GRUPO HERDEZ

FIRST QUARTER CONFERENCE CALL TRANSCRIPT

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PRESENTATION

Operator:

Good morning, everyone, and welcome to Grupo Herdez First Quarter 2021 Results Conference Call.

Before we begin, I would like to remind you that this call is being recorded and that the information discussed today may include forward-looking statements regarding the Company's financial and operating performance. All projections are subject to risks and uncertainties, and actual results may differ materially. Please refer to the detailed note in the Company's press release regarding forward-looking statements.

At this time, I would like to turn it over to Mr. Gerardo Canavati, Chief Financial Officer. Please go ahead, sir.

Gerardo Canavati Miguel:

Thank you, Shana. Good morning, everyone. Thank you for joining us on today's call.

I hope you and your families are doing well.

We kicked off 2021 on a positive note. Although it seemed it would be difficult to surpass the first quarter of 2020 due to a high comparable base, we achieved top line growth against last year considering the businesses withdrawn in 2020.

Results in the Preserves segment showed the resilience and strength of our portfolio, and we are optimistic about the household penetration of our products after a year of the stay-at-home restrictions. Meanwhile, results in the Frozen segment continue to face challenging conditions due to the mobility restrictions at the beginning of 2021, which are starting to subside.

As usual, Andrea will walk you through the results for the quarter and we will take your questions at the end. Andrea?

Andrea Amozurrutia Casillas:

Thank you, Gerardo. Good morning, everyone.

As mentioned in the press release, this quarter is not comparable versus 2020 for several reasons. First, we don't have the sales of Nair and fresh tuna, as well, we ended the distribution agreement with Ocean Spray effective 2021. Finally, EBIT and EBITDA comparisons will be affected by the extraordinary income registered last year as a result of the divestiture of the tuna business.

Having said that, on a comparable basis, net consolidated sales increased 7.7%, while Preserves grew 10.4% in the quarter. Growth was mainly driven by price increases implemented in the last 12 months but also by double-digit growth in categories that have experienced significant penetration as a result of the cook-at-home phenomenon.

On the other hand, our Frozen business continue to be affected by the mobility restrictions through January and February of this year, which resulted in limited hour operations. At Helados Nestle, modern trade continued to drive top line performance, while the traditional channel lagged.

Consolidated gross margin in the quarter was 37.5%, 30 basis points lower than last year. In the Preserves segment, however, gross margin expanded 190 basis points to 37.4% as a result of higher prices and a favorable sales mix.

Gross margin at Frozen decreased almost 600 basis points as a result of sales channel mix in Helados Nestle and lower operating leverage. In exports, gross margin decreased by a stronger U.S. dollar.

Consolidated SG&A in the quarter was 26.6% of net sales, 40 basis points higher compared to same period in 2020. This expense is related with the digital transformation announced in February.

Consolidated EBIT before other income decreased 4.2%. In Preserves, EBIT before other income increased 16.2%, with a margin expansion of 200 basis points. Frozen registered an operating loss of 195 million, which compares unfavorably versus last year.

During the quarter, we registered other income of 8 million compared to the extraordinary MXN 194 million recorded in the previous year coming from the divestiture of 50% of the tuna fleet.

Consolidated EBIT decreased 24.8%, although on a comparable basis it would have decreased only 6.5%, representing a margin of 11%.

During the quarter, equity investments in associated company was MXN 243 million, 78% higher than in 2020 as a result of sequential improvements in MegaMex related to lower avocado prices, as well as the recovery of the food-away-from-home channel.

Consolidated net income in the quarter was MXN 542 million, which was 18.7% lower than the previous year, but excluding one-offs, it would have been flat.

Free cash flow in the quarter was MXN 535 million, we bought back 3.1 million shares and Capex amounted to MXN 129 million.

As you may be aware, yesterday's annual shareholders meeting approved a share buyback program of 1.5 billion and canceled 26 million shares held in treasury. It also declared a dividend of MXN 1.2 pesos per share paid in two exhibitions.

With that, I will now turn the call over to Gerardo.

Gerardo Canavati Miguel:

Thank you, Andrea.

The stay at home trend continues to bring growth to small categories, which we believe has staying power, such as spices, pasta sauces, honey and teas. Despite difficult comps, we still see flattish to low single-digit volume growth in like-to-like categories.

What has been unprecedented is the run-up in soft commodities driven by renewal diesel demand. The "food for fuel" chatter is again on the table after 14 years.

The input inflation has been the worst we have seen lately and may stay for a while. It will erode 2 to 3 full points out of Preserve's gross margin. No price action is big enough to fully offset this impact in the short term, but we plan to compensate for it over time, when the dust settles.

The Frozen division is looking better as the economy reopens, but we do not expect to reach 2019 levels until 2022 on a comparable basis.

Counterintuitively SG&A is expanding somewhat due to maintenance investments in our biggest warehouse and IT expenses related to the digital transformation.

On this issue, we expect to develop -using Google technology- artificial intelligence models to better predict demand and have a higher effective promotional grid. Together with this is the ERP kickoff to upgrade our technological architecture.

We are pleased to announce that we've reached an agreement with General Mills to distribute several brands in Mexico. This portfolio includes iconic brands, such as Betty Crocker, Pillsbury, Annie's, Nature Valley, Fiber One and Häagen-Dazs. This new business will represent about 4% of sales on an annual basis and will completely offset the divested businesses of 2020. We see tremendous opportunities expanding this portfolio.

Lastly, I will share our revised estimate as follows. Top line growth including the new General Mills business. Preserves will have growth in the mid-single digits. Frozen top line will experience a 40-plus growth rate. And as mentioned previously, Preserves gross margin erosion of 200 to 300 basis points, while Frozen will experience gross margin expansion of 200 basis points. Lastly, exports gross margin will decline by 200 basis points due to exchange rate. Consolidated EBIT before extraordinary income and expenses will drop

100 to 130 basis points. Finally, EBITDA margin will drop between 300 and 400 basis points due to the gross margin erosion and non-recurring items of last year.

That concludes our prepared remarks. We would now like to open the call to your questions. Please go ahead, Shana.

Gerardo Canavati Miguel:

Thank you, Shawna. Thank you for your participation on the call today. We look forward to speaking with you again next quarter, and please do not hesitate to contact us in the interim. Have a good day.

Operator

This concludes today's conference call. You may disconnect your lines. Thank you for participating, and have a pleasant day.

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ABOUT GRUPO HERDEZ

We are proud to be the oldest Mexican food company in the country. Since 1914, we have been bringing Mexican families the best of our cuisine and the flavors of the world, and taking the most delicious flavors of Mexico to the rest of the globe. We have been listed on the Mexican Stock Exchange since 1991, and our mission is to be a worthy representative of Mexico worldwide.

We are leaders in the processed foods sector, and an important player in the ice cream category in Mexico, in addition to being the fastest-growing company in the Mexican food segment in the United States through Megamex. We are currently present in 99% of Mexican households through our large portfolio of more than 1,500 products, with which we provide solutions to the daily lives of our consumers, offering them variety and convenience for different lifestyles. We participate in the categories of tuna, spices, guacamole, ice cream, frozen yogurt, mayonnaise, marmalades, honey, mole, mustard, pastas, organic products, tomato purée, homemade salsas, ketchup, tea, canned vegetables, and many more, and we are leaders in several of these categories in Mexico. These products are sold through an exceptional portfolio of brands, including: Aires de Campo, Barilla, Blasón, Búfalo, Cielito Querido Café, Del Fuerte, Doña María, Embasa, Helados Nestlé®, Herdez, McCormick, Moyo, Nutrisa and Yemina.

We are committed to the social and environmental needs of the locations where we operate, and have aligned our sustainability strategy with the United Nations 2030 Agenda. This vision is shared with an exceptional team of more than 9,000 employees, and it is implemented through the solid infrastructure of our 13 production plants, 25 distribution centers, and more than 600 points of sale of our brands: Cielito Querido Café, Lavazza, Moyo and Nutrisa.

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FORWARD-LOOKING STATEMENTS

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