



HOSTESS BRANDS FOURTH QUARTER 2022 EARNINGS CALL

Tuesday, February 21, 2023

Pre-Recorded, Live Q&A Session Scheduled at 5:00 p.m. Eastern

CORPORATE PARTICIPANTS

Amit Sharma, Vice President, Investor Relations
Andy Callahan, President and Chief Executive Officer
Travis Leonard, Chief Financial Officer

PRESENTATION

Amit Sharma

Good afternoon and welcome to the pre-recorded discussion of Hostess Brands' fourth quarter 2022 earnings conference call. This is Amit Sharma, Vice President of Investor Relations and joining me today are Andy Callahan, Hostess Brands' President and CEO and Travis Leonard, Chief Financial Officer.

The earnings release for the period ended December 31, 2022, along with investor presentation was published at approximately 4:00 p.m. Eastern time, and are available on Hostess' website at www.hostessbrands.com.

In addition to these remarks, we will host an analyst question and answer session at 5:00 p.m. Eastern today. A replay of this webcast and our subsequent Q&A session will be available on the Investor Relations section of our website.

During the course of these calls, management will make a number of forward-looking statements, including expectations and assumptions regarding the Company's future performance. Actual results may differ materially from these forward-looking statements, and we undertake no obligation to update or revise these forward-looking statements. A detailed list of these risks and uncertainties can be found in today's earnings release and in our SEC filings.

Management will make a number of references to non-GAAP financial measures that we believe will provide useful information to the investors. A full reconciliation of these non-GAAP measures to the most comparable GAAP measures is included in the earnings release.

With that, I will turn the call over to Andy Callahan, our President and CEO.

Andy Callahan

Thank you, Amit.

I would like to begin by offering a few highlights from our solid quarterly results. I will then offer a few comments on the sustainability of our top-tier performance before handing it to Travis for a detailed review of our quarterly financial results. We will wrap up with a discussion of our initial 2023 guidance.

We delivered another year of strong top and bottom-line growth, surpassing our long-term growth targets across all three key elements of our financial algorithm - net revenue, adjusted EBITDA, and adjusted EPS, as we continue to execute on our key strategic initiatives even in a dynamic operating environment. Our net organic revenue increased by 18.9% during the year, including 2.6% of volume growth, demonstrating the strength and resiliency of our brands and portfolio in a highly inflationary environment.

More importantly, this strong foundation of sustained growth coupled with our superior innovation and execution gives us the confidence to guide to an above-algo year for profitability in 2023 even as we lap strong growth. Specifically, we expect 2023 net revenue to increase by 4%-6%, adjusted EBITDA of \$315-\$325 million, or 7-10% growth and adjusted EPS in the range of \$1.08-\$1.13 which is 10-15% growth over a very strong 2022.

Now to the quarterly highlights.

Our fourth quarter organic net revenue increased by 14% as the over 20% contribution from price/mix was partially offset by lower volume as we lapped 10% volume growth in the year-ago quarter and the impact from multiple pricing actions executed throughout 2022. That said, this was our twelfth consecutive quarter of at least 9% net revenue growth and seventh consecutive quarter of double-digit growth, highlighting the consistency of our topline growth over the last three years. In fact, on a two-year stack basis, fourth quarter net revenue was up nearly 33% and up 57% on a three year-basis, underscoring the sustainability of our topline momentum.

Our price/mix and productivity initiatives enabled us to deliver sequentially better gross margins and positive earnings growth in the quarter even as we absorbed 20% COGS inflation and substantially increased our A&M investments behind both our core brands and Bouncers innovation launch.

At the retail sales level, our Sweet Baked Goods point-of-sale, led by the Hostess brand, grew by 9% in the quarter. Year-ago comparisons and the magnitude of our pricing actions reduced our fourth quarter growth rate vs our growth in Q3. To further put fourth quarter performance in perspective, on a two-year stacked basis our point of sale growth of 33% in Q4 accelerated from 31% in Q3.

Our Voortman portfolio continues to post impressive growth as quarterly POS increased by 28% in the quarter, the seventh consecutive quarter of at least 20% growth. Voortman growth continues to be driven by the zero-sugar segment, which increased by 29% and gained 420 points of sub-segment share during the quarter. Voortman continues to be very well positioned to benefit from increasing

consumer focus on the zero-sugar sub-segment within the Eight Billion Dollar cookie category, and this is driven by our investments to build brand awareness and impactful innovation.

With strong double-digit top and bottom-line growth over the last three years, we have built a track record of profitable, peer leading growth through a period of unprecedented volatility and challenges. And as we look forward to the year ahead, we are confident of continuing our profitable topline growth for a number of reasons.

- First, the structural advantages that have driven our industry-leading growth over the last three years remain in-place and we continue to focus on executing on our key strategic priorities to deliver sustained profitable growth in 2023 and beyond.

Underlying consumer snacking preferences and increasing snacking occasions, including for sweet snacks continue to increase, even as consumers adjust to the current economic environment. Historically, our core snacking categories held up well during past recessions. Based on our recent discussions with consumers as we seek to better understand the impact of the current environment, we expect that snacking will continue to perform better than overall food.

Our ongoing investments in brand building, product quality, and capabilities continue to unlock the true potential of our brands as we expand our presence in our five targeted, fast growing snacking occasions. We are attracting new households, including millennial parents to our brands, and our investment in quality throughout shelf life is keeping these new consumers in the franchise as evidenced by the increase of two-time buyers, which is growing more than twice that of the overall Sweet Baked Goods category.

This combination of our advantaged business model and superior execution continues to be a source of lasting competitive advantage that is difficult to replicate, enabling us to continue to deliver top-tier growth over time.

- Second, our innovation continues to be an ever-increasing driver of our topline growth as we leverage our deep, data-driven insights to expand further into targeted snacking occasions. Once again, we led the SBG category in innovation in 2022, accounting for nearly 45% of the category's innovation driven in part by the strong introduction of Bouncers - which reimagines our iconic Twinkies, Ding Dong, and Donettes offerings in a poppable version. Additionally, we continued to build on last year's standout innovation launch – Baby Bundts - with a new Strawberry flavor. Our vitality rate, measured by the percentage of revenue contribution to this year's total revenue of new products launched over the last three years, continues to be in the targeted 15%-17% range, highlighting the consistency and robustness of our innovation pipeline. And, while Bouncers' strong start is encouraging, I am even more excited about what's next for Hostess Brands, and what's next is right around the corner. Later this week, we will be launching our next big innovation. I know you will be wowed!

We continue to support our innovation with strong marketing... Our A&M investment increased by over 20% in 2022, on top of a double digit increase in each of the last three years, as we remain committed to investing in our brands to drive top-of-mind awareness for both our innovation and our core business. While our A&M spending will likely grow ahead of our topline over the next several years, we continue to be highly ROI focused with 100% of spend in digital formats.

- Third, we expect to get back to historical consumption patterns in 2023 as consumers adjust to new prices and we lap multiple year ago price increases. Specifically, Q1 2023 comparisons to a year ago will be distorted when compared to 2022's total growth of 25% of which 15 points of that came from volume growth. We expect an impressive two-year stacked growth in Q1 2023, although slightly below Q4. Historically, our team has demonstrated a good ability to forecast market conditions, which gives me confidence in our full year forecast and above algorithm growth in the second half.

Additionally, we continue to make great progress on our corporate responsibility agenda as we are committed to growing the right way. Attaining these goals is part of my leadership team's strategic objectives, with direct oversight from our independent board of directors as we continue to build a strong, sustainable corporate culture that values nimbleness, integrity, tenacity, inclusivity and a commitment to quality.

I am proud of our dedicated and talented workforce. They execute at high levels, care for each other and our consumers. It is our team that is building this great company and has enabled us to build a track record of excellent results through various operating environments.

In conclusion, we delivered record high sales and earnings in 2022, capping off the third consecutive year of double-digit top and bottom-line growth. We are unlocking the growth potential of our brands and business model with our superior execution and focused investments in our people, our capabilities, and our consumers.

We are positioned well to deliver another year of solid growth in 2023 and for many more years to come.

With that, let me turn it over to Travis to go through the quarterly financial results and our 2023 guidance in greater detail.

Travis Leonard

Thanks, Andy. I am proud to speak to another quarter of outstanding performance at Hostess.

Today, I will review our fourth quarter 2022 financials and share how we are well-positioned to continue to grow in 2023.

Organic net revenue for the fourth quarter increased 14.2% to \$339.5 million. Our topline was driven primarily by price/mix as we benefitted from pricing and successful execution of our revenue growth management initiatives. The increase in price/mix was partially offset by a decrease in volume.

Our sweet baked goods portfolio, which is nearly 90% of total sales, grew 13.8% during the quarter, while our cookie portfolio grew 18.0%, demonstrating growth across our entire business.

Switching to retail sales trends. Our Nielsen measured Sweet Baked Goods point-of-sale increased by 9.2% for the 13-week period ending December 31st, with broad-based growth across multiple channels.

Our Voortman Point of sale increased by 28.2% in the period, well above the 19.5% growth for the overall Cookie category, driven by pricing, innovation and distribution gains, with strong growth in the sugar-free sub-segment. Voortman's share of the Cookie category increased by nearly 130 basis points in the quarter.

Adjusted gross profit of \$123.1 million increased by 11.3% in the quarter driven by pricing actions, revenue growth management initiatives, and productivity savings, which were partially offset by inflation. Adjusted gross margin of 36.3% for the quarter declined 95 basis points from the year-ago period as 20.2% inflation offset the benefits of favorable price/mix in the quarter. Our continued focus on the development of our revenue growth management capabilities led to higher net price realization during the fourth quarter.

Adjusted EBITDA increased by 2.6% to \$75.1 million in the quarter as higher gross profit was partially offset by higher operating expenses. Our adjusted operating expenses, including SG&A, increased by 21.9% to \$65.3 million, driven primarily by a step up in advertising to support innovation and planned investments in our people and capabilities. Adjusted EBITDA margins declined by 249 basis points to 22.1% primarily due to higher operating expenses as previously discussed.

Our effective tax rate excluding discrete items was 27.3%, consistent with the prior year quarter and largely in line with our expectation of 27%.

Adjusted net income of \$33.9 million and adjusted earnings per share of \$0.25 for the quarter were consistent as compared to the prior year period as the contribution from higher adjusted EBITDA was offset by higher interest and depreciation expense.

In Q4, we continued our track record of responsible capital deployment with a prepayment of \$100 million on our outstanding term loan and share repurchases of \$36 million dollars.

For the full year 2022, we repurchased 5.8 million shares of our common stock for \$130.1 million dollars, leaving approximately \$20 million dollars remaining on our current share repurchase authorization.

As of December 31st, we had cash and cash equivalents of \$98.6 million, short-term investments of \$17.9 million and net debt of \$866.7 million with a leverage ratio of 2.9x.

2023 Full Year Guidance

Turning to our guidance for 2023, we are proud of our strong 2022 performance and expect the momentum to continue into 2023. We expect to deliver net revenue growth of 4 to 6%, Adjusted EBITDA of \$315 to \$325 million, and Adjusted EPS of \$1.08 to \$1.13 per share.

The 4 to 6% net revenue growth in 2023 is expected to be driven primarily by price/mix with relatively flat volume for the full year. The quarterly cadence in 2023 is likely to be more in line with our historical patterns with a higher percentage of our revenue in the second and third quarters. As a reminder, 2022 did not follow these historical patterns as we achieved 25.1% net revenue growth in Q1 driven by both strong volume and price/mix benefits.

As we continue to respond to changes in consumer behavior and market conditions, while working closely with our customers to drive growth, we believe the benefits of our innovation and merchandising will become more pronounced in the second half as the impact of 2022's multiple pricing actions dissipate. As Andy mentioned, we will continue to see strong two-year stack growth performance throughout the year, including in Q1.

We remain committed to recovering our gross margins fully over time leveraging our toolkit, including productivity and revenue growth management. For 2023, we are expecting full year adjusted gross margins to be relatively flat versus prior year, primarily driven by inflation and Arkadelphia start-up costs, of which approximately \$5 million are one-time and included in our guidance.

Digging into inflation more specifically. We currently expect high single-digit inflation for the full year, with greater headwinds in the first half.

We continue to develop a strong pipeline of productivity initiatives, which fuels our investments in our long-term growth.

As we have previously discussed, we are investing in advertising and marketing, which we anticipate will continue to increase faster than our revenue growth. Including these advertising and marketing investments, our total operating costs as a percentage of revenue are expected to be relatively consistent with 2022 as we benefit from our previous investments in people and capabilities.

Our adjusted EPS guidance for 2023 of \$1.08 to \$1.13 per share, or 10 to 15% growth, is expected to be driven by 7-10% adjusted EBITDA growth, as well as the benefit from 2022 share repurchases and the effective management of our debt.

We continue to believe disciplined, high ROI investments to drive organic growth are the best use of our cash. We expect 2023 capital expenditures in the range of \$150 to \$170 million, which include the

investment in our new Arkadelphia bakery, which we expect to come online in the fourth quarter of 2023.

Our capital deployment strategy continues to include returning capital to shareholders through opportunistic share repurchases. Absent any strategic acquisitions, and given our strong cash flow, we remain committed to returning capital to shareholders and anticipate our leverage to be below 3 times at the end of 2023.

We are excited by the opportunities we have ahead of us to generate long-term shareholder value as we remain committed to delivering our long-term financial objectives of mid-single digit organic revenue growth, adjusted EBITDA growth of 5-7% and adjusted EPS growth of 7-9%, which we believe will result in shareholder returns in the top quartile of our peers. With that, I will turn the call back to Andy for closing comments.

Andy Callahan

Thanks, Travis. Over the past three years, we have a strong track record of being agile and executing with excellence in various operating environments to deliver top-tier growth. I am confident that our continued strong execution and disciplined approach will enable us to deliver another year of solid growth in 2023.

I would like to close by thanking and congratulating the talented Hostess Brands team for delivering yet another year of record high net revenue and earnings.

This concludes our prepared remarks. I invite all of you to listen to our live question-and-answer call, which will begin at 5:00 p.m. ET.

Thanks, everyone for your participation and interest in Hostess.