

J&J Snack Foods Corp. (Q1 2025)
February 4th, 2025

Corporate Speakers

- Norberto Aja; J&J Snack Foods Corp.; Investor Relations
- Daniel Fachner; J&J Snack Foods Corp.; Chief Executive Officer
- Shawn Munsell; J&J Snack Foods Corp.; Chief Financial Officer

Participants

- Todd Brooks; Benchmark Company; Analyst
- Andrew Paul Wolf; CL King; Analyst
- Robert Dickerson; Jefferies; Analyst

PRESENTATION

Operator^ Good day. Welcome to the J&J Snack Foods Fiscal 2025 first quarter Conference Call. As a reminder, this call may be recorded.

I would now like to turn the call over to Norberto Aja, Investor Relations. Please go ahead.

Norberto Aja^ Thank you, Operator. And good morning, everyone. Thank you for joining the J&J Snack Foods fiscal 2025 first quarter conference call. Before getting started, let me take a minute to read the safe harbor language. This call contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements made on this call that do not relate to matters of historical facts should be considered forward-looking statements including statements regarding management's plans, strategies, goals, expectations and objectives as well as our anticipated financial performance.

These statements are neither promises or guarantees and involve known and unknown risks, uncertainties and other important factors that may cause results, performance or achievements to be materially different from any future results performance or achievements expressed or implied by the forward-looking statements.

Risk factors and other items discussed in our annual report on Form 10-K for the year ended September 28, 2024, and our other filings with the Securities and Exchange Commission could cause actual results to differ materially from those indicated by forward-looking statements made on the call today. Any such forward-looking statements represent management's estimates as of the date of the call today February 4, 2025. While we may elect to update forward-looking statements at some point in the future, we disclaim any obligation to do so even if subsequent events cause expectations to change.

In addition, we may also reference certain non-GAAP measures on the call today including adjusted EBITDA, adjusted operating income or adjusted earnings per share --

all of which are reconciled to the nearest GAAP measure in the company's earnings press release which can be found in our Investor Relations section of our website.

Joining me on the call today is Dan Fachner, our Chief Executive Officer, along with Shawn Munsell our Chief Financial Officer. Following management's prepared remarks, we will open the call for a question and answer session.

With that, I would now like to turn the call over to Mr. Fachner. Please go ahead, Dan.

Daniel Fachner^ Thank you, Norberto. Good morning, everyone. Thank you for joining us today to discuss our fiscal Q1 results. Starting with a quick review of our first quarter results. We delivered solid top line growth of 4.1% to \$362.6 million, driven by a combination of volume increases and pricing. However our performance was impacted by a less than favorable sales mix along with the input cost inflation that was not fully covered with price increases. And although we delivered strong earnings improvement in the Frozen Beverages, foreign exchange headwinds associated with the peso limited the improvement.

Overall, gross margin declined to 25.9% from 27.2% compared to the prior year. The gross profit decline along with the higher operating expenses ultimately impacted our bottom line for the quarter. The unfavorable mix impact during the quarter primarily reflects two items. The first is the loss of some seasonal business within bakery, with a declining margin profile that we bid on but did not retain.

The second is attributed to lower churros volumes in Food Service, as we lap the benefit from a limited time offer with a quick-serve restaurant last year. Although we were able to grow volume elsewhere in the portfolio to help compensate for these losses, the mix was less favorable. Our cookie volume is up meaningfully versus the prior year, and we've recently invested in new capacity to augment our capabilities. We also added new churros customers in Food Service and believe this business will continue growing over time. Regarding pricing, while we realized price increases during the quarter, we were not able to fully offset the net impact of the higher input costs.

We experienced significant inflation in chocolates, eggs and proteins that was only partly offset by deflation, primarily in flour and dairy. We have implemented additional pricing action in the second quarter for select categories that will further mitigate input cost inflation. We also had some nice wins across the portfolio that helped to support our results during the quarter. Our Frozen Beverage business achieved record first quarter results on a rebound in theater traffic as the movie lineup recovered from last year.

We achieved record results despite an unfavorable year-over-year weakening of the peso that impacted our Frozen Beverage performance in Mexico. We also delivered strong results in frozen novelties across the portfolio, led by the growth in Dogsters and Dippin' Dots. Food Service pretzels recovered in the quarter mainly from a rebound in the convenience store channel and elsewhere.

While we're not satisfied with our results, we view the underlying challenges as temporary.

As I mentioned, we have implemented incremental pricing that has taken effect early in the second quarter. And as always, we continue to pursue volume growth and mix improvement across the portfolio. Encouragingly, Frozen Beverages and snacks showed sequential improvement during the quarter, supporting confidence in our recovery trajectory. We remain disciplined and focused on the business principles that have driven long-term success and shareholder value. To that end, I am pleased to announce that our Board has approved a new \$50 million stock repurchase authorization. This decision reflects our confidence in J&J's long-term value and our financial flexibility.

With a strong balance sheet and ample liquidity, we are well equipped to execute this plan opportunistically while continuing to invest in organic and inorganic growth opportunities. We remain disciplined and thoughtful in deploying capital, ensuring that any investments we make deliver sustainable value for our shareholders. Let me now briefly review highlights from each of our three business segments.

Starting with Food Service. This segment continues to grow, driven by innovation and strategic partnerships despite some unfavorable changes to the sales mix. We realized 4.5% sales growth across Food Service, led by a 4.8% increase in soft pretzels as convenience store sales rebounded. Frozen novelties increased an impressive 9.8%, which included 8.4% sales growth in Dippin' Dots, driven by the theater and our new vending channels. Churros sales declined 9.2%, reflecting the lapping of a limited time offer volumes that I referenced earlier. Bakery sales growth of 6.6%, largely reflects price increases to offset input cost inflation.

As for Retail, we saw opportunities and challenges that led to a 2.2% increase in sales. Frozen novelty sales increased meaningfully, led primarily by volume gains in LUIGI'S and Dogsters which outpaced declines elsewhere in the retail portfolio. The soft pretzel sales decline of 7.4% was partly attributed to an ordering system issue with a large customer that temporarily suppressed volumes. Resolution of this issue in late December positions us for improvement in Q2. Frozen Beverage sales increased 4% driven by an impressive 10% volume increase. The boost in volume was attributed to 45% growth in theater channels compared to the prior year thanks to strong content releases in November and December.

In addition to volume growth, machine revenue increased by 13%, offsetting a 3.7% drop in maintenance revenue. As it relates to our end markets, the outlook for the 2025 North America box office is strong with growth projected at over 10% year-over-year driven by a recovery from last year's strike. The industry has demonstrated remarkable resilience, and we remain optimistic about its long-term recovery and growth trajectory.

We're seeing a continuation of growth in overall consumer spending on leisure, entertainment and experiential categories, which are outpacing traditional retail channels. Leisure and entertainment segments, in particular, are performing better now than they did pre-pandemic as consumers prioritize memorable experiences. These trends provide a strong tailwind for our business as we look to align with these evolving preferences.

As we've demonstrated, our growing presence in the theater and entertainment channels, especially through ICEE and Dippin' Dots positions us well to take advantage of these trends. With regard to our operations and logistics, our supply chain initiatives driven by the addition of three new RDCs are delivering as planned by increasing capacity and improving the efficiency of how we move products to customers.

With operations now spanning nine cold storage facilities, we have simplified logistics management across our network and lowered our inventory levels without compromising service. Currently, over 94% of our sales orders are shipped from the new distribution network compared to under 30% a year ago. This has resulted in more than a 12% reduction in average haul length, improved on-time performance and decreased line haul costs 13% per pound in our snack food business compared to the same quarter last year.

Moving to the marketing front. We're investing heavily in digital and shopper marketing to drive conversion across key brands like SUPERPRETZEL, LUIGI'S and Dogsters. In Food Service in particular, we're maintaining strong business-to-business marketing efforts focused on soft pretzels, churros and funnel cakes with direct-to-operator engagements driving leads.

I want to highlight progress against a couple of our growth initiatives. We have made great progress on the rollout of Dippin' Dots to the theater channel. We increased our presence by 186 locations or about 21% in the first quarter. We're also excited about the recently launched Dippin' Dots Sundaes for Retail, which represents a great entry into the retail channel for this iconic brand. The new sundaes hit the shelves in January with a large retailer and will reach other retailers throughout the quarter.

As it relates to capital deployment, our strong balance sheet and strong liquidity position provide us with the flexibility to pursue strategic opportunities including M&A that align with our long-term growth objectives. We remain disciplined and thoughtful in deploying capital, ensuring that any investments we make deliver sustainable value for our shareholders.

In summary, while Q1 presented challenges, we believe they are short term in nature and remain confident in our ability to leverage the strength of our diversified product portfolio and iconic brands. Looking ahead, we remain focused on driving incremental placements, fostering innovation and expanding partnerships, which will position us well for sustained growth and value creation. I'd like to thank all the team members at J&J for their discipline and dedication to our long-term success. Thank you for your continued support.

I'd now like to hand the call over to Shawn.

Shawn Munsell^ Thank you, Dan. And good morning, everyone. Looking at our fiscal first quarter results, revenue increased 4.1% to \$362.6 million, marking a Q1 record. As Dan mentioned, we experienced increased sales across the portfolio from a combination of volume and price increases. Food Service revenue increased 4.5%, Retail was up 2.2% and Frozen Beverage grew 4%. Cost of goods sold increased 5.9% to \$268.7 million,

leading to a gross profit of \$93.9 million compared to \$94.6 million in the year-ago period, while gross margin declined to 25.9% from 27.2%.

As Dan mentioned, despite the top line growth compared to the prior year, price increases lagged input cost inflation, and we also experienced some unfavorable mix changes associated with our bakery business as well as the loss of limited time offer churros volumes from last year. Record Q1 Frozen Beverage performance supported results despite headwinds from a weaker peso related to our Mexico business.

Additionally, hurricane impacts contributed to an estimated \$600,000 of lost gross profit. Moving down the income statement. Total operating expenses were 24.2% of sales as compared to 24.4% last year. Overall, operating expenses increased 3.3%. Marketing expenses were 7.9% of sales in line with last year's percentage of sales. Overall, marketing and selling expenses increased 4.4%. Almost half of the year-over-year increase was related to increased brand amortization expenses associated with the legacy Churros brand that is being phased out for the Hola. Churros brand.

Distribution costs were 10.9% of sales, down from 11.6% in the prior year. The decline primarily reflects the impact of start-up costs at our regional distribution centers last year. Absent those impacts in the prior year, distribution costs would have been approximately in line with last year's percentage of sales. As volume ramps up over time we expect the distribution cost rate to decline. Administrative expenses were 5.2% of sales, in line with the prior year. Other general expense increased \$1.6 million year-over-year, primarily reflecting favorable impacts in the prior year period.

Operating income for the quarter declined to \$6.2 million from \$9.7 million, reflecting the near-term pressures on profitability. Adjusted operating income was \$8.2 million compared to \$13.5 million last year. The effective tax rate was 27.2% for the quarter compared to 26.6% in the prior year. This resulted in net earnings of \$5.1 million compared to \$7.3 million in the first quarter of fiscal 2024 and earnings per diluted share of \$0.26 versus \$0.37 in the prior year period.

Adjusted earnings per diluted share were \$0.33 versus \$0.52 in the prior year quarter. Adjusted EBITDA declined to \$25.3 million from \$30.2 million in the first quarter last year. Taking a look at our balance sheet and cash flow. We continue to have a healthy balance sheet and liquidity position with \$74 million in cash and no long-term debt at quarter end. During the quarter, we generated approximately \$16 million in free cash flow, and we had approximately \$213 million of borrowing capacity under our revolving credit agreement.

In closing, although the quarter presented some challenges that we're navigating, we're encouraged by some of the positives we've seen this quarter, particularly with the recovery in theater traffic given our presence in that channel. Our top line continues to grow from a combination of price and volume growth. Our bakery business has experienced some challenges, but it does provide some contractual protection from input cost volatility. The Dippin' Dots rollout to theaters is progressing smoothly, and new product launches are poised to drive further growth, positioning us well for the year

ahead. Additionally, a strong balance sheet and cash generation continue to provide us with the flexibility to invest in the business.

Before I turn the call over to the operator, I want to thank Dan, our Board of Directors and every member of the J&J team for their warm welcome.

I would now like to turn the call over to the operator for questions and answers.

QUESTIONS AND ANSWERS

Operator^ (Operator Instructions) And our first question comes from the line of Todd Brooks of the Benchmark Company.

Todd Brooks^ Welcome aboard, Shawn. Good to have you. Is there a way that you could provide kind of a gross margin bridge for the decline year-over-year kind of parsing out for us? How much was commodity related, peso related and mix related? I think that would be helpful.

Shawn Munsell^ Yes. Yes. So in simple terms, Todd, if you look at the decline from where we were last year to this year in gross margin, you've got about 80 basis points that we associate with what I would call the gap in pricing relative to input costs. The balance of that is really coming through a mix with the loss in our bakery business. That's just simple broad strokes. When you think about the foreign exchange impact relative to last year, keep in mind that we have a relatively large Frozen Beverage business in Mexico, had a really solid quarter, but there was a headwind associated with the peso. So the peso weakened about 20% versus prior year. That amount is -- that's almost \$1 million.

Todd Brooks^ Okay. Great. And just a more structural question. How does this kind of creep up in such a dramatic fashion over the course of a quarter? And as we're taking additional price actions in the current quarter, I think the comment in the release was that those actions would help to further mitigate some of these pressures that you just highlighted, but it doesn't necessarily imply that it's being fully mitigated. So just kind of the thoughts on taking pricing. How much of these kind of, especially commodity pressures, you think you can mitigate and maybe tie that into a view for gross margin potential for the full year?

Shawn Munsell^ Yes. Sure. So again going back to my earlier point, if you take the price increases and keep in mind, these price increases have already been implemented in the quarter. Most of those were implemented in January, some roll through in February, but that is behind us. The magnitude of the pricing that we've taken, had it been, say retroactive to Q1, that would have closed right around 80 basis points of that gross margin contraction.

So again not to imply that, that's going to cover all of the ingredient cost inflation, but it's going to help to cover a fair bit of that gap that we experienced in Q1. And just as it relates to the ingredient cost inflation, the input cost inflation year-over-year, we did have some relief in flour, we had relief in dairy and some other items. But when you look at

chocolates and you look at eggs, just the unit cost of both of those products have nearly doubled on a year-over-year basis.

Surely, we would have liked to have had that pricing implemented in Q1, that didn't happen, but we're confident that we're getting it here in Q2. That pricing that I was just referencing, that's really kind of the snack side pricing. We expect that we're going to have about -- we've already implemented another 4% -- approximately 4% in price increases associated with the Frozen Beverage business, another 3% in Dippin' Dots. But the sales team has worked through this with our customers, and it will make a difference.

Todd Brooks^ That's good to hear. Then finally, is there any worry that with the consumer in a -- maybe let's call it a fragile, but stable place right now that you get the pricing through, but what are you watching and where are you most worried about potential volume response, the downside that would offset some of this benefit?

Daniel Fachner^ Yes. Todd, that's a great question. Good talking with you. We're watching that really closely and we will continue to watch it closely. But as you know some of these increases that we've received from things like chocolates and eggs are pretty standard wide across the industry. So we're going to have to pass some of those on, and then just watch what happens at the end user. We've been fortunate enough to be able to grow volume across the organization and even this quarter, having a 4.1% increase. So we'll watch it closely, but we do feel like we need to pass those increases on.

Shawn Munsell^ Just to build on that, I mean we've been selective in terms of where the pricing is being implemented, what products. So it's not as if, it's just across the board.

Operator^ And our next question comes from the line of Andrew Wolf of CL King.

Andrew Paul Wolf^ Great. Sort of have a -- start with a follow-up on what Todd was -- some of the -- where he was sort of going at. So this is like, if you adjust for the hurricane, the second quarter in a row where the gross margin contracted roughly 100 basis points or a little more. So I mean is there any systems issues with regard to tracking costs and being time -- picking them up in a timely enough manner? Or are there contractual issues where you just can't bump the price up that immediate because you're stuck in a contract? Or is it more trade relations where certain price increases only come through with certain customers kind of on a fixed schedule? Can you help us just understand why the -- from the outside, why it's sort of half a year of price increases and - of cost increases or the amount -- and now we're seeing price realization, a little bit sort of lagging.

Shawn Munsell^ Yes. Sure. Great question. This, I would describe this as not being a matter of visibility. This was predominantly a function of just the time that it took to get these price increases through to our customers. There's been a lot of price increases in the industry for sure, given what we've seen in those inputs. And so it just -- it took a little bit more time than we were planning for to get that pushed through.

Daniel Fachner^ Andrew, this is Dan. Shawn is spot on there. Todd just asked the question about the customer and what happens to the end user as these prices go up.

Whenever you're raising prices, it's a touchy subject to go after. Sometimes you're under contracts, sometimes there's a lag of time that it takes to get there. We believe that we have that covered as we go into the second quarter, but yes, there's [definitely] a lag going into it.

Andrew Paul Wolf^ Okay. So roughly, again taking out the hurricane impact, the 20 to 30 basis points that isn't yet covered. Is that pretty much all mix?

Shawn Munsell^ Yes. That's right.

Andrew Paul Wolf^ And to the extent it is, can you kind of -- is it more to do with losing the high-margin churros? Or is it within the bakery business? Any specificity on how you -- how that sort of gets better going forward is helpful.

Daniel Fachner^ We really had two things that happened in the quarter. One is, as you mentioned, the high-volume churros business from a QSR that was really promoting it strongly. We'll do that in the second quarter. We still have to face that a little bit as well. The other is we lost some pie business at a major retailer that is really seasonal. The only impact that it has is in that first quarter, but that also had an impact on us. We retained the no sugar added piece of the pie business, but we lost the other as it became more competitive, and we've been on it and just did not retain the bid.

Shawn Munsell^ Yes. I would describe that as being pretty attractive margin profile last year on the pies. But that margin wasn't going to hold this year given some of the competitive pressure. We bid on it at a lower price, ultimately didn't -- weren't awarded it, but it was -- in the prior year, it was a healthy margin, same with the churros.

Andrew Paul Wolf^ So last thing, if we wanted to build back your operating profit by segment, I guess we would take most of the 80 basis points into the profit in Food Service and most of the 20 basis points for mix into the profit for food retail...

Shawn Munsell^ Yes. Yes. That's right. Yes.

Andrew Paul Wolf^ And did you -- how much did the peso impact profitability for the beverage -- gross beverage?

Shawn Munsell^ Yes. It was -- look, it was close to \$1 million impact for the quarter. It's a pretty substantial business down there. And keep in mind, it's just -- we've reached that period where you're lapping, the peso was trading around 17% last year at this time and now we're up around 20%. So it was close to a 20% impact.

Operator^ And our next question comes from the line of Robert Dickerson of Jefferies.

Robert Dickerson^ I guess just a couple of questions, hopefully, not too hard. Dan, maybe first question. I know you had a comment in the prepared remarks around just kind of recovery in the convenience store channel, and maybe if you could just spend a little time trying to provide a little bit more color as to kind of what you're seeing actually

in that channel, maybe more broadly speaking? Then also just kind of specific to kind of what's working for you more within the channel? That's the first question.

Daniel Fachner^ Yes. The reference there was our pretzel business growing inside the convenience store channel. We have a really strong team associated with that today and they've gone out there and found some good new business over the last six months or so, and we're seeing a nice recovery where maybe some of that business has lagged over the last year. I like what our team is doing, and I see a good recovery in that portion of our business.

Robert Dickerson^ Okay. Cool. Super. Then maybe just kind of, again broadly on the gross margin side. I clearly understand everything you said so far around kind of the cost-price differential in the near term, there's some contractual protections and probably certain products, certain commodities. Then -- but then I also hear you're kind of like ongoing growth potential such that movie channel traffic can improve, the lineup looks good, et cetera, et cetera, with maybe still a little bit of kind of margin pressure in Q2.

I mean it doesn't sound like it would be as much, let's say just given some of the pricing catch up. But as we kind of think about like first half, back half. I feel like we talk about J&J a lot first half, back half just because of the seasonality of the business. As we sit here today like could we be in a situation such that as we're in the back half of the year that, that gross margin could actually wind up being at least flattish, let's just -- like argument's sake, right? Pricing comes through, some of the one-offs kind of go away maybe traffic, movie channel picks up. Just trying to gauge how you're kind of thinking about that one line item as we look through the year?

Daniel Fachner^ Yes, Rob, great question. I'm going to let Shawn answer some of it, and then I'll add some color to it. But thank you for that question.

Shawn Munsell^ Yes. Good question. So the way I would portray that is when we think about the second half, we're -- the goal here, our expectation is that we're going to get back to that low 30% gross margin level. This quarter, the second quarter, I would describe that as being sort of transitional between Q1 and the back half. The one headwind that we really face in the second quarter is the churros volumes that we had last year.

So we had pretty significant QSR churros volumes for the Super Bowl. We've added new churros customers, but we don't expect to see the same volume in churros this second quarter that we did last year. That's a relatively attractive business. But when you look at the second half of the year, the expectation is that we still get back in that low 30% gross margin range. And keep in mind that just the seasonality of the business, that's where you're going to start to see more help from the Frozen Beverage and the Dippin' Dots in the portfolio.

Daniel Fachner^ Yes. You mentioned in that -- in your conversation that the theaters and the theaters do anticipate being up 10% year-over-year. As you know we've continued to grow inside the theaters with Dippin' Dots and with ICEE and really on our snack food side, too. Then there's some good wins across the business as we enter into the second

half of the year. We feel pretty confident that we'll be back into that range that we were last year, if not better, by the time the year is up.

Robert Dickerson^ Okay. Okay. Super. That's very helpful. Then I guess just quickly on Dippin' Dots. Again Dan, I thought I heard you -- I just missed it a little bit from the detail, so I'm sorry, but I thought I heard you speak to kind of a new retailer you're entering or have entered with Dippin' Dots, and you clearly were sitting here early February. I mean that is a product that, again probably would have some seasonal lift. So maybe just kind of spend two seconds on kind of the magnitude of that retailer. Is that like a large national retailer, a lot of units, the majority of their locations? Just trying to get some sense as to how material that is.

Daniel Fachner^ Yes. We're really excited about the release of the Dippin' Dots into retail, and we've had great acceptance really all across the board. We did kick off with a major retailer that's nationwide in January. Then it will be in the market really in all of them by the time we get into mid-February. Then you'll see it grow across retailers all throughout the quarter. Really great acceptance to the new product. So far, the early readings of the sell-through have been really good. So we're watching it closely, but we have a lot of really high hopes on that particular product.

Robert Dickerson^ All right. Super. Then just last quick one for me is just the repo authorization. We don't see that every day come from you while at the same time also speaking to always actively looking for kind of the next attractive acquisition opportunity. Should it just be assumed at this point that like, well absent an acquisition opportunity that yes, we will look to repurchase at least some of our stock and especially just kind of given where valuation sits today relative to history? That's all.

Shawn Munsell^ Yes. I'll take that one. Yes. So I described this as just being consistent with the company's capital deployment strategy. Our objective, of course is to deploy capital that we think generates value for shareholders over time. We see compelling value in the shares. I will say that our plan is to be opportunistic in terms of the pace and the timing, but I would view this as being complementary to the rest of the capital deployment strategy. This isn't something that is kind of an and/or with -- that's an or with respect to M&A. So yes, it's just a consistent approach is the best way to describe it.

Operator^ I'm showing no further questions at this time. I'd now like to turn it back to Dan for closing remarks.

Daniel Fachner^ Thank you, Operator. In closing, we are executing our strategy effectively in a dynamic operating environment, and we remain confident in our ability to achieve our goals, both in 2025 and over the long term. I'd also like to take a moment to commend Shawn on his smooth transition and ability to quickly take a leadership role within our organization. We look forward to sharing our fiscal 2025 second quarter results with you. And in the meantime if you have any questions or would like to connect with us, please reach out to our Investor Relations team at JCIR at (212) 835-8500. Thank you. And have a wonderful day.

Operator^ Thank you for your participation in today's conference. This does conclude the program. You may now disconnect.