Flowers Foods(UPDATE Call 2025)

January 29, 2025

Corporate Speakers:

- J. T. Rieck; Flowers Foods; Executive Vice President of Finance and Investor Relations
- Ryals McMullian; Flowers Foods; Chairman, Chief Executive Officer
- Steve Kinsey; Flowers Foods; Chief Financial Officer

Participants:

- William Chappell; Truist Securities; Analyst
- Robert Dickerson; Jefferies; Analyst
- James Salera; Stephens; Analyst
- Mitchell Pinheiro; Sturdivant & Co.; Analyst
- Max Gumport; BNP Paribas; Analyst

PRESENTATION

Operator^ Good morning. And thank you for standing by. Welcome to the Flowers Foods Conference Call to Discuss their Acquisition of Simple Mills.

Please be advised that today's event is being recorded.

I would now like to hand the conference over to your opening speaker today, J.T. Rieck, Executive Vice President of Finance and Investor Relations.

Please go ahead.

J. T. Rieck^ Good morning. Thank you, everyone, for joining us on our call to announce the definitive agreement for Flowers to acquire Simple Mills.

I hope everyone had the opportunity to review our press release and slide presentation they were posted earlier on our Investor Relations website.

After today's Q&A session, we will also post an audio replay of this call.

Please note that on this call we may make forward-looking statements about the company's performance.

Although we believe these statements to be reasonable, they are subject to risks and uncertainties that could cause actual results to differ materially.

In addition to what you hear in these remarks, important factors relating to Flowers Foods business are fully detailed in our SEC filings.

We also discuss non-GAAP financial measures for which disclosure is provided in the press release and the slide presentation on our website.

Our commentary on this call will be expressly limited to the planned acquisition of Simple Mills.

We expect to report fourth quarter and fiscal year 2024 results in February and will not be able to address those results or our expectations for fiscal year 2025 until then.

Joining me today are Ryals McMullian, Chairman and CEO; and Steve Kinsey, our CFO.

Ryals, I'll turn it over to you.

Ryals McMullian^ Okay. Thanks, J.T. Good morning, everybody. Ladies and gentlemen, we're absolutely thrilled to announce our agreement to acquire Simple Mills. This is a transaction that offers significant strategic and financial benefits to both organizations.

In addition to enhancing Flowers' growth prospects and diversifying our category exposure the transaction provides immediate financial benefits, which we expect to compound over time. The acquisition leverages Flowers' demonstrated ability to grow acquired brands in the better-for-you space and we expect to apply our best-in-class capabilities and deploy additional resources to enhance Simple Mill's growth by broadening distribution, accelerating innovation and amplifying brand awareness. Founded by Katlin Smith, in 2012, Simple Mills is a leader in natural snacking segments driven by its unique ability to blend purposeful, nutritious ingredients with exceptional taste.

That approach has enabled Simple Mills to successfully garner mainstream appeal and dedicated consumers for what historically has been a specialty market. Much like the self-proclaimed breadheads, fiercely loyal to Dave's Killer Bread, Simple Mills consumers have demonstrated a strong loyalty to the brand and a willingness to follow Simple Mills into new segments.

Consumers love the products, which has translated to impressive sales growth generating a compound annual growth rate of 28% from 2019 through 2024. And we see significant long-term upside potential in the large categories in which the brand has been gaining share with a total available market size of approximately $32 billion.

We're confident in our ability to continue that growth by further expanding distribution, developing new innovative products and increasing velocities.

Simple Mills products are carried in more than 30,000 stores and significant opportunity remains to grow sales with those existing customers by increasing the average number of items carried at each store.

For example, category-leading brands offer more than twice as many items per store than Simple Mills does, which presents attractive potential upside.

We see additional opportunity to expand distribution by adding new retail partners in existing channels.

For example, Simple Mills has less than 10% household penetration in crackers and cookies and less than a third of total distribution points compared to leading cracker brands, offering ample upside for future growth. Another promising area of potential growth is adding new distribution in channels where Flowers' portfolio already has a presence, but simple Mills does not have current distribution. Channels such as food service and convenience stores present exciting opportunities and highlight the compelling potential upside in out-of-home occasions, which are largely untapped today.

Innovation is core to Flowers and has also been a key growth driver for Simple Mills, which has demonstrated the brand's ability to enhance its presence in existing categories as well as enter new ones.

Simple Mills' robust internal research and development capabilities including in-house labs and deep technical understanding of alternative Flowers and other ingredients, provide a repeatable innovation approach that has consistently generated a pipeline of successful products. Building on its initial launch of baking mixes in 2012, Simple Mills has leveraged its innovation capabilities to successfully enter the cracker, cookie and bar categories.

We see significant opportunities to leverage Simple Mills' strong brand and consumer loyalty by adding new products in its existing categories as well as entering new categories in snacking and beyond. A third growth driver is increasing velocities, where we see potential to drive sales by improving retail fundamentals and leveraging consumer marketing. Capitalizing on Flowers' deep experience and promotional and in-store execution, along with the additional resources we offer, we expect to build upon existing momentum and drive meaningful velocity growth.

On top of the expected growth benefit, the addition of supplementals to Flowers also diversifies our category exposure.

Our portfolio strategy is intended to increase the proportion of sales from branded retail products, and this transaction furthers that strategy both immediately and over time.

On a pro forma basis, our 2024 branded retail sales are expected to increase to approximately 66% of total sales. And given the outsized growth rates expected compared to our existing business, we expect that percentage to continue to grow over time. The transaction also supports our focus on moving into faster-growing parts of branded retail particularly better for you and snacking.

With DKB and Canyon Bakehouse, we already have a strong position in better-for-you products. And more recently, we've moved into snacking with the DKB bars and snack bites. The addition of Simple Mills accelerates that transition, immediately boosting our position in those attractive spaces and offering a robust platform from which to expand far into the future.

Before I turn the call over to Steve to discuss the financial benefits, I would like to touch on Flowers' M&A track record.

As many of you know we have a long history of generating growth through acquisitions, having purchased more than 100 companies that's going public in 1968.

In that time we've learned that while the strategic and financial benefits of the transaction are certainly important, to maximize those expected benefits, it is crucial to have a strong cultural fit. That said, enable us to merge the unique cultures of both DKB and Canyon into Flowers in a way that significantly enhanced both organizations. Katlin and her team have built a remarkable company.

And one of the things we appreciate most about Simple Mills is that its values are aligned with ours, focused on honesty and integrity, respecting inclusion and sustainability.

We have a deep respect for their team and a strong appreciation for their business, and we look forward to working together to further extend their brand.

As part of that collaboration, I want to be clear that as in past deals including DKB and Canyon, Flowers is committed to stewarding and protecting the Simple Mills brand that so many consumers have grown to love. Most importantly, its commitment to bringing delicious purposeful ingredients to its products to improve the lives of its consumers. Reflective of that commitment, I am delighted to report that Simple Mills will operate as an independent subsidiary of Flowers Foods and will continue to be led by Katlin and the Simple Mills leadership team.

And the company will maintain its current operations in Chicago and Mill Valley, California.

So with that, I'll turn it over to Steve to cover the attractive financial profile and the exciting value creation opportunities we see ahead.

Steve?

Steve Kinsey^ Thanks, Ryals. And good morning, everyone. Let me echo Ryals on welcoming the Simple Mills team to Flowers.

As Ryals mentioned, we expect Simple Mills to accelerate our growth prospects, offering immediate accretion to net sales and adjusted EBITDA growth. Profitability is also expected to benefit with 2024 adjusted EBITDA margins expanding on a pro forma basis. The transaction is expected to be accretive to Flowers earnings per share in 2026.

As disclosed in the press release and slide deck, total consideration for the acquisition of Simple Mills at $795 million to be paid in cash.

In the past, we discussed the optionality enabled by our strong balance sheet. And in this case, it allowed us to capitalize on this unique opportunity.

We have entered into a binding commitment letter for a $795 million term loan from Royal Bank of Canada to help fund the transaction as required. Pro forma total net debt estimated at the closing date will be approximately $1.9 billion and the pro forma total net debt-to-EBITDA ratio is expected to be in the range of 3.1x to 3.3x.

As we evaluate more permanent financing, the company intends to maintain its balanced capital deployment model, along with the commitment to its investment-grade debt rating. The transaction is subject to customary regulatory approval and closing conditions, and is anticipated to close in the first quarter of 2025.

We will provide greater detail about the impact of the acquisition on our fiscal 2025 results when we report fourth quarter and full year 2024 earnings in February.

Thank you, and now I'll turn it back to Ryals.

Ryals McMullian^ Okay. Thanks Steve.

Well as you can tell we are tremendously excited about this acquisition, and it's consistent with our clearly defined M&A strategy and focus on seeking compelling brands that complement our existing portfolio and the skew towards better-for-you products.

It also enhances our growth prospects, diversifies our category exposure, tips more of our sales into higher growth categories and offers an attractive financial profile. Even better, the deal unites us with first-rate partners led by Katlin and her team, who are aligned with our culture and our mission.

We look forward to welcoming the Simple Mills team to the Flowers family and delivering significant additional value to our shareholders.

I'd like to close by thanking both Flowers and Simple Mills employees for their dedication to this process. This transaction would not have been possible without their hard work and collaboration and we're very excited about embarking on our next phase of growth together.

So with that, Tanya, we can open it for question.

QUESTIONS AND ANSWERS

Operator^ (Operator Instructions) Our first question comes from Bill Chappell of Truist Securities.

William Chappell^ Just maybe give us a little more on the background of this deal and the timing? Was it an auction? And the reason I ask that is I think you've been talking about this type of acquisition since you became CEO four or five years ago, you've alluded to several other transactions that have kind of come and gone.

But why now why this one and how long you've been looking at it? A little bit more kind of on the background would be helpful.

Ryals McMullian^ Sure.

Well first of all, Bill, it's been almost six years.

I got hard to believe.

But no, we're -- obviously we're under NDA.

So we can't really comment on the process itself.

What I will tell you is that, as we've said, we've consistently remained active in the M&A market.

We talk about it almost every quarter.

We look at dozens of companies. And Bill, if you think about it, other than the Papa Pita acquisition we did a couple of years ago, which was essentially folding in a co-man.

We really haven't done an acquisition of a significant brand since Canyon in 2018 is up seven years ago.

And I think that, that speaks to the rigor of our process, our patience, our discipline, I can tell you that I've first met Katlin back in 2019.

So I've known her for some time.

We've been following this company pretty intensely over that period of time studying it and frankly, becoming, over time you're just more and more convinced about its fit with our company, its future growth prospects.

Obviously Katlin and her team have done a remarkable job to this point. The cultural fit, as I mentioned in the prepared remarks, is definitely there and plays such a crucial role in these types of things.

And the timing just worked, and then fortunately, it all came together.

So as we've said, we say no to a lot more than we say yes to. And it takes significant conviction for us across all considerations, financial, operational, cultural, commercial, et cetera, and our conviction is very high across all of those considerations.

William Chappell^ Got it. And then I could just kind of -- maybe just understanding the dynamics of distribution and maybe this is mainly a wholesale or warehouse model, but, I mean how does it work getting some of these different new products through your DSD network? Can you get them? Is it easy just to just add them on to the trucks or in every region? Is there revenue synergies coming from that?

Or is it fairly distributed? Just a little more background on how that works would be great.

Ryals McMullian^ Sure.

So we don't anticipate any of these products being carried on the DSD routes. This is a warehouse-delivered model, it's also 100% co-manufactured.

So all the manufacturing is outsourced and the products are and will continue to be delivered through the warehouse.

William Chappell^ Got it.

So just last question on that.

So any cost synergies would just be more from purchasing input costs versus improving the manufacturing or distribution or what have you?

Ryals McMullian^ Yes. That's right. And look, I'm happy to be perfectly transparent on this. There are some minor cost synergies here, probably not as many as you would maybe traditionally see. The real prize here is the forward-looking growth rate of the business. And our ability to help them continue to scale that business, grow the distribution, grow the velocities, continue to innovate.

And if we do that and our forecasts are correct, this will look pretty inexpensive in a few years time.

William Chappell^ Congratulations.

Operator^ (Operator Instructions) Our next question will be coming from Rob Dickerson of Jefferies.

Robert Dickerson^ Ryals.

So I guess -- just a couple of questions.

I guess just firstly, it sounds like Katlin and team all stay in place, it kind of operates as if it's somewhat independent, but clearly, it is absorbed by Flowers.

So I'm just curious like as you move forward, kind of like, how does that play out? Like does Katlin you probably can't really disclose so much, but is Katlin have a certain timeframe?

Or is Katlin maybe become a broader head of healthy snacks at Flowers or just trying to understand the integration at some point, potentially of the business into kind of broader Flowers?

Ryals McMullian^ Yes.

So first of all, Rob, thanks for the question. And we're just over the moon frankly, that Katlin and her team are saying. That was a very big part of this transaction for us, having them stay. They know this business so well.

This is a very, very mission-driven and oriented business with a very strong culture that Katlin has put together.

So it was very important to us that she and her leadership team remains.

So we're just thrilled that, that has come to pass.

Look, we're going to take it one step at a time.

As we said in the prepared remarks, it will be an independent subsidiary.

Katlin and the team will continue to run it.

As you say, obviously it is part of Flowers.

We are a public company, so there is oversight and those types of things.

But Rob, we learned so much from the acquisition and integration of Dave's and Canyon and how to do that right and how to match the cultures, how to provide support and capabilities that we can bring to bear without overrunning the business, right, and letting them be who they are, who they are is what got them to where they are today, and we want to preserve that.

So yes, we will be bringing our expertise in retail customer management and trade promotions and market execution, procurement, all those things that you might expect.

We will be bringing those to bear.

But by the same token, it will be a fairly light touch, particularly in the early days, which I think is important to keeping that entrepreneurial spirit, if you will, alive in the business.

Robert Dickerson^ Okay.

Okay. Fair enough. Makes sense. And then I guess just a quick question on the co-mans piece.

A lot of companies kind of higher growth phase, co-mans makes sense. $40 Million, right, is not super small right? I mean it's actually kind of a proof of concept for 12. Again, this would be longer term kind of dynamic.

But it seemed like if you try to increase distribution velocities, et cetera, operating leverage, you'd also love to increase the profitability profile margin of the business.

Would that be something you would consider at some point potentially kind of bringing in-house on the manufacturing side?

Ryals McMullian^ Yes.

So I mean for the time being, they're in great shape from a co-mans standpoint. Their team has done an outstanding job managing and working with their co-manufacturers.

So from a growth standpoint, there's plenty of runway. And so there's no rush to do something like that.

Now longer term, Rob, down the road, 5, 6, 7 years or whatever it might be, sure.

We would absolutely consider that.

But certainly no plans in the immediate future for sure to do anything like that. The margins of this business are already attracted, we're happy with where they are and where they can go. And so no immediate plans to do that.

But certainly down the road, it could be a possibility.

Robert Dickerson^ Okay.

So I mean it sounds like the co-mans are all kind of locked in with plenty of capacity as you grow?

Ryals McMullian^ Yes, exactly.

Robert Dickerson^ Okay. Cool. And then last question, I'll pass it on.

I have a bunch, but I'll ask one more.

Steve, I think you and maybe even J.T. upfront, you said like they were not talking about '25 but we're talking specifically about the deal.

But then the deal specifically is going to be accretive in '26. There's always some questions off of what number, right? Because we don't even have '25. When we think about '25, sometimes companies provide some color, not always, but I'm just curious, is this like I'm not sure if you're willing to provide any type of color, let's say, on '25, like to be low single digit dilutive or as you pay down the debt and the deal closed in Q1?

Or kind of someone's going to ask that question probably for the next two months.

So I figure just can ask you now.

Steve Kinsey^ Sure. No.

I don't expect that honestly, Rob.

But the reality is, we said it would be slightly dilutive in 2025.

We plan to get more color when we give our guidance for 2025 on our call in early February.

So it won't be months.

It will just be a few weeks, and we'll be able to get in some more detail there at that time.

But for now I mean obviously it will be slightly dilutive for a lot of the reasons you just articulated.

Robert Dickerson^ No. I get it.

Operator^ Our next question will be coming from James Salera of Stephens.

James Salera^ I wanted to start off, Ryals, with just kind of quantifying the white space opportunity.

It seems like most of the sales come from the natural channel.

Is there still a lot of opportunity to expand within that channel? Or do you need to jump into mainstream to continue to support the double-digit growth that this brand is seeing?

Ryals McMullian^ Yes.

So they're in both. They're in both.

I mean certainly their strength and sort of where they got their start is in the natural channel, but they've moved into mass and the mainstream resellers.

I think the big opportunity there really is to continue to help them grow the depth and breadth of that distribution.

We talked about how many SKUs they have on the shelf relative to some of the larger competitors. And in addition, some of the other channels, out-of-home channels like convenience and foodservice, are largely untapped today.

But they have a nice presence in club, for example.

I do think that there's additional opportunities in mass and additional opportunities, as I said, to grow the depth and breadth of that distribution and the other mainstream retailers.

James Salera^ Great. And Steve, you had mentioned accretive to the EBITDA margin in 2025 and then obviously EPS accretive in 2026.

Can you just quantify what Simple Mills EBITDA was over the last 12 months or whatever time series just so we can kind of back into a multiple and if you're also able to help quantify what the EBITDA margin uplift would be in 2025?

Steve Kinsey^ Yes.

I mean good question.

Obviously as Ryals said earlier, we haven't closed yet.

So there's still some things that from an NDA perspective, we've enough, not discussed today.

So as we said, I don't know if we said it in our comments, but we're not prepared to give the absolute EBITDA today.

But I think as we go through the 2025 guidance, you'll begin to see really the nice margin profile of this brand and the strength of the branded portfolio.

So we'll provide that in a few weeks on our guidance.

Ryals McMullian^ Sorry, I was just going to tack on to that a little bit.

We did give the sales multiple at 3.3 or so. And the only other thing I would offer is that -- while we're not prepared to disclose the absolute number yet today for the reasons Steve talked about the EBITDA multiple is also in line with precedent transactions for growth companies of this size.

So not out of line.

James Salera^ Are you able to quantify just like the EBITDA margin uplift for 2025 just like how many basis points that you would expect it to add?

Ryals McMullian^ I mean again, we'll do that in a few weeks when we give our full year 2025 guidance.

Operator^ Our next question will be coming from Mitchell Pinheiro of Sturdivant & Company.

Mitchell Pinheiro^ Most of my questions have been asked, but I do have just a couple of odd ones here.

In 2023, it looked like there was about 50% growth at Simple Mills, and I was wondering what drove that in particular?

Ryals McMullian^ In what year?

Mitchell Pinheiro^ In 2023? I mean you went from $150 million to $210 million. That was the biggest jump. And I was wondering what drove that particular jump.

Ryals McMullian^ Yes. It would have been a couple of things, mainly distribution gains, and there was a price increase taken in 2022, that likely contributed to that.

Mitchell Pinheiro^ Okay. All right. Helpful. And then -- and so -- and as you look at the growth rates that you gave on Slide 9 in terms of their growth.

Is that coming from all distribution?

Is there consumption growth, same-store sales growth there? How much of that is sort of pricing versus volume in general?

Ryals McMullian^ Yes.

So looking at Slide 9, there's not going to be any pricing in that because there -- like I said, there was pricing taken in '22, but none since then.

So all of that is going to be volume, velocity, distribution growth.

Mitchell Pinheiro^ Okay. And so when -- if you just sort of back in just based on the numbers that you gave us so far, it looks like the EBITDA margins are in the mid-teens. And I'm curious is that going to be -- are margins in general for this business is going to be sort of -- that's where they are -- or is there -- because it's all co-manufactured, is it simply -- this is going to be sort of a volume story and not a margin expansion story for Simple Mills?

Ryals McMullian^ It's going to be both.

It's definitely going to be both.

As I said, the margins are attractive today and certainly accretive to our margin profile, but we see additional upside particularly as we continue to scale the business. Probably more so on the SDA side, Mitch. You mentioned the co-mans, it's probably more on that side.

But we definitely see a continued lift in margins as does scale.

Mitchell Pinheiro^ Okay. And I know you're under an NDA answer with that.

But in terms of the four sort of segments that you outlined, crackers, cookies, baking mixes and snack bars, are they reasonably consistent in their margins? Or is -- are crackers are something a better margin than the others?

Ryals McMullian^ Yes.

I mean we're not specifically obviously breaking that out right now but I'll just say that across all of those categories, the margins are attractive.

Mitchell Pinheiro^ That's all I have. Congratulations.

Operator^ And our next question will be coming from Max Gumport of BNP Paribas.

Max Gumport^ Just with regards to the top line growth that's embedded in your assumptions.

I mean it does -- like obviously the brand has been growing at a 28% CAGR. From what we see in Nielsen and ACV is still quite low, below 6% or so. You called it household penetration, it looks like below 10%, it looks like dollar share across all these three categories is still cookies, crackers, nutrition bars, so the point of share is lower in Nielsen.

That imagine you're forecasting that this type of growth rate that we've seen over the last couple of years can continue for some time and that was embedded in your assumptions when you agreed to the deal, but can you just give us a bit more color on the type of growth you are expecting for this business over the next five years or so just with regard to the top line?

Ryals McMullian^ Sure. Max, you were breaking up a little bit there, but I think I got the gist of it.

Obviously as Steve said, we'll give some more color when we get to the fourth quarter results here in a few weeks.

But look, obviously we are very attractive to the growth potential for this business. The categories that they play in today are growing categories.

They are exceeding the category in terms of growth rate. They have taken what might have a few years ago have been perceived as a niche product and have taken it mainstream. And so they're appealing to mainstream consumers.

One of the things that got my attention early on about this business is that while all of the products are gluten-free, they don't really lean very heavily into that gluten-free equity. And as a matter of fact, only about 17% or 18% of their shoppers are gluten-free shoppers.

So they're very much appealing to mainstream consumers that are looking for more nutrients foods. And so we think that the growth profile for this business for many years to come is very attractive. They have a very robust innovation pipeline that they have historically done kind of on a 2-year basis.

We would look with our capabilities to help them speed up that cycle and bring more new and exciting products to market both in these categories and beyond.

So certainly the profitability margin profile of the business is attractive.

But the top line growth potential over the foreseeable future is also attractive as well.

So let me just leave it at that for now.

We'll give a little bit more color in February.

Max Gumport^ Okay's.

I appreciate it. And then last one for me would just be, if we think about the organic innovation you've done, especially for '25 in terms of expanding in adjacent snacking categories. And now just deal into more snacking categories.

Is it fair to say that snacking is really the place where you're trying to move this business into and any long-term view you can give us on five years the (inaudible) Flowers Foods will look much different in terms of a much smaller mix from bread and the much bigger mix of sales from snacking.

Just how are you thinking about where you want to take this business in the next 5, 10 years? I'll leave it there.

Ryals McMullian^ Yes. No, great question. And no, you're absolutely right.

I wouldn't say that snacking is the only area.

But it's certainly one of our main areas of focus, particularly when it comes to better-for-you snacking platforms with Simple Mills certainly fits that bill.

Whether five years is the right timeline or not, I think, is yet to be seen.

But look, we recognize that our core category is a slower growth category.

We certainly have some highlights within that category with Dave's and Canyon and Wonder and Nature's Own Perfectly Crafted, but we have been searching diligently for other growth accretive areas to move into.

And as I said at the outset of the Q&A, we take a very disciplined approach to doing that. And we're very careful about who we choose to partner with. And Simple Mills certainly fit that bill to it.

So we're -- as we said, we're tremendously excited about this and can't wait to hopefully get it closed and in mid-late February, hopefully, and move forward from there.

Operator^ And I'm showing no further questions.

I would now like to hand the call back to Ryals McMullian, Chairman and CEO, for closing remarks.

Ryals McMullian^ Okay, Tanya, thank you very much. And listen, we just appreciate everybody joining the call.

We hope you're as excited as we are about this acquisition, and we look forward to speaking with you again in early February. Thank you very much.

Operator^ And this concludes today's conference call. Thank you for your participation.

You may now disconnect.