last year, but I do think that that's an important part. It's also the distribution system and scale in produce for us that makes us more important to the retailer. So I know I'm very committed to the business and we expect big things from it going forward.

Michael Lavery - *CLSA Limited - Analyst*

Okay. Thanks. And just any thoughts on the branding? You said you wanted to step that up. I know you've talked about some of the packaging changes. Garden Fresh, for example, I think it may be the new packaging you're showing, is that some of what you're anticipating or is it beyond some of the packaging changes? What's some of the initiatives there?

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

I think over time we have an opportunity to build two very strong brands here with Bolthouse Farms and Garden Fresh Gourmet. We're continuing to invest in digital marketing; as you point out, some new packaging; and definitely new product innovations, so we will continue to support these businesses in the marketplace.

Operator

Rob Dickerson, Deutsche Bank.

Rob Dickerson - *Deutsche Bank - Analyst*

Just a question around increased brand building, potentially over the next, call it, three to 12 months, and in light of, let's say, a competitor who is stepping away from DSD, which could cause some transitional pressure there for them that they've acknowledged upfront and then also another competitor who seems to be stepping off a bit on promotional activity in the soup category, and you're showing some near-term gains there.

So I'm just curious. Do you -- you are obviously aware of what's happening in each of your core categories and you are aware of what your competitors are doing. Could you foresee the next 12 months potentially being a period of time in which you might have opportunities to actually increase your investment to try to capture share in kind of a period of instability, so to speak, which I think you actually did fairly well with at one point in time in the bread category? Thanks.

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

As you can see from the quarter, we're continuing to invest in marketing and brand building, and Anthony pointed out that as we navigate through our cost-savings initiative, which we just increased, we will be spending back on our businesses to continue to build these brands. We still need to drive sustainable, profitable sales growth and I fundamentally believe that's going to come from investing in the brands and engaging with the consumer. So, we will continue on that track.

Rob Dickerson - *Deutsche Bank - Analyst*

Okay. Great. Thanks a lot. I'll see you next week.

Operator

Thank you and that concludes our question-and-answer session for today. I'd like to turn the conference back over to Ken Gosnell for closing remarks.

Ken Gosnell - *Campbell Soup Company - VP Finance Strategy & IR*

Sure. Thanks, Candace. Thank you, everyone, for joining our second-quarter earnings call and webcast. A full replay will be available about two hours after this call by going online or calling 1-404-537-3406; the access code is 40985838. You have until March 3, at which point it will move to our -- the earnings call [is on] the website at investor.campbellsoupcompany.com. Just click on recent webcasts and presentations.

If you have any further questions, please call me at 856-342-6081. If you are a reporter with questions, please call Carla Burigatto, Director of External Communications, at 856-342-3737. Thank you, everyone.

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.
