Management's Prepared Remarks

Q4 2023 Earnings Call

February 14, 2024

JP O'Meara

Senior Vice President, Head of Investor Relations

Thank you operator, and good morning everyone.
I am delighted to welcome you to our Q4 2023 results conference call.

On today's call are Frans Muller, our President & CEO and Jolanda Poots-Bijl, our CFO. After a brief presentation, we will open the call for questions.

In case you haven't seen it, the earnings release and the accompanying presentation slides can be accessed through the Investors section of our website aholddelhaize.com, which provide extra disclosures and details for your convenience.

To ensure everyone has the opportunity to get their questions answered today, I ask that you initially limit yourself to 2 questions.

If you have further questions then feel free to re-enter the queue.

To ensure ease of speaking, all growth rates mentioned in today's prepared remarks will be at constant exchange rates unless otherwise stated.

I'll now turn the call over to Frans.

Ahold Delhaize

Frans Muller

President, Chief Executive Officer

Thank you JP, and good morning everyone.

I am pleased to report a solid fourth quarter, and end to 2023.

Taking a quick look at our scorecard, we achieved or exceeded all of our key goals for the year. Jolanda will go through these numbers in more detail, but first let me share some of our operational highlights for context.

Reflecting on the year, it clearly wasn't an easy one – not for societies worldwide, nor for businesses. Our teams around the world had to adapt to dynamic, and in many cases, volatile market conditions.

Through it all, we achieved a lot – delivering on our commitments, and advancing key strategies for our long-term success.

For this, I would like to thank our over 400 thousand strong dedicated and passionate associates, for living our values and continuously feeding our winning culture.

This culture starts first and foremost with serving our existing and growing customer base of over 63 million. With high inflation rates impacting the entire value chain, we have been steadfast and left no stone unturned to create value for them.

We expanded our high-quality own brand assortments. We optimized and personalized our loyalty programs. And we ensured that every day, the best of our value proposition was presented for our customers in a clear and seamless way at each touchpoint of our various omnichannel shopping experiences.

To fund this, disciplined cost management has been as important as ever, especially as global conflicts create volatility in supply chains. Inflation in operating costs also played catch up during the year with the lofty levels of headline inflation numbers from 2022.

Those of you who have followed us for a long time KNOW that we are not afraid to roll up our sleeves in such climates. And I firmly believe our track record in cost control is second to none as you can see on slide 8. Our teams delivered a new record high in our long standing Save for Our Customers program, generating over 1.25 billion euro in cost savings, or 29 percent above the prior year level.

In addition to this, I am also proud of our continued support of local communities. Our role as a company goes beyond just the prices on the shelf. It is also our responsibility to help with broader societal challenges provide access to healthy food and foster a nurturing environment for associates to thrive. To this end, our brands contributed more than 240 million euro in charitable cash, product and food donations to local and regional food banks and non-profit organizations throughout the year.

Growing faster than the market is one of the long-term ambitions that keeps us sharp and focused.

Three areas in particular matter: 1) Vibrant, modern stores and shopping experiences 2) high-quality high-value product assortments, and 3) simplifying our go-to-market models to excel on the aspects that really make the difference for our customers. Let me give you an example of each.

For example, at Food Lion, we continue to elevate the brand's fleet of stores to our best-in-class omnichannel format. In 2023 alone, we remodeled more than 10 percent of the store fleet. This perpetual cycle of store elevation has in no small way contributed to the now 45 consecutive quarters of comparable store sales growth.

At The GIANT Company, we are also moving at a fast pace with now more than 60% of the store fleet on the latest 'For Today's Table' floor design, and the brand is also punching above its weight in loyalty & digital with Giant Choice Rewards ranked in the top 10 of dunnhumby Retailer Preference Index.

In Europe, one of the key drivers of returning volumes to growth for the first time in 10 quarters is the extensive roll out of our entry-priced high-quality own brand assortments. In the region, we now offer more than 7,000 Price Favorites products at entry price level, and our ambition is to further increase this with 20 percent in 2024. Albert Heijn is a great example of own brand execution, which it is leveraged extensively to help customers save and get the most for their wallets over the last quarters of high inflation. And customers love our products with 16 own-brand products named "Best Product of the Year" in the Netherlands.

An example of where we simplified our go-to-market model is Delhaize Belgium. Almost a year now since the team started its Future Plan, Delhaize has finalized agreements to franchise 107 of the 128 own operated stores. And the good news is – we already see promising results from the over 40 stores that have already transitioned – with customer frequency and basket size trending upwards. This means markets shares have stabilized and increasing market share won't be far behind. This project took conviction and perseverance from the team in Belgium, but with the right plan for customers and associates, the organization will be in stronger shape to win in the market moving forward.

In addition, we also took some meaningful decisions as part of our yearlong "Accelerate" initiative, which we launched at the beginning of 2023 to create more agile organizations, further leverage our scale and empower our people to take action to drive efficiency. The operating model harmonization in the CSE region, the divestment of FreshDirect and the move to a more asset light approach in online fulfillment in the U.S. are just some of the areas we worked on that will yield important savings, which we will reinvest in growth in 2024.

Finally, let me spend a moment on Health & Sustainability.

Our brands continued to implement projects to promote healthy, affordable food, and drive sustainable business practices like reducing food waste and energy consumption and promoting diversity and inclusion in the workplace. These topics remain key and align very closely with our Group values.

At the end of 2023, we launched our updated climate plan in which we refined decarbonization levers and sharpened the categories for our emission reduction targets.

We will host a dedicated session on this and other topics at our upcoming Strategy Day in May. More on that later. Now let me hand you over to Jolanda, to share her remarks on the financials as well as on our key Health & Sustainability KPI's.

Jolanda Poots-Bijl

Chief Financial Officer

Thank you Frans and good morning to everyone.

Looking at our financial performance, the strength of our international portfolio allowed us to deliver a consistent set of results. We are maintaining high performance in challenging market circumstances.

On slide 17 and 18 we present you the key underlying numbers for the quarter and the full year. To summarize, for the quarter:

- Q4 net sales grew 1.9 percent, to 23 billion euro
- Net consumer online sales increased by 2.6 percent to 3.3 billion euro
- Group underlying operating margin was 4.3 percent, a decrease of 10 basis points versus last year
- Diluted underlying earnings per share for the quarter were 73 euro cents, up 2.5 percent at actual rates.

For the full year:

- Net sales grew 3.8 percent to 89 billion euro
- Net consumer online sales increased 5.9 percent to 11.9 billion euros
- Our underlying operating margin for 2023 was 4.1 percent

- Full year diluted underlying EPS were 2.54 euro, in line with the Company's original guidance of around prior year levels of 2.55.
- Our free cash flow was 2.4 billion, finishing at the higher end of our guidance.

Looking into various line items in more detail.

Starting with revenues. On slide 19, you see comparable sales growth by region including and excluding weather, calendar and other effects.

Q4 Group comparable sales were 1.8 percent which includes a negative impact of 0.3 percentage points from weather and calendar shifts, primarily related to the timing of New Year's Eve.

In the U.S., comparable sales ex. gas declined 1 percent or half a percent excluding calendar shifts, as inflation rates moderated and we continued to lap the end of the emergency SNAP benefits program which ended in Q1 of 2023. On its own, the reduction in SNAP benefits resulted in approximately a four percentage-point headwind to sales. Against the backdrop of a declining grocery market in the fourth quarter, especially Food Lion and Hannaford continue to excel with positive growth rates – both brands also showing double-digit growth in online sales.

In Europe, comparable store sales were up 6.5 percent in Q4. This is a strong result, and comes along with the first positive volume trends in over two years. Key to this milestone has been our brands' relentless focus on rolling out local everyday low-price programs as Frans already explained.

We saw very strong growth in online grocery sales which were up over 9 percent with accelerating growth at Albert Heijn. I think it is fair to say Albert Heijn won the holiday season in the Netherlands finishing the year with over 37 percent market share, which is being supported by more than 950 thousand AH premium subscribers.

In our CSE markets, we continue to see positive market share gains in most markets as the teams benefit from further collaboration and harmonization of products and processes. One specific CSE brand I would like to call out is our Czech brand Albert, which had its 8th consecutive year of positive comparable sales growth. As you know this region is important to us. With the acquisition of Profi on the horizon, we see the CSE region as a meaningful differentiator in terms of growth and a profit driver for our company.

Finally on Europe, a word on bol. Despite difficult market conditions for eCommerce and general merchandise, 2023 was a good year for bol. GMV (“gross merchandise value”) increased 5 percent to 5.8 billion euro, with good traction in multiple categories. We also saw strong double digit growth in value added services such Advertising and Logistics which grew almost 50 and 20 percent for the full year, respectively. In addition, due to the extensive cost savings work of the prior year, underlying EBITDA also improved growing from 125 to 151 million euro.

Moving on to Group profitability as a whole, the Group’ s underlying margin was 4.3 percent in the fourth quarter, representing a slight compression compared to a year ago. One-off adjustments in the U.S. partially offset declines in our European margin and lower insurance benefits at the Global Support Office.

Underlying operating margin in the U.S. was 5.2 percent, up 0.4 percentage points primarily due to a favorable reserve release, one-off settlements and a modest margin mix benefit from the divestment of FreshDirect. This was partially offset by an increase in shrink which continues to be a focus area of our brands. Our U.S. brands are deploying additional solutions in stores to counter this negative trend, including a strong focus on ensuring the safety of our associates and customers. Excluding one-offs, U.S. margin would have been around 4.5 percent which is comparable to the prior year margin, adjusted for one-offs.

Underlying operating margin in Europe was 3.7 percent, down 0.3 percentage points. The impact on Q4 European margins from the Belgium transformation and energy was minimal. Investments in higher wages and in our value proposition were partially offset by a decrease in the non-cash service charge for the Dutch employee pension plan, consistent with the prior quarters. With lower discount rates in the Netherlands, the latter will be a headwind in 2024 of around 10 million per quarter.

Given the various transformation initiatives that took place in 2023, there was quite some difference in our results on an IFRS basis which you can see on slides 24 and 25. Let me give you some additional color on the major moving parts.

Our Group operating income for the quarter was 675 million euro, representing an IFRS operating margin of 2.9 percent, mainly impacted by:

- 250 million euro loss on the divestment of FreshDirect.
- 60 million euro in restructuring and related costs pertaining to Belgium and other Accelerate initiatives.

For the full year our Group operating income was 2.8 billion euro, representing an IFRS operating margin of 3.2 percent, mainly impacted by:

- 266 million euro on impairment charges related to FreshDirect and Belgium store assets;
- 250 million euro losses on the divestment of FreshDirect; and
- 189 million euro of restructuring and related charges, related to Belgium and other Accelerate initiatives.

On slide 26, I would like to give a bit more color on the overall impact of the divestment of FreshDirect on our operational results and our cash flow. For the full year we absorbed 415 million in non-recurring items on our operating income, while we included 130 million in our cash flow as part of our cash from investing activities. As the majority of these elements are excluded from our free cash flow, the impact on 2023 free cash flow is 43 million.

And moving on to our free cash flow. Q4 free cash flow was one billion euro, which represents a decrease of 455 million euro compared to Q4 2022. This was mainly the result to changes in working capital as well as increased net investments. The majority of this higher working capital is timing, related to implementation of the netting processes during the SAP transition in the US, where the negative impact in Q3 2022 was reversed in Q4 2022.

Looking at the full year, we realized a free cash flow of just over 2.4 billion euro, which is at the higher range of our most recent guidance, with good improvements in working capital year over year.

Within this number, inflows from the Belgium tax receivable of 377 million euro was partly offset by our outflows of around 200 million euro from the operating cash flow effects of executing the Belgium Future Plan and other Accelerate initiatives such as the ecommerce fulfillment and last mile changes in the U.S., which we discussed last quarter.

To complete the picture, on Slide 29 you can see our net debt bridge year over year, where you can see a slight decline mainly related to FX movements.

With our strong balance sheet, I am also pleased to announce our proposal to increase the dividend per share by 4.8 percent for 2023 to one euro and ten cents per share. This is of course subject to approval at the AGM. We have also initiated the one billion euro share buyback in January, as planned.

Last but certainly not least, let me provide some detail on our Health and Sustainability KPI's, where we can also report improved performance in the four key areas of our Health & Sustainability strategy. Our brands continued to increase the percentage of own-brand healthy food sales, reaching 54.8 percent in 2023. Furthermore, we reduced CO2-emissions in our own operations by 35 percent compared to our 2018 baseline. Our total tons of food waste per food sales was 37 percent lower than our 2016 baseline and we can report a 10 percent reduction in virgin own brand plastic packaging compared to 2021.

We are now already fully focused on 2024 and beyond.

From a financial perspective, for 2024 we expect a predominantly consistent performance year-over-year, albeit with some different phasing across the quarters – as for example, we lap the impacts of inflation rates, SNAP and the various impacts both positive and negative of the transformational initiatives in Europe and the U.S of the prior year. Our Group underlying margin is expected to be at least 4 percent. Earnings per share are expected to be around 2023 levels and free cash flow is expected to be around 2.3 billion euro. Our net capital expenditure guidance of around 2.2 billion euro includes over 200 million of divestments, a large part related to the sale of two meat facilities to Cargill which we announced last week. Our gross capital expenditure therefore will be roughly in line with or slightly below 2023 levels. In this environment of heavily inflated costs in materials and other building related costs, we believe it is also important to remain disciplined and focused on return on investment, recalculating and phasing differently if necessary.

For our reported sales numbers in 2024, there are also a few specific factors you will need to reflect in your expectations this year.

- The divestment of FreshDirect will reduce the amount of 2024 reported net sales and online sales for the U.S. region by 600 million dollars.
- Albert Heijn will stop selling tobacco in 2024, already having done so in its own operated supermarkets. This will have around a 2 to 3 percentage point impact on reported and comparable store sales growth in Europe in 2024.

On that note, I'm looking forward to seeing you all at our Strategy Day in May. For now, let me hand back to Frans to give a little more flavor on how we see the coming year shaping up operationally.

Frans Muller

President, Chief Executive Officer

Thank you Jolanda.

While we will spend quality time together on our strategic initiatives at our Strategy Day in May, here are a few things you can already count on:

- A relentless focus on the customer, our price positioning and assortments, and leveraging the strength of our great local brands;
- Continuing to advance our own-brand strategies, increasing penetration and category depth;
- Further simplification of our organization to sustain growth investments;
- And as always, continuing to be laser focused on cost control and cash flow delivery

Innovation across the board, including in AI, in online, data, and digital – will remain an important differentiator for our company. This year, we will complete the roll out of our proprietary PRISM platform to all U.S. brands. In Europe, we will also deliver an app convergence project which has already started with Albert in the Czech Republic.

In addition, we will continue to increase our ecommerce reach and service levels through more automation and partnerships. Infrastructure projects such as our Home shop Centers in Barendrecht and Zwolle in the

Netherlands, and new partnerships such as Doordash in the U.S. which we announced last week will provide addition delivery options, tap into additional customer journeys, enhancing speed and convenience for customers.

From an organization simplification perspective, you will see further steps taken in 2024 to ensure we continue the momentum and implementation of learnings from the Accelerate initiative we completed last year. As one of those further steps for example, JJ Fleeman has implemented a new support organization structure which will create the environment to reduce overlap and streamline activities in our U.S. support organizations.

And finally, in terms of prioritizing investments and capital expenditure, we will continue to follow our strategy of building a vibrant and modern network of stores & experiences for our great local brands.

This will include a more deliberate and holistic reset of Stop & Shop – to restore competitiveness for the remaining 50 percent of the network we still need to transform.

These are just a few examples, to reiterate our excitement and confidence in the growth opportunities that are ahead of us. And I am looking forward to sharing more live and in person at our Strategy Day on May 22 and 23 in the Netherlands.

With that, I would like to thank you for your continued interest in our company and Operator, please open the lines for questions.

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Cautionary notice

This communication includes forward-looking statements. All statements other than statements of historical facts may be forward-looking statements. Words and expressions such as constant, solid, achieved, key, goals, through(out), commitments, advancing, strateg(ies)/(y), long-term, values, continu(e)/(es)/(ed)/(ously)/(ing), grow(ing)/(th), impact(ing)/(ed), steadfast, create, drive, record, long standing, beyond, responsibility, ambition(s), keeps, offer, further, increase, help, see, project, will, stronger shape, yearlong, remain(ing), align, targets, strength, maintaining, challenging, quarter, full year, reduc(e)/(tion), milestone, accelerating, offset, focus(ed), ensuring, would, transformation, proposition, consistent, mainly, majority, transition, improvements, year over year, proposal, subject to, expect(ed)/(ations), guidance, believe, count on, innovation, important, steps, ensure, momentum, prioritizing, deliberate, transform, opportunities or other similar words or expressions are typically used to identify forward-looking statements.

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