Ahold Delhaize

Management's Prepared Remarks
Q3 2023 Earnings Call
November 8, 2023

JP O'Meara
Senior Vice President, Head of Investor Relations

Thank you Sharon, and good morning everybody. I am delighted to welcome you to our Q3 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 provides 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.

Frans Muller

President, Chief Executive Officer

Thank you JP, and good morning everyone.

Of course, a special welcome to Jolanda who is joining her first quarterly call as CFO of Ahold Delhaize. Jolanda has been on an extensive induction program that started in August and officially assumed the CFO role on October 1st. She will share some thoughts and take you through the financials in a few moments.

As we head into the busy Holiday season for our customers and associates, it is a good time to reflect on the environment we are operating in as well as the important strategic and operational choices we are taking to drive long term value creation.

No doubt, times continue to be turbulent. The war in Ukraine already lasts almost 2 years, and in the Middle-East, we are facing another war between Israel and Hamas. In our own markets, we also see first-hand some of the tragedies of the current political and social climate. On October 25th, the city of Lewiston in the state of Maine, Hannaford's home state, experienced one of the darkest moments in its history – a mass shooting took the lives of 18 people and injured many more. We unfortunately know that mass shootings have become more frequent in the U.S., but this incident was particularly chilling because such events are unprecedented in Maine. Our thoughts are with our colleagues in Maine, and everybody in Lewiston who will be dealing with this tragedy for a very long time.

Reflecting on business trends, many of the ones I outlined during our last quarterly call indeed materialized as expected. While inflation has passed its peak, customers' household budgets remain under pressure as many of them are also experiencing higher interest rates and in the case of the U.S., declining federal and state government assistance.

With our strong portfolio of brands, we grew comparable store sales by 3.1 percent in the third quarter. We delivered an underlying operating margin of 3.8 percent and diluted underlying EPS of 58 cents. While both these metrics are lower year-over-year, from a margin perspective, around half of the decline is linked to insurance-related adjustments, with the other half resulting from lower margins in the U.S., which Jolanda will discuss in a few moments.

Our formula for success therefore has continued to play an important role:

1) first of all, being Agile and Adaptable to meet and exceed customer needs;
2) secondly, Embracing Transformation in our operating model; and
3) third, continuing to Advance our Sustainability agenda.

Today, I am going to focus on the second point – Embracing Transformation.

Here there are four important moves I would like to highlight, each also underpinning our strong, disciplined focus on value creation.

The first is the announcement of the planned addition of local Romanian supermarket chain Profi to our family, subject to approval from the regulatory authorities. Densing up existing markets is a tried and tested strategy of ours, where we have a proven track record of delivering highly accretive returns in a short space of time.

This acquisition will more than double the size of Ahold Delhaize's existing Romanian business, which operates under the Mega Image brand and has 969 stores, predominantly in urban areas. Profi operates 1,654 stores mainly in rural areas and generated roughly 2.5 billion euro in sales for the 12 months ended June 2023.

The strong format fit and complementary customer propositions between the Profi and Mega Image brands, will allow them to better serve the Romanian customer, driving both sales growth and profitability. The combination with Profi is expected to be sales growth and EBIT margin accretive (post synergies, and integration) to Ahold Delhaize Europe, and EPS accretive to Ahold Delhaize as a group, in the first full year after closing. The implied fully synergized acquisition multiple is approximately seven times on June 2023 Last-12-Month EBITDA basis (post IFRS 16).

Secondly, we thoroughly believe our strength lies in the seamless mix of in-store and online shopping, in our omnichannel strategy. To assess where we stand in this changing environment, we have done a thorough review and analysis, as part of our Accelerate initiative.

As customers' shopping preferences evolve in the U.S., one of the concrete outcomes is to orient our online fulfilment capabilities towards more efficient, less asset intense same-day delivery models such as click and collect. This has already led to the decision earlier this year to close the U.S. Jersey City and Hanover fulfillment centers and focus on pick from stores and third party partners.

Based on the economics of the omnichannel business model and return on investment we are striving for, divesting FreshDirect is an additional outcome of this analysis. This will enable us to focus on growth and investments in our broader-based omnichannel businesses, where we have strong store density and online presence, leading market share, and a longstanding heritage of loyalty and deep relationships with customers.

We believe Getir, a pioneer in the tech industry and the ultrafast online grocery delivery business, is the right company to carry FreshDirect forward. FreshDirect has been a trusted brand in the New York City area for more than 20 years, known for delivering the highest quality, freshest food and deeply loyal customers who are passionate about the brand. We expect this legacy to continue under the new owner.

Third, in Belgium, the Delhaize team continues to make excellent progress on the execution of its Future Plan. To-date, Delhaize has announced that it has signed agreements to transition 51 of its integrated stores to independent entrepreneurs, of which the first 12 stores have already opened their doors under the new entrepreneurs as of last Friday (with a further 3 planned for conversion this week). I am also pleased to report that impacts of Belgium on our Q3 results were rather minimal with the market delivering positive comparable store sales and having only a minor 20 basis point impact on European sales and 10 basis point impact on European margins.

Fourth, as you know we have a long and strong track record of working hard with suppliers to mitigate price increases and to swiftly reflect price decreases where possible, ensuring our customers have access to affordable, healthy options. Ensuring we continue to provide fuel to our long term Save For Our Customer program is another area where we invest time and energy. To help tackle persistent price differences between European markets, Ahold Delhaize has joined the European retail alliance joint venture EURELEC, which is a collaboration with REWE Group and E. Leclerc. This is in addition to our already existing memberships in the AMS and Coopernic buying alliances. With this specific partnership we aim to promote open and fair price negotiations with the largest FMCG brands across Europe, which ultimately benefits our customers. In the end, we owe it to our customers to keep our food affordable, especially during these challenging times.

And speaking of things that are important to customers, let me spend a brief moment on Health and Sustainability. This area remains a priority for our brands with several examples from the quarter on Slide 11.

Albert Heijn and bol were featured in a minidocumentary powered by Kickstart AI. Albert Heijn explained how they are using artificial intelligence to reduce food waste using demand forecasting. This is a great proof point of how they use innovation and technology to combine the reduction of food waste with providing customers access to affordable and healthy products while at the same time reducing costs.

Bol demonstrated how they use automatic packaging machines controlled by smart algorithms to ensure the use of less cardboard and smaller parcels. They also use AI to see if additional packaging is actually needed. This results in less transport movements and the use of smaller, more sustainable vehicles, like the bike couriers of Cycloon.

Looking at reducing carbon emissions, every initiative, big and small, counts. For example, Delhaize and French fast-charging provider Electra have plugged in the first six of a planned 1,200 fast charging points. Food Lion, Hannaford and The GIANT Company were recognized for their programs to reduce emissions from their refrigerant systems.

So as you can see, we have been very active over the past months, and I am particularly excited by the building blocks for future growth we are putting in place. More on that later. Let me now hand you over to Jolanda, to share her remarks on the financials.

Jolanda Poots-Bijl

Chief Financial Officer

Thank you Frans and good morning to everyone. I'm excited to be here and look forward to engaging with you in the years ahead.

As Frans mentioned earlier, I had the pleasure to start in the middle of August with an extensive six week induction program. This gave me the opportunity to dive into our business, visit almost all of our great local brands, and more importantly meet many of our wonderful associates across the company.

I am impressed by the dedication and the passion of my colleagues, their agility in managing dynamic times and their pride in the strong results our business continues to deliver. We are a true people-4-people business that is well positioned in the heart of our society.

Now, let's go into our Q3 numbers and the key highlights on slide 13.

- Net sales grew 2.9 percent, to 21.9 billion euro. This was mainly driven by the strong comparable sales growth in Europe of 7.0 percent, and continued market share gains in our most important markets.
- Group underlying operating margin was 3.8 percent for Q3, a decrease of 60 basis points versus last year, about half of which was related to insurance and interest related changes. From an operational perspective, I am proud of the work of our great local

brands to limit the impact of cost inflation through the Save for Our Customer program and additional Accelerate initiatives, which helped to offset a large portion of these higher costs.

- Diluted underlying earnings per share for the quarter were 58 euro cents, down 17.1 percent at actual rates, two thirds of which relates to an unfavorable exchange rate and the one-off items I already mentioned.

Slide 14 shows our results on an IFRS-reported basis for Q3.

Our Group operating income was 625 million euro, representing an IFRS-reported operating margin of 2.9%, mainly impacted by:

- a 153 million euro impairment charge for FreshDirect, mainly related to re-valuations of next day delivery equipment and buildings.
- 61 million euro in restructuring and related costs pertaining to Belgium and other Accelerate initiatives.

On slide 15, you see comparable sales growth by region including and excluding weather, calendar and other effects. These had a limited impact in the quarter. In the U.S., Hurricane Ian was a 40 basis point headwind which was offset by 20 basis points from calendar and 10 basis points from weather this year. In Europe, the Belgium transformation had a minor impact of 20 basis points in the quarter.

To share more detail on these developments, let’s now turn to our regional performance.

In the U.S., excluding the impact of weather and calendar shifts, comparable sales grew by 1.0% and reported net sales were 13.6 billion euro. Online sales in the segment were up 4.4 percent, driven primarily by double-digit growth at Food Lion and Hannaford as they continue to invest in their omnichannel proposition. Two key highlights of the quarter were Food Lion's 44th consecutive quarter of comparable store sales growth, as well as overall strong growth in omnichannel customers which increased 8% compared to a year ago.

The reduction in emergency federal SNAP benefits, higher interest rates and the resumption of student loan repayments in October continue to weigh on customer sentiment. On its own, the reduction in SNAP benefits resulted in approximately a four percentage-point headwind to sales growth in the third quarter.

We were able to offset a large portion of this headwind through our strong value propositions and ongoing momentum in online sales.

Underlying operating margin in the U.S. was 4.2 percent, down 80 basis points from the prior year. This was due to the cycling of an insurance reserve release in the prior year that was 30 basis points favorable, wage inflation, an increase in shrink and the unfavorable effect of a change in sales mix. The increase in shrink is a result of the current economic conditions and rise in social tensions, which is a real concern for both the safety of our associates and our customers. We are deploying additional solutions in stores including upgraded camera systems, self-checkout monitoring, anti-push out grocery carts, and in-store live surveillance to counter this negative trend.

With the help of the measures we are putting in place through our Accelerate initiatives, in-store actions to reduce shrink, and further volume support incentives from vendors, we expect this modest margin pressure to be transitory and pass in a couple of quarters.

Turning now to Europe, sales increased by 7.1 percent, resulting in net sales of 8.3 billion euro. When looking at Europe, which has endured a lot of pressure in the last two years, I am confident we are on the path to recovery, particularly on returning margins in the region to their historical averages.

While inflation is also moderating in Europe, our major efforts to elevate and harmonize our customer value proposition also saw accelerated comparable sales growth compared to Q2, with volume improvements also playing an important role.

Underlying operating margin in Europe was 3.5 percent, consistent with the prior year. The impact of the Belgium transformation, energy and wage inflation in many of our markets were offset by strong cost control, the successful execution of the Save for our Customer program and the decrease in the non-cash service charge for the Dutch employee pension plan. To be consistent with prior quarter, Belgium and energy impacted the Q3 margin by around 15 basis points.

In the Netherlands, Albert Heijn and bol had outstanding market share gains. At Albert Heijn, AH Premium is now approaching 900 thousand members, and the brand launched the “AH Terra” own-brand product line with around 200 plant based products. We are also delighted to have completed the conversion of the first 15 Jan Linders stores to Albert Heijn in Q3.

Turning to bol, we saw healthy growth rates again in Q3 as gross merchandise value ("GMV") was 1.3 billion euro, an increase of 6.5 percent compared to the prior year. And we continue to see very strong growth in our highly profitable new services areas, with Advertising services up almost 50 percent, and Logistics offerings up over 20 percent compared to last year.

I expect growth to continue at a good pace over the remainder of the year with bol well set up to gain further share during the holiday period.

Moving on to our free cash flow. Q3 free cash flow was 512 million euro up from 133 million in the prior year. The major increase in working capital year-over-year reflects the SAP S/4 Hana go-live in the U.S. this time last year. The optimization of netting processes in SAP were normalized by the end of Q4 2022. So expect the counter effects of this change in the upcoming Q4.

Excluding this timing impact, we nonetheless see good progress on underlying working capital in both regions. And we will continue to look for further opportunities as we leverage our scale, supply chain transformation and new data capabilities through AI and machine learning.

To this end, we also need to ensure we maintain a good pace in modernizing our infrastructure to support our omnichannel growth. We are a well-invested company. And we will be rigorous and disciplined in executing large scale projects.

During the quarter we moved forward on many projects in Europe, including:

- Albert Heijn's newly opened and technologically advanced mechanized Home Shop Center in Barendrecht powered by Swisslog. The new center will use 300 robots to collect non-perishable products, making the work easier for associates.
- Bol recently opened its second warehouse for extra-large items such as trampolines, TVs and aircos, a category with significant untapped market share potential.
- In Belgium, while a lot of focus this year has been on the transformation plan, Delhaize has also been diligently preparing for further growth in online, building a new e-commerce center slated for early autumn of 2024.
- Finally, in the CSE we plan to Go Live with our first Homeshop Center at Mega Image in Romania in the coming weeks, in this instance, applying the successful Albert Heijn ecommerce model.

In the US, our brands continue to update and modernize the local store networks and ecommerce platforms. For example,

- Food Lion launched omnichannel remodels in 47 stores in the Greenville, North Carolina, market, with sales so far exceeding expectations.
- We continue to invest in PRISM our own proprietary e-commerce platform. Because it is our own platform, we fully own the customer digital experience – and the first-party customer data – which provides a unique opportunity for us to continue to learn about our customers and make changes to meet their needs.

In summary, our strong and consistent financial performance gives us a great platform to unlock the many growth opportunities we see on the journey ahead. Optimizing and nurturing Ahold Delhaize's long term value creation will be one of our top priorities. I look forward to the opportunity to meeting many you all in person in the coming months.

With that, let me pass back to Frans for our Outlook.

Frans Muller

President, Chief Executive Officer

Thank you very much, Jolanda.

As we approach the halfway point of our Leading Together 2025 ambitions, we are on track, and in many cases ahead of our ambitions.

A lot has changed since we embarked on our Leading Together journey. Rest assured, our leadership team, which is now back to its full complement with Jolanda, has the energy and determination to keep this trajectory going.

Taking stock of what we have learned so far, we are currently refreshing our priorities to calibrate to the macro and competitive environment. This will require some shifts in focus, but I also believe this will lead to faster growth rates and higher ROIs.

For example, we will double down on our customer value proposition and our clearly winning omnichannel model. Just to take a few proof points for the U.S.:

- Online Traffic was up 19 percent in Q3, including sessions with purchase intent also up 19 percent year over year.
- Omnichannel customers, our most profitable customers, grew by over 8 percent year-over-year in Q3.

- Long-term customer retention remains strong. Of the first-time online shoppers during peak-COVID (Q2 2020), 66 percent were still active shoppers (online or in-store) with us in Q3 2023.

With this strong pivot to digitally driven customers in our model, and there are also many European examples I could have used here as well, I see tremendous opportunities to build further on our complementary revenue streams.

In 2023, from a capability perspective, we have made solid ground, and put in place best-in-class solutions to really accelerate growth.

- Together with AdTech Company Adhese of which we acquired a 25% stake last year, the European team reached their first major milestone with the expansion of their self-service platform to include display campaigns on ah.nl and in the AH app.
- Simultaneously, in the U.S. advertisers can now reach our 44 million customers all from one platform. And just recently, our U.S. AD Retail Media ranked 5th best overall US Retail Media Network and scored the #2 position in the area of omnichannel sales data.

These are just a few examples to reiterate our excitement about the opportunities that are ahead of us and I am looking forward to sharing more on these and others at our Strategy Day in May 2024 in the Netherlands.

In the meantime, you can continue to count on us to leverage our scale and position as market leaders, work closely with suppliers to mitigate price increases and doing our homework managing our costs and investments. As a responsible company, we will also continue to take action and create future focused plans to tackle the challenges of climate change and sustainability.

In terms of the 2023 outlook, we are updating as follows.

- We now expect free cash flow for 2023 in a range from 2.2 billion to 2.4 billion euro, reflecting the ongoing strong operating cash flows and improvements made by our brands in working capital management.
- Net capital expenditures are now expected to be around 2.4 billion euro.
- Underlying EPS is now expected to be slightly below 2022 levels, as we see the reduction in federal government support having a more negative impact than we originally expected.

In addition, we remain committed to our underlying operating margin of ≥4.0% for 2023, to our dividend policy and share buyback program, as previously stated.

We are also announcing today a new one billion euro share buyback program to start at the beginning of 2024.

Thank you for your continued interest in our company and Operator, please open the lines for questions.

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This communication includes forward-looking statements. All statements other than statements of historical facts may be forward-looking statements. Words and expressions such as expect(ed)/(s)/(ation), growth, planned, implied, commitment, continu(es)/(e)/(ing), long-term, ambitions, transforming, transition, to be, commit(ted)/(ment), strategy, will, accelerate initiatives, outlook, uncertainty or other similar words or expressions are typically used to identify forward-looking statements.

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