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Pinnacle Foods, Inc. (PF)

Q2 2017 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, ladies and gentlemen, and thank you for standing by. Welcome to the Pinnacle Foods, Incorporated Earnings Call for the second quarter, ending June 25, 2017. This conference is being recorded, and there will be a question-and-answer session at the end of the call.

I would now like to introduce your host for today's conference, Pinnacle's Senior Vice President of Investor Relations, Ms. Maria Sceppaguercio. Ms. Sceppaguercio, please go ahead.

Maria Sceppaguercio
Senior Vice President, Investor Relations & Communications, Pinnacle Foods, Inc.

Thank you, Howard. Good morning, everyone, and thanks for joining us today. Earlier this morning, we issued our press release for the first quarter of 2017, which is available on our website. As you know, the second quarter was an eventful one for us. Beyond the significant slate of exciting and highly differentiated innovation we launched during the quarter, we also voluntarily recalled, and subsequently decided to exit certain Aunt Jemima Frozen Breakfast products in May. We also accelerated into this year a number of investments in our manufacturing network that we believe position us well for the future. Importantly, as we indicated in the press release this morning, much of the discrete costs associated with these actions are expected to serve as tail winds to 2018.

Here with me to discuss the quarter and our outlook for the year are Pinnacle's CEO, Mark Clouse, and our CFO, Craig Steeneck. Before turning the call over to Mark, let me remind you that as usual, our release and conversation this morning will include our results on an adjusted basis. The adjusted basis excludes acquisition, merger, and other restructuring charges, and other items effecting comparability. The company believes that the adjusted basis provides investors with additional insight into our business and operating performance trends. While the exclusion of these items is not in accordance with GAAP, we believe that it is a meaningful comparison, and an appropriate basis for discussion of our performance. Details of the excluded items are included in the reconciliation tables included in our press release, and discussed in detail in our 10-Q, which will be filed later today.

In addition, our discussion this morning may include forward-looking statements, which are subject to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995. These statements are subject to a number of risks and uncertainties that could cause actual results to differ materially, and the company undertakes no obligation to update these statements based upon subsequent events. A detailed discussion of these risks and uncertainties is contained in the company's filings with the SEC.

With that, I'll hand it over to Mark.

Mark A. Clouse

Chief Executive Officer & Director, Pinnacle Foods, Inc.

Thanks, Maria, and thanks to everyone for dialing in. As Maria referenced, we have a lot to talk about this quarter. At a high level, we posted very strong end market results, and the fundamentals of the business remain very much on track. However, before getting into a discussion of the fundamentals, I want to first discuss, and provide my perspective, on the decisions we made during the quarter, and the impact they had on our adjusted results for Q2, and our outlook for the year.

First, the Aunt Jemima voluntary recall, and subsequent business exit, were executed quickly and effectively in the quarter. In addition, the exit of the low-margin Aunt Jemima grains business was contemplated in our long-term strategic plan, as part of our network optimization initiatives. The impact of these actions to the quarter was about $16 million, or $0.08 of EPS, versus the originally communicated $10 million, or $0.05 of EPS, driven by some additional enhancements we made in our Jackson plant before starting back up. We are back up and running, and doing so on a stronger platform.

Second, as we began to see the benefit of the enhancements in Jackson, we chose to accelerate into 2017 some additional manufacturing investments, also consistent with our long-term strategic plan. These investments include improving or replacing some assets while strengthening capabilities, systems and quality in our plants. This resulted in us having to absorb an additional $5 million of expense or about $0.03 of EPS in the quarter. So, in total, the second quarter was impacted by a total of $21 million or $0.11 of EPS. These discrete costs all hit gross margin. And while we're pleased that we had tax and interest savings along with very aggressive management of expenses to cover the bottom line impact in the quarter, we recognize that the composition of the P&L is different than what you and what we were expecting.

In terms of the full-year impact, we are expecting approximately another $10 million or about a $0.05 of EPS from these discrete items to waterfall through the P&L in the back half of this year. The vast majority of this incremental expense is expected to occur in Q3, resulting in us now pointing to the low-end of our $2.55 to $2.60 adjusted EPS guidance range for the year. With regard to full-year capital spending, we expect these enhancements to cost approximately $10 million to $15 million, which we are absorbing within our existing 2017 capital budget.

Finally, I want to emphasize that these decisions represent important investments that are consistent with our strategic plan and that we firmly believe strengthen our business going forward. In addition, they have been largely completed and the discrete expenses we are absorbing this year will serve as gross margin tailwinds in

2018 enabling us to maintain the gross margin target we established for 2019. So a challenge in 2017 for sure, but one from which we fully expect to benefit next year and, combined with the strength of our underlying fundamentals, we remain confident that we will deliver another year of outsized EPS growth in 2017. In addition, we believe that 2018 will play out essentially in line with our long-range strategic plan.

Now turning to the fundamentals, which are quite good, starting with our top line. As outlined in our release this morning, our net sales were up 1.9%, including the benefit of Easter, but excluding the impacts of Aunt Jemima, as well as the Boulder UK business wind-down and SKU rationalization. In a food industry environment struggling to find growth, we are pleased with our underlying top-line performance.

In-market performance was even stronger, with our consumption versus year-ago up 3.6% in the quarter, or as much as 4.5%, excluding the Aunt Jemima exit. This performance reflected strong growth of all three retail segments. Composite market share across the portfolio continued to be strong, registering a 0.7 point increase in the quarter and marking our 13th consecutive quarter of share growth.

Our adjusted gross margin was down 150 basis points in the quarter, including a more than 200 basis point headwind from the discrete items referenced earlier. Our underlying gross margin drivers in the quarter were very strong, with productivity coming in at 4% of cost of product sold and acquisition synergies tracking slightly ahead of plan. Inflation of a modest 2.5% was a partial offset. Importantly, these margin drivers were all in line with, or better than, expectations.

Total operating expenses declined almost 14%, primarily reflecting later timing of our marketing spending versus year ago, and lower SG&A overhead resulting from both synergy capture and the aggressive management of expenses in the quarter. Interest expense in the quarter declined 20%, reflecting the benefit of our refinancing in February and lower outstanding debt.

Pre-tax earnings advanced 8% in the quarter, despite the impact of the discrete items. Excluding the impact of these items, pre-tax earnings advanced 34%, reflecting the improvements in underlying net sales and gross margin, reduced operating expenses, and lower interest expense.

Our effective tax rate in the quarter declined to 26.2%, reflecting the benefits of the change in accounting treatment for stock-based compensation, as well as the impact of favorable state tax legislation in the quarter. Adjusted diluted EPS advanced 26% to $0.53 in the quarter, even after giving effect to the impact of the discrete costs, which totaled $0.11 in the quarter.

Now turning to our segments. I'll start with Frozen, which had a great quarter. Net sales advanced 2.5% due to vol/mix growth of 9.2%, reflecting the strength of recently launched innovation and the benefit of the later Easter, partially offset by lower net price realization of 2.4% and the unfavorable impact of 4% from the AJ exit. Excluding the AJ exit, net sales for Frozen advanced 6.5%, fueled by double-digit growth of the Birds Eye franchise, our largest business.

We continue to expand our retail distribution for the Frozen segment, posting a 5% increase in TDPs for the quarter, fueled by a double-digit increase for the Birds Eye franchise. Supporting Birds Eye expansion was the introduction of five new platforms during the quarter, much of which proved to be incremental. Importantly, many of the items are still building distribution, which we expect to continue to grow over the balance of the year.

The new platforms, all introduced in April, are Birds Eye Veggie Made Pasta, a line of side dishes made from zucchini, spinach and lentils, that mimic the taste and mouthfeel of pasta while reducing the carbs and delivering a full serving of vegetables. Birds Eye Superfood Blends, a line of nutrient-rich side dishes in a convenient Steamfresh bag that would otherwise be hard to make at home. Birds Eye Veggie Made Mashed, a line consisting of mashed cauliflower side dishes that delivers a mashed potato taste and texture, along with a mashed sweet potato item. Birds Eye Organic, a limited offering of organic vegetables for mainstream consumers seeking this option. And Disney-themed Birds Eye Voila! meals for kids, extending the Disney license into Voila! meals for the first time.

Market share performance for the Frozen segment advanced 0.4 share point in the quarter, driven by Birds Eye vegetables, which were up 0.9 share point. Birds Eye meals, which advanced 1.2 share points and seafood, which advanced 1.6 share points. Adjusted EBIT for the Frozen segment, including $13 million of discrete costs, declined 14% to $38 million in the quarter. Excluding the discrete costs, adjusted EBIT advanced 14% and adjusted EBIT margins expanded 115 basis points, reflecting strong productivity and later timing of marketing spending, partially offset by inflation.

Turning now to our Grocery segment. Net sales for Grocery declined 1.8% due to lower net price realization, including new product introductory expenses, partially offset by higher vol/mix. The standout for the quarter was Duncan Hines. The brand registered double-digit net sales growth in the quarter, fueled by the significant success of recently-launched Perfect Size for 1.

The new 18-item line is an ultra-convenient, single-serve baking solution made with real, simple ingredients that are baked in a mug, in the microwave, in one minute. Perfect Size for 1 has tapped into consumer needs in a number of key areas, including convenience, individuality, and portion control, while also eliminating the category challenges related to the decline in household size. Distribution for the new line, which is still in the process of rolling out to some key customers, has proven to be highly incremental, supporting the double-digit growth in retail distribution Duncan Hines already achieved in the second quarter.

On the other hand, net sales for Vlasic pickles and Wish-Bone salad dressings were down in the quarter, reflecting highly competitive category dynamics. In the pickle category, competitive intensity in the form of pricing and innovation has put pressure on Vlasic. During the quarter, we launched Vlasic Purely Pickles, a new four-line item (sic) [four-item line] of pickles, made with no artificial flavors, colors or preservatives, supported by a new social media and digital marketing plan. We expect the innovation and our new marketing plan to strengthen Vlasic trends in the second half.

In dressings, you'll recall that we launched Wish-Bone Avocado Oil salad dressings in three varieties late in the first quarter. This new line adds to our presence in the premium segment of the category with on-trend healthier oils and is a great example of the balance we are working to strike between gross margin expansion and growth. Given the extremely competitive nature of the category, we will continue to be thoughtful in making the appropriate tradeoffs between innovation, pricing and promotions to optimize our overall results, as we did during the second quarter with the reduction of some lower ROI promotional programs.

In-market performance for the Grocery segment was exceptionally strong with retail consumption advancing almost 5% in the quarter, in a category composite that was essentially even with year ago. This performance drove a market share gain for Grocery of 0.5 share point, largely reflecting a 5.9 share point increase for Duncan Hines, and to a lesser extent, share growth for Armour, partially offsetting by Vlasic and Wish-Bone.

Supporting the consumption and share growth for Grocery in the quarter, was strong retail distribution expansion, approximating 5%, led by double-digit growth for Duncan Hines and continued expansion for Armour, syrups and pie and pastry fillings.

Adjusted EBIT for the Grocery segment advanced 14% in the quarter. And adjusted EBIT margin grew 310 basis points, largely reflecting the benefits of strong productivity, a reduction of lower ROI promotional programs, and acquisition synergies, partially offset by input cost inflation.

Turning to the Boulder segment. This segment had a very good quarter. Although overall net sales were even with year ago, underlying net sales grew 7.7%. This performance was due to volume/mix growth of 4.9% and favorable net price realization of 2.8%, entirely offset by the unfavorable impacts of 3.4% and 4.3%, respectively, from the UK business wind-down and the SKU rationalization program, both of which were implemented in the second half of 2016.

Driving the underlying growth in net sales for the segment were Evol, gardein, Earth Balance and Glutino, partially offset by Udi's. Udi's decline reflected growth of new competitive entrants in the gluten-free bread category, which continues to enjoy double-digit growth. You've heard me refer to our biggest Udi's opportunity as eliminating the compromise for gluten-free, which I believe will be a game-changer in the category, enabling items like gluten-free bread to appeal to a much larger consumer base. As I indicated previously, we feel very good about our outlook for Udi's, and we'll be sharing more exciting details with you later this year.

In-market performance for Boulder remains strong, with retail consumption up almost 6%, despite the SKU rationalization program. Market share for Boulder was down 0.2 share point, reflecting the impact of the SKU rationalization, and to a lesser extent, an underlying share loss in gluten-free bakery and pizza, which more than offset solid underlying share growth in our other categories.

Adjusted EBIT for the Boulder segment advanced 30% in the quarter. And adjusted EBIT margin grew 390 basis points, reflecting the benefits of the underlying net sales growth and related mix improvement from the SKU rationalization, along with acquisition synergies and productivity, partially offset by modest input cost inflation.

Finally, turning to our Specialty segment. Specialty net sales were significantly impacted by the Aunt Jemima exit, which accounted for almost 900 basis points of the segment's net sales decline of 15% in the quarter. The underlying sales decline of 6.2% was driven by the previously disclosed gardein private label business exit and lower sales of foodservice, both of which significantly benefited Specialty margins in the quarter.

Adjusted EBIT for the Specialty segment declined 40% to $4.4 million versus $7.3 million in the year-ago period, entirely due to $6 million of discrete costs related to the Aunt Jemima exit. These discrete costs more than offset the benefits of productivity, acquisition synergies and higher net price realization. Excluding the discrete costs, Specialty adjusted EBIT advanced 40%, and adjusted EBIT margin grew 390 basis points versus year ago, very much in line with our strategy of focusing on higher margin businesses within this segment.

With that, I'm going to hand it over to Craig.

Craig D. Steeneck

Chief Financial Officer & Executive Vice President, Pinnacle Foods, Inc.

Thanks, Mark. And good morning, everyone.

Let me start with the results for the quarter and then transition to our outlook for the back half of the year. Net sales for the second quarter decreased 1.6% to $745 million, as strong underlying growth of 1.9% was more than offset by the impacts of the Aunt Jemima exit and the Boulder UK wind-down and SKU rationalization. Driving the underlying growth was higher volume/mix of 3.3%, partially offset by lower net realized pricing of 1.3%, due in part to higher new product introductory expenses and unfavorable foreign currency translation of 0.1%.

Net sales in our Frozen segment continued to be very strong, increasing 2.5% in the quarter, despite a negative 4% impact from the Aunt Jemima exit. This growth was fueled by a 9.2% increase in volume/mix, reflecting the strength of the recently-launched innovation and continued momentum of the Birds Eye franchise, along with the benefit of a later Easter in 2017. Partially offsetting this growth was lower net price realization of 2.4% and unfavorable foreign currency translation of 0.3%.

Net sales for our Grocery segment decreased 1.8%, largely reflecting lower price net realization of 2.1%, including the impact of higher new product introductory costs versus year ago, partially offset by higher volume/mix of 0.3%.

Net sales for our Boulder segment were even with year ago, reflecting volume/mix growth of 4.9% and favorable net price realization of 2.8%, entirely offset by the wind-down of the Boulder UK operations and the SKU rationalization program. The underlying sales growth of 7.7% reflected strong growth across the portfolio, partially offset by Udi's.

Finally, net sales of our Specialty segment declined approximately 15%, primarily due to the 8.9% impact from the Aunt Jemima exit, as well as lower volume/mix of 6.8%, primarily due to the previously-disclosed exit of the gardein private label business and lower sales of foodservice. Partially offsetting these drivers was higher net price realization.

Before turning to gross profit, it is worth noting as we go through the next three quarters, top-line performance for both the Frozen and Specialty segments will be negatively impacted by the lost sales associated with the AJ exit. As we report our results, we will break this impact out to enable visibility into the underlying trends.

Now turning to adjusted gross profit. We remain quite bullish on our gross margin opportunity, despite the reported softness in the quarter, stemming from the discrete items. Productivity in the quarter was exceptionally strong at 4% of cost of goods sold. And Boulder acquisition synergies are tracking slightly ahead of our $15 million target for the year. These two factors combined to more than offset modest input cost inflation of 2.5%, resulting in solid underlying gross margin growth for the quarter. However, the discrete items in the quarter were a 200-basis-point headwind to gross margin, resulting in a 150 basis point decline versus a prior period that posted a 260 basis point increase.

Let me pause here and take a moment to provide a little more context around the discrete items and how we expect them to impact our performance in the second half. As Mark previously mentioned, as we executed the Aunt Jemima exit, we gained important insights into the benefit of making certain upgrades that strengthen capabilities and quality in our plants. With the organization already highly focused on the enhancements in our Jackson facility, we decided to leverage that focus and learning across our frozen manufacturing network to accelerate select improvements consistent with our strategic plan.

With the vast majority of the work is now complete, we anticipate an additional $10 million of expense, or about $0.05 of EPS, to flow through the P&L, primarily in the third quarter. However, because most of these discrete costs are one-time in nature, we expect them to become tailwinds for 2018, allowing us to maintain our stated target of growing gross margin by 300 basis points to 400 basis points by 2019, and preserve our overall performance outlook for 2018.

Now, continuing through the P&L; adjusted EBIT declined 0.5% in the quarter to $114.2 million, largely reflecting the impact of the discrete items, offset by lower operating expenses, as we aggressively managed overhead expenses, continued to realize Boulder synergies, and benefited from the later phasing of marketing spending, given our innovation calendar this year (sic) [period].

Through the first six months of this year, we have realized $12 million of Boulder acquisition synergies. Adjusted interest expense in the quarter decreased by nearly 20%, reflecting the term loan refinancing we completed in the first quarter of the year, as well as the reduction of outstanding indebtedness versus the prior year.

Our effective tax rate in the quarter, excluding items affecting comparability, came in at 26.2% compared to 37% in the year-ago period, largely reflecting the benefits of the new accounting treatment for stock-based compensation and favorable state tax legislation.

Given the significance of this change in accounting treatment on our results this year, let me take a moment to elaborate on our outlook. You'll recall that at the beginning of the year we expected this change would benefit our EPS in 2017 by about $0.05. After significant benefit in Q1 and our first-ever vesting event under our long-term equity incentive plan in April, we updated the expected EPS benefit to $0.10 for the year. With the significant first half activities behind us, which benefited EPS by about $0.08, we continue to estimate the impact of this change in accounting treatment to be approximately $0.10 for the full year of 2017, with the remaining $0.02 benefit expected in the second half.

Finally, adjusted net earnings increased 26% to $63 million compared to $50 million in the prior year, while adjusted diluted EPS also advanced 26% to $0.53 compared to $0.42 in the year-ago period.

Now, turning to cash flow. Net cash provided by operating activities in the quarter totaled $57 million compared to $88 million in the prior year. For the six-month period, net cash provided by operating activities totaled $120 million compared to $165 million in the year-ago period, largely reflecting the working capital build associated with the company's robust innovation agenda in 2017, and the cash impact of the AJ exit.

Capital expenditures in the second quarter totaled $20 million compared to $26 million in the year-ago period. Free cash flow in the second quarter decreased to $37 million compared to $62 million in the prior-year period, largely reflecting the lower cash from operating activities.

Turning to liquidity, at the end of the second quarter, our total debt was $3 billion, including a $2.3 billion secured term loan and $700 million of senior notes. Cash totaled $131 million, bringing our net debt to $2.9 billion and our net leverage ratio to 4.17 times.

And finally, in terms of our outlook for the year; for the full year, we have maintained our guidance for adjusted diluted EPS in the range of $2.55 to $2.60, and now expect to be at the low end of the range, reflecting the inclusion of the full year impact of the discrete items that we've discussed today. The benefit of the 53rd week is still expected to add approximately 1% to full year net sales and $0.03 to adjusted diluted EPS. This impact will be spread across all four segments in the fourth quarter of 2017.

Input cost inflation remains estimated in the 2.5% to 3% range. Productivity for the year is now estimated to be at the top or slightly ahead of our 3.5% to 4% of cost of products sold range. In addition to the productivity, we expect Boulder Brands acquisition synergies of at least $15 million this year. These synergies will benefit both gross margins and SG&A overhead.

Adjusted net interest expense is now forecasted to be slightly below $123 million. The effective tax rate for the year, including the benefit of the change in tax treatment for stock-based compensation, is now estimated in the range of 33% to 33.4%, with the second half rate expected to be significantly higher than the first half, given the timing of equity vesting being skewed to the first half of the year.

The strategic manufacturing investments that impacted the second quarter are also expected to impact the balance of the year by another $0.05, with the vast majority of that impact occurring in the third quarter. The weighted average diluted share count for the year continues to be approximated at 120 million shares, with the second half of the year higher than the first half. And finally, capital expenditures for the full year continue to be estimated in the range of $115 million to $125 million.

With that, I'll turn the call back to Mark for some concluding remarks.

Mark A. Clouse

Chief Executive Officer & Director, Pinnacle Foods, Inc.

Thanks, Craig. As we open it up for questions, I want to leave you with three key thoughts. First, the discrete decisions we made this quarter, while not in our 2017 plan or without impact to our financials, reflect the right investments to support our long-term goals. Second, our fundamentals are very strong, with industry leading in-market results and very strong financial drivers, such as productivity, synergy capture, and aggressive cost management. Excluding the discrete investments we made, we are ahead of expectations. And third, at the end of the day, despite the investments, we remain on track to deliver EPS growth approximating 19% this year, with the majority of these discrete costs creating tailwinds for 2018.

And with that, I'll turn it back to Howard to open it up for your questions.

QUESTION AND ANSWER SECTION

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

Andrew Lazar
Analyst, Barclays Capital, Inc.

Q

Good morning, everybody.

Maria Sceppaguercio
Senior Vice President, Investor Relations & Communications, Pinnacle Foods, Inc.

A

Good morning.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Hi, Andrew.

Andrew Lazar
Analyst, Barclays Capital, Inc.

Q

Hi. I've got two questions. The first one would be, of the five new platforms that you discussed and a lot of the incrementality of it in Frozen, trying to get a sense of, I guess, from where you're sourcing a lot of that, that sort of highly coveted freezer space. I think last quarter you talked about three potential buckets of source. One is redundancy in sort of the frozen vegetable category. The other was maybe from some adjacent frozen categories. And then the other one might have been in also proactively pruning some of your less productive SKUs. So I'm just trying to get a sense of where you're seeing so far a lot of that space coming from.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Yeah. So, Andrew, those are really the right drivers. And I think it's played out essentially consistent with what we would have expected where the primary driver of space that we've been able to create is from the redundancy in the category. And if you look at a lot of the smaller regional players where you would have been on number three or four frozen corn or peas, that was an opportunity for us to really point out the better return for the slot by putting our innovation in.

I do think we continue to make progress too on expanding or broadening the footprint, especially as many of our products are beginning to spread more broadly than just a frozen side dish. And so our opportunity to go after the lower-margin, low-price frozen meals category has continued to be very strong. And, as we said, we would continue to look at velocities on our own portfolio and make sure we're making good choices and ensuring that we've got the best items in place. And so we did make a few trade-offs, as you might imagine, with five platforms coming in. But with distribution up almost double digits this quarter, we're feeling really good. And that's actually ahead of full distribution reflection of the rollout of the platform. So we continue to see a good road ahead for us.

And I think one of the things that's important this quarter too is the pivot that we are seeing in the category. We've talked a lot about the fact that as we get our strategy embedded and as we see the broader potential for frozen veg, we want to make sure that we're also seeing it driving category performance. And even with Easter helping a bit in the quarter, we did see very strong trends all the way through June and into July. So we're feeling really good about where we are right now on the Birds Eye franchise as well as the potential going forward.

Craig D. Steeneck
Chief Financial Officer & Executive Vice President, Pinnacle Foods, Inc. A

And, Andrew, I'd note that most of these lines are premium priced...

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc. A

Yeah.

Craig D. Steeneck
Chief Financial Officer & Executive Vice President, Pinnacle Foods, Inc. A

...right on the higher end of the category which are obviously margin accretive to us and margin accretive to the standard core straight veg items.

Andrew Lazar
Analyst, Barclays Capital, Inc. Q

Got it. Well, thank you for all of that. And then it's a good segue into – I know that takeaway or consumption obviously was impacted both in the first quarter and the second quarter in opposite ways because of the – sort of the Easter holiday. And I was just trying to get a sense of, if you have handy, maybe just sort of a – some – a year-to-date metric of just where consumption is in the key sort of areas, whether it's Frozen, in Grocery, just to get a sense of like underlying where's takeaway at this point on a sort of underlying basis.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc. A

Yeah. So if you look across our categories, and it was a little choppy from quarter-to-quarter, we see positive momentum across the board. I mean, if you look at the – our Veg business or our Birds Eye business, we're up almost 5% year-to-date in Veg, certainly with that accelerating into the second quarter. Our Voila! business or Meals business under Birds Eye is up almost double digits, 9.5%. Total Frozen looks very strong. We're up about 0.5 share point year-to-date. On the Grocery side, again, as we said in our comments, we do have some strengths clearly coming through in baking, continued strength in canned meat. A little bit weaker performance on Wish-Bone and pickles, although we expect that to improve in the balance of the year.

Overall for Grocery, you see consumption positive year-to-date, obviously with a stronger ramp-up in the quarter. And a pretty steady share gain from quarter-to-quarter where we're up year-to-date, almost 0.5 share point, about 0.4 share point.

And then I think one of the other things that's pretty exciting is the building momentum we see on select pieces of our Boulder business. As we've talked a lot about the migration from integration mind-set to acceleration mind-set, we're starting to see really strength building on businesses like gardein as we've opened up Hagerstown; our Evol business through distribution expansion; Earth Balance, all look good. We understand the challenges we've got on Udi's and are really looking good I think as we go forward on that business. Gluten-free as a category continues to be very healthy, with a lot of competition. But I think we've got some great ideas and some great innovation as we roll through the balance of the year. And we'll talk more about that in future meetings.

Does that help?

Andrew Lazar
Analyst, Barclays Capital, Inc.

Q

That's great. Thank you very much.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Yeah. Yeah. Okay, great.

Operator: Thank you. Our next question or comment comes from the line of Bryan Spillane from BoA. Your line is open.

Bryan D. Spillane
Analyst, Bank of America Merrill Lynch

Q

Hey. Good morning, everyone.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Hi, Bryan.

Bryan D. Spillane
Analyst, Bank of America Merrill Lynch

Q

Just two questions for me. First, I just want to make sure I've got the math right. As I'm thinking about the tailwinds relative to the discrete items for 2018, I guess I was getting to about $30 million. Is it the $16 million of the exit costs in the quarter, $5 million of manufacturing investment in the quarter, and then the incremental $10 million in the back half? Those are all sort of discrete items which kind of don't repeat next year. Is that the right way to think about it?

Craig D. Steeneck
Chief Financial Officer & Executive Vice President, Pinnacle Foods, Inc.

A

Yeah. So I think you have the math right, Bryan. There was $21 million of discrete items in the quarter, and we've said an incremental $10 million for the year, so that's 30 – $30 million all-in. Of the $30 million, $10 million of it is in the strategic investment component. The residual $20 million is in the overall AJ recall and exit and enhancement work we did in the Jackson facility in the quarter that, that some of it also falls through to Q3. I wouldn't say it's 100% tailwind relative to next year and a full bounce-back, but you could certainly anticipate it would be the majority of it.

Bryan D. Spillane
Analyst, Bank of America Merrill Lynch

Q

Okay. And then the second – the follow-up to that is just related to some of the cost savings or some of the remedial actions you've taken to try to offset some of the incremental costs. Just want to be clear, has there been any change in terms of marketing or like advertising in consumer investment? Or have all of the savings been sort of outside of that?

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Well, certainly as you would imagine, as we made a decision to make these investments, we went through and looked for opportunities to tighten our belt across a variety of areas, although, protecting the operational investment behind our brands and innovation we've maintained. I think one of the things that is benefiting us a bit in the second quarter is the fact that our innovation flow for the year is a bit more back-loaded than we've been historically. So although you see the negative of the slotting cost being a bit higher in Q2, we're also getting the benefit of what is a lower marketing rate. You'll see that reverse as the year plays out, and we feel very good about the support levels we have on the business, and I would say that our in-market performance certainly supports that.

And so I think although you're always going to be very disciplined and looking at every dollar that's being spend, I feel great about what we've been protecting and what we will continue to spend throughout the year.

Bryan D. Spillane
Analyst, Bank of America Merrill Lynch
Q

Okay. Thank you.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.
A

Thanks, Bryan.

Operator: Thank you. Our next question or comment comes from the line of Michael Gallo. Your line is open.

Michael W. Gallo
Analyst, C.L. King & Associates, Inc.
Q

Hi. Good morning.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.
A

Hi, Michael.

Michael W. Gallo
Analyst, C.L. King & Associates, Inc.
Q

I was wondering if I could just dig in on the strategic investments, and to what degree those expect you to improve efficiencies, and just a little bit more on how you expect that'll help you on the margin side, and to what degree you expect that'll help you in 2018. Thanks.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.
A

Yeah, sure. So let me give you a little bit of a sequence of events. It might help kind of explain both what those investments are, and to some degree, why did we choose to do them now, which I think is probably a fair question also. As you walk through the sequence of events in Q2, it starts with the decision for the voluntary recall in May, and with that, some good insights and work that we began to do in the Jackson facility. As we went through that work and we really understood where the opportunities were to improve – and again as you would imagine, quality will always be our top priority – we saw the opportunity not only to improve quality, but some of the improvements we were making would also enhance efficiency going forward.

And the great news for us is we had a very clear strategic plan defined, especially in the frozen category where we saw a lot of opportunities to invest in facilities as we rolled out over the next couple of years. And as we saw the benefits we were getting in Jackson, we decided to move those investments forward, both to strengthen capabilities as well as improving quality, which is a great double benefit of these.

So as we went through them, the composition of these investments relate to a couple of different areas. One is upgrading some assets. In some cases, we're segregating our activities so that we're able to reduce the risk of contamination or cross-contamination while also being able to improve the effectiveness as we operate the plants. We've upgraded some systems and improved – and transferred best practices forward. So we feel very good about all of those having this double benefit of improving quality while also improving efficiency.

So as part of our margin agenda – and we continue to feel very confident in our 300 basis point to 400 basis point expansion by the end of 2019 – we feel that this will accelerate those benefits and help us move down that agenda, albeit contemplated in the plan, doing it faster and unlocking those benefits sooner made a lot of sense. And to complement that, as you might imagine, as we were doing the work on Jackson, we had the team mobilized to go do that, they were focused, learning from that experience, and we saw it as an opportune moment just to continue through our frozen network and bring those strategic investments forward.

Also, I have to say, I like doing this kind of work when you're coming from a position of strength. And given where the business is right now and the underlying fundamentals, although I recognize fully it altered a bit the composition of the P&L in the quarter and to some degree for the year, it's a great build on top of very good fundamentals. And again, having it behind us and set up for the future going forward I think is a good win for us, and will pay benefits down the road.

Michael W. Gallo Q
Analyst, C.L. King & Associates, Inc.

Okay, thank you.

Operator: Thank you. Our next question or comment comes from the line of Ken Goldman. Your line is open.

Kenneth B. Goldman Q
Analyst, JPMorgan Securities LLC

Hey, good morning, everyone.

Mark A. Clouse A
Chief Executive Officer & Director, Pinnacle Foods, Inc.

Hi, Ken.

Maria Sceppaguercio A
Senior Vice President, Investor Relations & Communications, Pinnacle Foods, Inc.

Good morning, Ken.

Kenneth B. Goldman Q
Analyst, JPMorgan Securities LLC

I just wanted to ask a little bit, some of the product discontinuations you've undertaken, you seem pleased with how they're going. My experience has been and I think everyone's is, when you do something right, you do more of it. So is it reasonable – as we in the outside think about modeling sales in 2018 and beyond – I'm not asking specifically about guidance, but is it reasonable to assume there will be more of these – if I could say it, these discontinuations to come? I'm just trying to get a real general sense of how you're thinking about that sales versus margin balance, your portfolio strategy ahead.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Yeah. Well, on that – I think that is – the key is, we do have a very well defined portfolio strategy. And although I would tell you that shrinking your way to greatness will never be part of our plan. I do think we will continue to look at the portfolio and make sure that we're optimizing it in the best way possible. The good news is, a large portion of the foundation brands that we have are very good supporters to the overall business.

As I've said before, one of the power – one of the things that really powers this portfolio is the ability to have kind of users and donors where the foundation brands are solid performers, they're covering expenses, they're generating cash flow, as well as margin and profit that enables us to accelerate investment in the sum of the businesses with greater growth potential. I like that dynamic. And so in general terms, I continue to feel very good about how our portfolio shapes, and how that should enable us to continue to see progress in top line.

Having said that, though, I think you raise a good point, and one that we will continue to look at, as we had already before the decision to exit the grains business in Aunt Jemima, clearly we did not see that as a strategic business going forward. And I think that did help us make the decision quickly following the recall. So although I don't think there's big distinct plans for it, we'll continue to optimize as we go forward. And again, remember too, we will have cycled through the exit of our Udi's business in the UK, our Boulder SKU rationalization program, and although we'll have a couple of quarters to lap of Aunt Jemima as we play through the year, we will cycle that. So that should be tailwind for us as well, and that may create some room to make some of those decisions going forward.

Craig D. Steeneck
Chief Financial Officer & Executive Vice President, Pinnacle Foods, Inc.

A

But, Ken, your observation is absolutely fair. We're driving the gross margin agenda. I mean, the mainstays of it is driving productivity, network optimization, getting improvements in the infrastructure and how we manage the business, clearly offsetting modest inflation. But above and beyond that, we look to get mix improvement. And as we see opportunities like an unprofitable Boulder UK business, unprofitable SKUs in the core Boulder portfolio, a low-margin Aunt Jemima, we take the opportunities to drive incremental mix improvement to help that gross margin, and opportunities in net realized pricing with trade optimization, list price increases anywhere where we can do that.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Yeah. I think it's really a balanced attack. I think it's fueling the things that have high growth potential while we manage appropriately those that do not. And especially those that have margins that are disadvantaged, we will take a tougher view on those.

Kenneth B. Goldman
Analyst, JPMorgan Securities LLC

Q

Can I ask a very quick follow-up? And that's extremely helpful. But just so I understand, your gross margin guidance long term is for it to be up 300 basis points to 400 basis points from 2016 to 2019. In that assumption, how much are you relying on mix from discontinuing certain items? Or is really that's just such a small part of it that you can't really model that even?

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

It's a relatively small part of it.

Craig D. Steeneck
Chief Financial Officer & Executive Vice President, Pinnacle Foods, Inc.

A

Yeah.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

As we laid out kind of the three big building blocks of the margin agenda, it really starts with the productivity. And again, as we said earlier in the comments, we really are executing well on productivity. I mean, we're on the 4% range to the higher end of where our direction has been, and we continue to see that road map strengthening going forward, again through this balance of vertical and horizontal cost management. And that will be the biggest contributor. In addition, we've got the synergy and the opportunity to continue to drive improvement in Boulder.

And then finally, we look at mix and prices, the complementary nature. But certainly, with the leadership businesses that are as advantaged in margin as they are, while we tighten this portfolio with some of the actions we're taking, we certainly expect that to be an enhancement for the business going forward.

Kenneth B. Goldman
Analyst, JPMorgan Securities LLC

Q

Thank you.

Craig D. Steeneck
Chief Financial Officer & Executive Vice President, Pinnacle Foods, Inc.

A

Thank you, Ken.

Operator: Thank you. Our next question or comment comes from the line of Rob Moskow from Credit Suisse. Your line is open.

Robert Moskow
Analyst, Credit Suisse Securities (USA) LLC

Q

Hi. Thank you.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Hi, Rob.

Robert Moskow
Analyst, Credit Suisse Securities (USA) LLC

Q

I wanted to push a little bit more on the investments that you were making at the plants, because I think that there's this tension at times between productivity and then the quality improvements that you need to make in order to ensure no product recalls and the sort. So I guess I wanted to ask, Mark, are you sure that you're done in your review of the manufacturing footprint? Have you found all the areas where you think that there's risk of quality, I guess, set-backs? And can you tell us a little bit more I guess about the productivity improvements you want to make as you head towards a higher gross margin, and how that can be done without sacrificing quality?

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Yeah. So, clearly, as we think about this – and let me make sure that I start this conversation from the right first step. Quality will always be at the top of our list of priority. And I feel very good about our quality program and the foundation that we have built. I think what has helped us in that journey as we executed the Jackson work following the recall, and seeing the benefit, the best practices, identifying some insights – and again, I would say primarily in our frozen network, it gave us I think confidence and conviction that those improvements that strengthen quality do in many cases have the dual benefit of improving efficiency.

I mentioned segregating operations in a plant, let me just use that as a little bit of an illustrative example. So, although that is a great build to help control allergen contamination, or cross contamination, it also segregates the operation that enables your sanitation model and plans to be more targeted and focused versus having to shut down your entire operation to clean one line, now I can be more effective in cleaning a line at a time while continuing to run the others. So that's an example.

Certainly, you might imagine too, that as we look for better technology or better assets for freezers or some of our lines or assets there, those improvements come with an inherent improvement in efficiency and speed, dependability. So, I think the good news for us is, we spent a lot of time looking at the road map for our manufacturing network going forward, and we have looked for the opportunities to create these win-wins as we've been executing it. Certainly, if there are areas where we think we need to invest more fully on the quality side, we're going to do it, but we've created the room in this plan, and in this journey, where we believe we can accomplish both objectives well.

Robert Moskow
Analyst, Credit Suisse Securities (USA) LLC

Q

Okay. So, it's not a setback to your gross margin target, your three-year gross margin target. You can still do both at the same time.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

We can do both at the same time. And like I said, I think the fact that this year's composition looks a little different than perhaps we intended. I think in the long run, the benefit of having executed this more front-loaded will help us on that journey as we go forward.

Robert Moskow
Analyst, Credit Suisse Securities (USA) LLC

Q

Okay. Thank you.

Operator: Thank you. Our next question or comment comes from the line of Farha Aslam from Stephens. Your line is open.

Farha Aslam
Analyst, Stephens, Inc.

Q

Hi. Good morning.

Maria Sceppaguercio
Senior Vice President, Investor Relations & Communications, Pinnacle Foods, Inc.

A

Good morning, Farha.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

How are you, Farha?

Farha Aslam
Analyst, Stephens, Inc.

Q

Good, thanks. First question is for Craig. Just so we understand how we should think about the tax rate going forward into 2018 as well. Is this 33% to 33.4% tax rate sort of a new sustainable tax rate we should think about for Pinnacle?

Craig D. Steeneck
Chief Financial Officer & Executive Vice President, Pinnacle Foods, Inc.

A

It's a great question, Farha. Unfortunately, no. This year got kind of a significant windfall from the first-ever equity vesting of our long-term incentive plan and some benefits from state tax legislation. So, it won't be quite this low on a go forward basis. You could expect that it would tick up a bit in the out years. Obviously, we'll get greater clarity on that when we put the 2018 guidance out.

Farha Aslam
Analyst, Stephens, Inc.

Q

That's very helpful. Thank you. And the next one is for Mark. You always just have a great kind of macro view on the food industry. And the two things that really captured investors' minds right now is really the entry of the hard discounters here into the U.S., as well as the increased focus of online grocery in the United States. Could you just speak to how you're preparing Pinnacle for those two trends?

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Yeah, so, good question. And I do think it's very timely in the world we're living in today. Certainly a lot of news over the last quarter in this space as well. I think, first, let me start on the hard discounter side. It's probably good to kind of cast this in a broader umbrella to reflect the dynamics that are going on with private label, as well as the pressure on pricing in the industry. I think that as you think about that, it is an undeniable fact that that will continue to be a driver in the industry.

I feel very good about the Pinnacle position in that, because I think we've tended to focus on kind of three key elements that I think position us very well in that world of deep discounters and aggressive price pressure. One, we have spent a lot of time building our brands. And so the strength of our brands and the equity differentiation in categories, in some cases even categories that are challenged, like we've been doing in baking, like we're doing in frozen meals. This is all, I think, set us up well and to be positioned well against more deep discounters or pricing.

Second is innovation. We've done a very good job bringing new to the category in highly relevant innovation that tends to redefine a bit the price value relationship. Very much in line with what we're doing with Perfect Size for 1 in Duncan Hines, which is a great way to kind of change the comparison. So, we're not comparing $0.99 cake mix to $0.79 cake mix. So, I think that's another tenet that has worked very effectively in our play.

And the final one and a really important one, I think that's going to be the key to successfully navigating this, is the relationship and the partnerships that we create with retailers. The ability to understand what they're up against and what they're facing, how they're looking at the entry of some of these deep discounters and the pressure that's coming on price. Our ability to create really win-win solutions in the categories, where again, we changed some of the paradigms and help them building margin while also growing. I think frozen vegetables is probably one of the best examples, where we can continue to do that, represent the category direction and create and articulate a vision for them, where we both are successful together, I think has been critical to what we've accomplished, as well as what will be the blueprint going forward.

Within that, I would include the online world. So, as you think about what's going on in the spirit of e-commerce and certainly with the Amazon and Whole Foods merger that creates an interesting new dynamic, I think a little early to predict exactly what that means, but the fact that we have such a strong relationship with Whole Foods through our Boulder business, and we have been very aggressive in building our relationship with Amazon and really want to be seen as the thought leader in frozen and being able to help Amazon think about how frozen should look in an online world and how that will evolve over time, I think is positioning us very well and to the emergence and the continued growth there.

So, I think that it's really important that you get this mix right between building brands, innovation and then developing the relationships that recognize the environment we're in, and I think that will be true in the deep discounter world and I think that will be true in online as well. A little different solution to each problem, but I think a very solid playbook that has served us well.

Farha Aslam
Analyst, Stephens, Inc.

Q

Very helpful. Thank you.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Thanks.

Operator: Thank you. Our next question or comment comes from the line of Matthew Grainger from Morgan Stanley. Your line is open.

Matthew C. Grainger
Analyst, Morgan Stanley & Co. LLC

Q

Hi, everyone. Thanks for the question. I just had two. Mark, you talked last quarter about private label momentum in your categories. I was just hoping you could give us an update on how those trends have evolved through the quarter? And from a competitive perspective, pricing in Q2 was negative in both Frozen and Grocery. I know there was a lot of slotting behind some of the new product activity that seemed to work fairly well in the quarter. But is there any element in there of responding in any way to changes in the promotional or competitive environment?

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Yeah. So, let me start with private label and then I'll round it out with the pricing answer. As I said last time and as we kind of alluded to in the prior question, there is no doubt that the presence of private label and the focus on private label, I think, will continue to be a trend. The fact of the matter is the benefit of what we have been able to accomplish and where you see private label most prevalent in our categories, even where they are displaying growth, we are outgrowing them to a fairly significant extent.

The risk, I think, for the increase in private label resides heavily on the smaller players that are not sitting with differentiated portfolios or brands that are basically competing head-to-head on price. I think that's where you're going to see a lot of pressure and decline. Now having said that, we are being very diligent across our categories and making sure that we are positioned well and that we have created the right complete value proposition, as we look at places where they're adding value.

I mean, I'll give you one example. In gluten-free bakery and bread right now, you see a pretty significant step up in private label share. And so the onus on us is to strengthen our proposition and our offering relative to that, so that we're able to differentiate, justify the price, and do what we should be doing is leading that category.

Bless you, Maria.

Maria Sceppaguercio
Senior Vice President, Investor Relations & Communications, Pinnacle Foods, Inc.

A

Thank you.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

So, I think the reality is, I feel overall very good about where we are. I think we've got a good playbook, but there are places, where we've got to make sure that we remain very vigilant and do the work needed to keep that separation and value equation right.

On pricing for the quarter, remember one of the other things that impacted the quarter was the shift of Easter. So, as you moved a significant promoted event into the quarter, you would have seen a little bit more headwind on the pricing side than what you would normally have seen. And if you smoothed it out over the year, we continue to look in a balanced position, where we, I think, are getting the formula right between where we want to promote and where we don't and where we get the biggest return for our dollars.

And as you mentioned, one of the other factors was the little bit later timing of slotting that occurred in the second quarter, which put some additional pressure on the pricing line. But overall, I still feel very good as we think about the year in totality on where we'll be relative to pricing and how we're making those decisions and tradeoffs.

Matthew C. Grainger
Analyst, Morgan Stanley & Co. LLC

Q

Okay. Great, thanks. And if I could just follow-up on Andrew's question earlier about year-to-date consumption and take away. Even with some Easter timing benefit to shipments in this quarter, consumption was pretty far ahead of shipments for the second consecutive quarter and I was just hoping you could elaborate a little bit more on what's driving that gap? And is there any sense that inventories are possibly below normalized levels at the moment? Do you see them in the right place? Just trying to better understand the mismatch there.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Yeah, I do think if you look at it on a year-to-date basis, the numbers are much closer. You're not wrong that there is a little bit of a lead on consumption relative to shipments. A couple of factors that are there. Part of that is a little bit as we've said when we came out of the year, we were a little bit heavier on consumer inventory relative to the strength on Birds Eye exiting the quarter and heading into this year.

But outside of that, I actually feel pretty good about the calibration. Now, as we executed some of the things that we did this quarter, especially in Jackson, as you might remember or know, that the Jackson facility beyond Aunt Jemima also includes seafood and pizza. So, we did have a bit of downtime as we were executing those enhancements. But I think for the most part, we see that inventory level recovering quickly and I think will continue to align fairly closely with consumption going forward.

Matthew C. Grainger
Analyst, Morgan Stanley & Co. LLC

Q

Okay. Great. Thanks, Mark.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Thank you, Matt.

Craig D. Steeneck
Chief Financial Officer & Executive Vice President, Pinnacle Foods, Inc.

A

Thanks, Matt.

Operator: Thank you. We only have time for one more question, so our final question for the Q&A session will be from Steve Strycula from UBS. Your line is open.

Steven Strycula
Analyst, UBS Securities LLC

Q

...and congrats on a good quarter, fundamental quarter.

Maria Sceppaguercio
Senior Vice President, Investor Relations & Communications, Pinnacle Foods, Inc.

A

Thanks, Steve.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Thanks, Steve.

Steven Strycula
Analyst, UBS Securities LLC

Q

So, quick question for Craig on the gross margin. If I understand all the puts and takes, can you comment as to whether the third quarter is going to experience about half as much of gross margin pressure as 2Q did from one-time items? Then I have a follow-up.

Craig D. Steeneck
Chief Financial Officer & Executive Vice President, Pinnacle Foods, Inc.

A

Yeah. So, first, I would say, Steve, just focus on kind of productivity and inflation. So, productivity in the first half has been about 4%. We expect that to be even greater than that in the back half. Inflation has been around about 2.6%, 2.7% in the first half, and we'll see a little bit of an acceleration for that to get to the guidance range that we talked about. What we articulated in terms of the margin pressure for the quarter, obviously, is that we've experienced $21 million of discrete costs, $5 million of that being strategic investments.

And there'll be another $10 million, which will flow through the residual two quarters, with most of that being in Q3. So, clearly the one-time nature of the recall costs and some of the enhancements in Jackson don't replicate themselves in Q3, but some of the strategic investments do, and you do get a bit of a water-falling of those costs that have been incurred already actually hitting the P&L in Q3 and a little bit in Q4.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Yeah. You know, I think generally your approximation is not far off. I do think you will see a bit of a headwinds remaining in Q3 with momentum building as we exit the year and then certainly going into 2018.

Steven Strycula
Analyst, UBS Securities LLC

Q

Great. That's helpful. And then one quick follow-up on M&A strategy. You know, if we take a look at the past few acquisitions you've executed, there's been a little bit of a spear-fishing approach with gardein and Wish-Bone going after single brand assets, and then with Boulder, you did a little bit of a portfolio approach, and taking in five brands and it's delivered really nice synergies. Can you help us think how we should think about going forward given that you had success on both fronts, and now that you're a larger company and you've had a lot of learnings, just how these past transactions have influenced, how you think about going forward?

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Yeah. I mean, I think that's actually a fairly good depiction of the optionality that we have, and I think you will see us continuing to work both sides of the aisle, if you will. I think with the Boulder integration behind us and the platform that we've established there, the ability to continue to add to that platform with good tack-on acquisitions that enable us to strengthen our position in gluten-free, clean convenience or plant-based is a priority for us going forward.

What I don't think you're going to see us do is go out and add complicated businesses that have a large number of entities that would distract us for a long period of time to go through that integration. I say we're much more interested in either portfolios that are integrated or individual businesses. You know, at the end of the day, I think the playbook that we have been utilizing, where we are looking for North American-based businesses in our categories or adjacent, number ones or twos, so we can manage these brands after we get them into the portfolio, accretive deals, so you're not going to see us overpaying for any assets, and the speed in which we can integrate will continue to be the key decision factor for us, both on larger and smaller acquisitions, both within center-of-store iconic brands and faster-growing or faster-moving health and wellness brands.

Craig D. Steeneck
Chief Financial Officer & Executive Vice President, Pinnacle Foods, Inc.

A

And Steve, I'm sure you noticed the leverage ratio now is below 4.2 times, I mean exactly what we said when we've done the Boulder acquisition, on its way to 4 times or below by year-end. So, the Boulder integration is now complete. We paid off some debt earlier in the year with the refinancing. We're continuing to de-lever. We're certainly getting the balance sheet ready and have some dry powder as we move forward to execute exactly what just Mark just articulated.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Yeah. Vigilant and disciplined, I think is what we said last quarter. We certainly remain on that track and focused and ready. And again, you can trust that if there are things out there, we're going to take a look, but we are not going to lose that discipline portion of it. And as I have said before, the most powerful ally in us making these decisions is the confidence and conviction to the organic plan that we have, and that will continue to be foundational for us as we go forward.

Steven Strycula
Analyst, UBS Securities LLC

Q

Thanks. This was very helpful.

Mark A. Clouse
Chief Executive Officer & Director, Pinnacle Foods, Inc.

A

Thank you, Steve.

Operator: Thank you. I'd now like to turn the conference back over to management for any closing remarks.

Maria Sceppaguercio
Senior Vice President, Investor Relations & Communications, Pinnacle Foods, Inc.

Thank you, Howard. Thanks, everyone, for listening in today. I think we went a few minutes over, so I apologize for that. We wanted to take as many of your questions as we could possibly get to. I am around all day, so don't hesitate to reach out if you have any follow-ups. Take care. Have a good day.

Operator: Ladies and gentlemen, thank you for participating in today's conference. This concludes the program. You may now disconnect. Everyone, have a wonderful day.