Management's Prepared Remarks

Q1 2021 Earnings Call

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Senior Vice President, Head of Investor Relations

Thank you operator, and good morning everyone.

Welcome to our first quarter 2021 results conference call.

On today's call are Frans Muller, our CEO and Natalie Knight, 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.

I ask that you please limit yourself to 2 questions. If you have further questions, then please re-enter the queue.

I'll now turn the call over to Frans.

Frans Muller

President, Chief Executive Officer

Thank you, Alvin.

Good morning everyone.

We have now surpassed the one-year mark of the COVID-19 pandemic, and its effects continue to have an impact across our geographies. In response, we spent approximately €150 million in Q1 to support customers, associates, and communities with COVID-19 relief care, which is more than double the amount compared to Q1 of last year. We also pledged approximately €20 million in charitable donations for this year, split evenly between the U.S. and Europe. And we continue to support health and safety measures, which remains a top priority to enable us to further strengthen our brands' positions as leading local omnichannel retailers.

Our brands, together with our suppliers, remained focused on fulfilling their vital role in society by maintaining food and product supplies to local communities. In addition, our U.S. brands have supported vaccination efforts through their pharmacies.

I remain thankful for the efforts of associates, who have had a consistent focus on safety, while at the same time providing great customer service and community support.

Now let me focus a little bit on the financial results:

Natalie will go into more detail on the financial performance in Q1 as well as to our outlook for 2021. For now, you can see in our press release and on slide 4 some of the highlights.

Although COVID-19 continues to impact our results positively, we have now entered a period where our year over year growth rates are affected by the lapping of difficult prior year comparisons.

That said, we begin 2021 in a strategically much stronger position than before the COVID-19 pandemic began.

Overall, we are very pleased with the underlying Q1 performance in both the U.S. and Europe. Our two-year comparable sales stack sequentially accelerated in Q1 2021 versus Q4 2020 in both the U.S. and Europe, as we've been able to retain a strong level of underlying consumer demand by continuing to adapt to the enduring consumer behavior changes. These behaviors include increased working from home, preference for healthy and fresh products, ofcourse and higher online demand.

For those that are less familiar, we have spoken to a 2- year comparable sales growth rate, or what is also referred to as a 2- year comparable sales stack. This is simply the comp growth rate in the current year added to the comp growth rate in the prior year. Because of the volatility over the course of the prior year quarter, looking at the 2-year comp sales stack is a helpful measure and proxy to gauge the momentum between periods, and as I mentioned, it is was actually quite a good trend for the quarter.

Growth in our leading local omnichannel platform also sequentially accelerated, with nearly 190% net consumer online sales growth in the U.S. and nearly 80% growth in Europe in the quarter, at constant exchange rates.

Underlying operating margins were also very strong in the context of historical levels prior to COVID-19.

While COVID-19 continues to create significant uncertainty in 2021, the outstanding Q1 results provides us with the confidence to raise our underlying EPS and Group net consumer online sales growth outlook for the year as you have seen in our report.

Moving to slide 5. We began 2021 in a strategically stronger position versus pre-COVID-19 and as such, we remain confident that our 2-year stacked comp sales growth rates will be visibly better than they were pre-COVID-19. You certainly saw that happen this quarter for the reasons I mentioned a few moments ago.

In this slide, we highlight some of the initiatives to increase our share of the consumer wallet and improve our online capabilities.

- In 2021, we are continuing to increase our online capacity. A few examples are the opening of more U.S. click-and-collect locations and a new home delivery fulfillment center at Albert Heijn.

- We are moving forward with the launch of Ship2Me in the U.S., our "endless aisle" offering of over 100,000 general merchandise and food items in the second half of this year.

- We are expanding our no-fee home delivery service AH Compact to additional markets in the Netherlands and are offering also 2 hour or less delivery in more cities in Greece and Romania.

- With increased capacity and strong momentum, we now expect Group net consumer online sales to grow by over 40% in 2021 versus 30% previously indicated. This includes raised expectations of over 70% growth in U.S. online sales, versus over 60% growth previously. It also reflects the expectation for at least €5.5 billion in net consumer online sales at bol.com, versus at least €5 billion previously.

- Improving omnichannel productivity also remains a high priority, and we strive to improve online productivity by 20% this year through an end-to-end improvement of processes, systems, operating practices and innovation.

Slide 6 highlights some of the key achievements in the U.S.

In the U.S., we delivered accelerating levels of online growth of nearly 190%. Even excluding sales from Fresh Direct, which we acquired in January, growth accelerated to 135%. Fresh Direct is progressing as planned.

We are in a good position to continue capitalizing on the higher online demand, with our U.S. household coverage now 95% through home delivery and Click & Collect. We have household coverage of 94% for same-day options as well. These are significant improvements in coverage over the prior year.

Also, the Stop & Shop remodeled stores continue to provide a sales uplift and we expect to accelerate the number of remodels in 2021 to approximately 60 stores.

Food Lion achieved its 34th consecutive quarter of positive comparable sales growth and has successfully added and opened all 62 of the Southeastern Grocer stores which we acquired by April. Also in April, we secured and opened additional 9 locations that were previously closed by Southeastern Grocers. These stores are in addition to the previously announced deal.
Slide 7 highlights some of the key achievements in Europe.

In Europe, our Benelux ecosystem continued to perform well and we gained market share in both the Netherlands and Belgium in the quarter.

We were also pleased with high level of net consumer online sales growth which also accelerated, particularly at bol.com, where sales from third party sellers grew 101%. The number of sellers on the platform also continues to grow, and there are now 45,000 sellers in The Netherlands.

Albert Heijn continued to remodel an additional 29 stores to its fresh and technology focused format in Q1 and they are all performing inline or ahead of expectations. We will remodel approximately 60 stores by the year end.

Albert Heijn continued to expand its home delivery service in the Flanders region in Belgium. We are now serving an additional 100,000 households, totaling 400,000 households.

The Delhaize SuperPlus loyalty plan providing rewards and discounts to consumers of healthy and sustainable products is providing a sales uplift and continues to gain traction. The program ended Q1 with nearly 1.7M members, up from 1.35M in Q4 of last year.

Moving on to slide 8. We continue to make progress in elevating our Health & Sustainability strategy and I'll discuss a few of these items.

- We recently announced a new goal for all of our brands to achieve net-zero carbon emissions by 2050.

- In March, Albert Heijn was voted by consumers as the Netherlands' most sustainable supermarket chain in the Sustainable Brand Index 2021 ranking for the fifth consecutive year. Bol.com was voted as the most sustainable e-commerce brand in the Netherlands as well.

- We also successfully priced our inaugural sustainability-linked bond in March, amounting to €600 million with a term of nine years, linked to achieving targets in reducing food waste and scope 1 and 2 carbon emissions by 2025.

I'll now hand it over to Natalie.

Natalie Knight
Chief Financial Officer

Thanks and good morning everyone.

Our underlying performance in the first quarter was strong and continued to be impacted by high levels of demand due to COVID-19. As a result, net sales grew 5.8% at constant exchange rates to €18.3 billion and Group comparable sales growth ex-gas was 4.2%.

Group net consumer online sales increased 103.3% in Q1 at constant exchange rates.

Group underlying operating income fell 6.1% at constant rates, to €849 million, with underlying operating margin down 60 basis points to 4.6% at constant rates. The margin was strong in the context of historical levels prior to COVID-19. Recall that margins in Q1 2020 benefited significantly from the timing of unexpectedly higher sales late in the quarter that preceded the COVID-19 costs, especially in the U.S. Moreover, this year, group underlying operating margin in Q1 was negatively impacted by COVID-19 related costs of approximately €150 million, versus only €70 million in 2020.

Underlying income from continuing operations was €566 million, down 11.9% in the quarter.

In Q1, we repurchased 13.6 million shares for €312 million.

Diluted underlying EPS was €0.54, down 8.4% compared to last year's record Q1 results.

To put this into perspective, 2021 diluted underlying EPS grew approximately 38% relative to 2019, which was prior to the COVID-19 impacts.

Slides 11 shows you our results on an IFRS-reported basis for Q1.

Moving on to slide 12. You heard Frans mention that we have held onto the high levels of consumer demand, even as we began to lap the COVID-19 impacts from last year. You can see here why that was the case on this slide, as comp sales trends on a 2-year stack basis were strong and better than pre-COVID levels. There was even an acceleration in momentum as we moved from Q4 into Q1.

In the U.S., we posted a 15.5% 2-year comp sales stack in Q1, which is a clear acceleration versus the 13.5% 2- comp sales stack we achieved in Q4.

In Europe, it was 18.1% in Q1 versus 13.9% in Q4. So we have good momentum, clearly demonstrating that our brands are continuing to execute very well in this fluid environment.

On chart 13, you can see that even after we adjust for the influences of weather and calendar on the 2-year comp sales stack, it's the same story – our momentum has been strong and we it picked up from Q4 into Q1. I will talk more about exactly what these calendar and weather impacts were this year, in a moment.

From a regional perspective, we posted a 14.6% adjusted 2-year comp sales stack in the U.S. in Q1, which is an acceleration versus the 13.8% adjusted figure in Q4.

In Europe, it was an adjusted 17.2% in Q1 versus 14.0% in Q4.

So anyway you look at it, our 2-year comp sales stack momentum accelerated in both regions.

Moving on to our first quarter performance by segment on chart 14.

Net sales in the US grew by 3.6% at constant rates, to €10.7 billion. U.S. comparable sales excluding gasoline grew 1.7%, positively impacted by demand related to COVID-19, particularly in January and February. This represents a stable sales development excluding 1.7 percentage points of the net benefit from calendar shift and a weather impacts in the quarter, mainly related to winter storms and the Easter shift. Challenging weather results in more consumer stock up activity and eating at home, and an earlier Easter pushed demand forward into Q1 versus Q2 last year.

Strong growth in January and February was offset, in part, by a decline in March's comparable sales, which were unfavorably impacted by the lapping of significant consumer stock-up activity related to COVID-19 in 2020, when comparable sales excluding gasoline grew 33.8% that month.

Another important call out on the US topline, was our online sales, which increased 188.3% in the quarter. Excluding these sales from our acquisition of FreshDirect, the U.S. online sales growth rate in Q1 2021 sequentially accelerated to 135.2% growth versus the 128.5% growth of Q4 2020.

Our underlying operating margin in the U.S. was 4.8%, down 1.8 percentage points from the prior year at constant exchange rates, as margins lapped unusually high levels in the prior year. You'll recall that we experienced high COVID-19 sales late in the prior year quarter that preceded the COVID-19 costs. In addition, higher COVID-19 related costs versus 2020 also impacted this year quarter.

In Europe, net sales in the first quarter grew by 9.4% to €7.5 billion and comparable sales increased 8.3%. Sales were positively impacted by demand related to COVID-19, again particularly in January and February. To a lesser extent, Q1 comparable sales were favorably impacted by approximately 0.5 percentage points from calendar shifts in 2021. Comparable sales remained positive in March despite the lapping of significant consumer stock-up activity related to COVID-19 in 2020, when comparable sales excluding gasoline grew 15.9% that month.

Net consumer online sales in Europe grew 78.6% in Q1, which was a sequential acceleration from the 73.4% growth in Q4. At bol.com, our online retail platform in the Benelux, which is included within the Europe segment results, net consumer sales growth accelerated to 76.6% in Q1 versus 69.6% in Q4. A big driver of this development was Bol.com's third party sales, which grew 101% in the quarter.

Europe's Q1 underlying operating margin was 4.7%, up 60 basis points from the prior year at constant rates. Margin expansion was driven by operating leverage from strong sales growth as a result of COVID-19.

Moving on to free cash flow in the first quarter and you see that on slide 15. Free cash flow in Q1 was €295 million, which compares with about €1 billion last year. This development was largely impacted by the unwind of inventories and accounts payables due to lapping high levels of consumer stock-up activity related to COVID-19 last year. There was also an decrease in net capital expenditure of €217 million as we anniversary the acquisition of several C&S warehouses related to our U.S. supply chain transformation initiative in the prior year.

Moving on the outlook for 2021 on slide 16.

While COVID-19 continues to create significant uncertainty for the remainder of 2021, our strong Q1 results provide us with confidence to raise our underlying EPS growth outlook for the year. The results outperformed our expectations and we've been able to retain a solid level of underlying consumer demand, as evidenced by the high 2-year comp sales stack. The rest of the guidance items on this slide are unchanged from our previously provided outlook.

As a quick reminder, COVID-19, and to a lesser extent, a 53-week calendar, significantly distorted our 2020 financial performance. Lapping these effects will impact results in 2021, which returns to a 52-week calendar. While higher sales demand drove unprecedented sales growth and operating leverage in 2020, this development, and to a lesser extent- the once every 5- year occurrence of a 53rd retail week, will challenge comparisons significantly this year.

We continue to expect the comp sales trajectory to be better on a 2-year basis in 2021 compared to pre-COVID-19 level. And while it doesn't affect our comp store sales, our recent acquisitions of Fresh Direct as well as stores from Southeastern Grocers and Deen Supermarkets later this year, will provide us with incremental sales.

Moving on to underlying operating margin, we continue to expect at least 4% in 2021 due to the strong sales related to COVID-19. Our margin outlook reflects a balanced approach with cost savings of over €750 million offsetting cost pressures related to COVID-19, as well as the impact from increased online sales penetration.

We are raising our underlying EPS outlook due to the outperformance in Q1 and strong momentum in the business. We now expect it to grow in the low to mid- teen range relative to 2019 versus our previous outlook of mid- to high-single digit growth.

Free cash flow is still expected to be approximately €1.6 billion, inclusive of net capital expenditure of around €2.2 billion.

I'll now hand it back over to Frans.

Frans Muller

President, Chief Executive Officer

Thank you Natalie.

So let me wrap up.

We started 2021 in a strategically stronger position when compared to pre-COVID-19, and we delivered a sequential acceleration in the two-year Q1 comparable sales stack across our regions.

We also continued to accelerate our net consumer online sales growth in a meaningful way.

We posted a solid underlying U.S. operating margin in Q1, and expanded margins in Europe.

In Q1, we successfully closed the acquisitions of Fresh Direct and stores from Southeastern Grocers, and are progressing as planned for both. The acquisition of Deen stores still on track to close in 2H 2021.

We are raising our net consumer online sales outlook to over 40% in 2021, versus 30% previously. This includes a raised outlook for over 70% growth in the U.S. and a higher target for bol.com to achieve least €5.5 billion in net consumer online sales.

Our strong performance in the quarter provided us the confidence to raise our underlying EPS guidance to low to mid-teen growth relative to 2019.

On the ESG front, we are proud to have launched our inaugural Sustainability-Linked Bond amounting to €600 million in March, linked to achieving targets in reducing food waste and scope 1 & 2 carbon emission by 2025. We also recently announced our target to achieve net-zero carbon emissions by 2050 .

We will now be happy to take your questions. Operator, can you please proceed?

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