Management's Prepared Remarks

Q2 2021 Earnings Call

August 11, 2021

JP O'Meara

Senior Vice President, Head of Investor Relations

Thank you operator, and good morning everyone.

I'm J.P. O'Meara, the new incoming Head of Investor Relations and I am delighted to welcome you to our Q2 2021 results conference call.

On today's call are Frans Muller, our CEO and Natalie Knight, our CFO. Alvin Concepcion, the outgoing Head of Investor Relations is also joining us today. 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.

To ensure everyone has the opportunity to get their questions answered today, I ask that you please limit yourself to 2 questions. If you have further questions, then please re-enter the queue.

Before I turn over to Frans, I would like to announce that we are planning to host our Investor Day on November 15th, 2021. Please save the date for now, with more details follow in due course.

I'll now turn the call over to Frans.

Frans Muller

President, Chief Executive Officer

Thank you, JP and welcome on board.

Good morning everyone.

We are pleased with our Q2 performance, in which associates in all of our brands continued to work tirelessly in a rapidly shifting environment.

We would also like to express our support for everyone impacted by the recent flooding in the Netherlands and Belgium, as well as the fires in Greece. We are committed to serving these communities and our brands' associates during these difficult times.

In this regard, we remain on track to deliver on our pledge to contribute €20 million in charitable donations in 2021. And again, this is just a portion of our broader spending for COVID-19 related care and other initiatives, which amounted to €84 million in Q2.

In Q2, our brands, together with suppliers, remained focused on fulfilling their vital role in society by maintaining food and product supplies to local communities.

And we remain thankful for the efforts of associates, who have put a consistent emphasis on safety, while at the same time providing great customer service and community support.

We are aware of the recent increases in infection rates in many of our markets and will continue to provide assistance in all our communities, including COVID-19 vaccination efforts in the U.S..

Now let me highlight our key financial results:

As a reminder, Q2 2020 was a particularly difficult quarter to comp against, as it represented the height of COVID-19 stock-up activity, which drove 20.6% comp sales growth in the US and +10.2% comp sales growth in Europe during the year ago period.

In that light, I am very proud of our Q2 performance, in which US comp sales excluding gas were only down –1.5% versus last year's robust sales levels. And our European comp sales excluding gas grew +2.4% year-over year.

On a 2-year-stack comp sales basis, US and Europe grew 19.1% and 12.6% respectively, both representing an acceleration versus 2020.

This strong result comes against a backdrop in which several communities across our markets reopened during Q2, suggesting that new behaviors picked up by consumers during the COVID pandemic continue to be quite sticky, as demand for food-at-home remains very resilient.

At the same time, our results also underscore that our operations are exiting the COVID pandemic in a stronger position, led by our omnichannel platform which continued to drive strong market shares during the quarter.

As such, our online business posted strong double-digit growth in Q2, and our underlying operating margins were very strong in the context of historical levels prior to COVID-19.

This has prompted us to once again raise our 2021 EPS guidance, reflecting the strength of our first half year results. And we have also increased our group underlying operating margin outlook to approximately 4.3%, up from our original guidance of "at least" 4.0%.

Natalie will go into more detail on the financial performance in Q2 as well as our outlook for 2021.

So let me move onto slide 5, where we show why we continue to have confidence in the strength of our omnichannel proposition, which is being enhanced by the significant reinvestments we are making back into the business.

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

- In support of our online fulfillment capacities, we are opening two new home delivery centers in New York which will go live in 2022

- We are also scheduled to open our first home delivery fulfillment center in Serbia in early 2022

- In Q2, we expanded the acceptance of SNAP/EBT benefits for online grocery orders, which is now available at all of our US brands, improving accessibility for low-income customers

- Our no-fee home delivery service AH Compact added 20 new areas during Q2, and is now in 26 areas across the Netherlands

- And our focus on productivity will be enhanced by an AI-enabled end-to-end forecasting and replenishment system being finalized later this year

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

We remain on track for +70% US online sales growth in 2021, bolstered by the expansion of our Click and Collect capacity as well as the FreshDirect acquisition.

Speaking of Click and Collect, we opened 86 additional Click & Collect locations during Q2 and remain on pace to end 2021 with approximately 1,400 Click & Collect locations, up from around 1,100 at the beginning of the year.

We also remodeled 14 additional Stop & Shop stores in Q2, bringing the total number of stores remodeled since the inception of the program to nearly 100. And we continue to see solid sales uplifts from our remodeled stores.

Finally, from a brand perspective, I'd again like to call out Food Lion, which achieved its 35th consecutive quarter of positive comparable sales growth. In addition, the 71 stores that have been integrated year-to-date are exceeding sales expectations.

Slide 7 highlights some of our key achievements in Europe.

Our Benelux ecosystem continued to perform well and we gained market share in both the Netherlands and Belgium in the quarter. This was driven by both strong campaigns during the Euro championships, and continued strong performance of health and sustainability activities.

We were encouraged by the 24.2% growth in net consumer online sales at bol.com during Q2, which came on top of 65.4% growth in the year ago period. The number of sellers on the platform also continues to grow, and now stands at 47,000.

We are pleased with Dutch regulator ACM's approval of Albert Heijn's pending acquisition of 38 DEEN stores; which remains on track to close next quarter.

In Q2, Albert Heijn upgraded another 18 stores to its fresh- and technology-focused format and they are performing right in-line with expectations. We remain on track to remodel approximately 60 stores by year end.

And in Belgium, Albert Heijn continued to expand its home delivery service by doubling its coverage versus Q1 to 800 thousand households.

The Delhaize SuperPlus loyalty plan which gives rewards and discounts to consumers of healthy and sustainable products continues to gain traction providing a nice sales uplift. The program ended Q2 with approximately 1.9M members, up from 1.7M in Q1.

We were also encouraged by the rebound seen in the performance at our Central and Southeastern Europe brands.

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 are proud to be one of the leading signers of the EU Code of Conduct for Responsible Food Business and Marketing Practices, as part of the European Green Deal, which is committed to shifting to a sustainable food system. As part of the pact, we have made 10 commitments in the areas of healthier choices, product transparency, waste reduction and climate impact.

- Following successful implementation in other European markets, Mega Image became the first food retailer in Romania to introduce the Nutriscore nutritional navigation system across its own brand products. And in the U.S., we are pleased with our result that 52.4% of our Q2 sales are healthy, earning the Guiding Stars 1, 2 or 3 rating. This is inline with our company-wide ambition to raise sales of healthy own-brand products to 51% by the end of 2022; in 2020 we reached 49.8%.

- And in the US, the Giant Company rolled out the Flashfood app across all stores in June. The app reduces waste and promotes healthy eating by providing customers with significant discounts on fresh foods nearing their best before date.

Finishing on that positive note, let me now hand over to Natalie.

Natalie Knight

Chief Financial Officer

Good morning and thank you Frans.

Our underlying performance in the second quarter was strong and continued to be impacted by high levels of demand due to COVID-19. As a result, net sales grew 3% at constant exchange rates to €18.6 billion. And Group comparable sales growth ex-gas was flattish, which as a reminder comes against robust group comp sales growth in the year ago period of 16.4%.

Group net consumer online sales grew 35.8% in Q2 at constant exchange rates, aided by the strong performance in the U.S., including the FreshDirect acquisition, as well as at bol.com.

Group underlying operating income declined 12.2% at constant rates, to €832 million, with underlying operating margin down 80 basis points to 4.5% at constant rates. The Q2 2021 margin was strong in the context of historical levels prior to COVID-19. Recall that margins in Q2 2020 hit record levels, driven by significant sales leverage and mix benefits related to COVID-19 stock-up activity.

Underlying income from continuing operations was €551 million, down 15.5% in the quarter.

And in Q2, we repurchased 7.5 million shares for €176 million.

Diluted underlying EPS was €0.53, down 12.1% at constant rates, compared to last year's record Q2 results.

To put this into perspective, 2021 diluted underlying EPS grew approximately 55% relative to 2019 at current rates, which was prior to the COVID-19 impacts.

Slides 11 shows our results on an IFRS-reported basis for Q2.

Moving on to slide 12. We have been able to drive high levels of consumer demand, even as we are lapping the COVID-19 impacts from last year. You heard Frans mention that many of the habits formed by consumers during the COVID-19 pandemic in 2020 are proving sticky, aided

by our initiatives to improve our omnichannel offerings for consumers. You can see this in our results, particularly on this slide, as comp sales trends on a 2-year stack basis were strong and better than pre-COVID levels.

In the U.S., we posted a 19.1% 2-year comp sales stack in Q2, which is a clear acceleration versus the 15.8% 2-year comp sales stack we achieved in 2020, as well as the 15.5% 2-year comp sales stack from Q1.

In Europe, it was 12.6% in Q2 versus 12.3% in 2020, and 18.1% in Q1. So the strong level of 2-year comp sales stack continued into Q2, where we also saw several of the Central and Southeastern Europe countries rebounding after being challenged much of the past year.

All in all, we have good momentum occurring across our business, demonstrating that our brands are continuing to execute very well in this fluid environment and that consumer behavior towards eating more at home is proving to be sticky.

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 sales trends are strong, and remain elevated versus pre-COVID levels. 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 15.9% adjusted 2-year comp sales stack in the U.S. in Q2 which includes holiday shifts for Easter and the Fourth of July as well as the exclusion of 2019's Stop & Shop strike effect, which is an acceleration versus the 14.6% adjusted figure in Q1.

In Europe, the 2-year comp sales stack was 13.4% in Q2 versus 17.2% in Q1 after adjusting for calendar and weather impacts.

So any way you look at it, our 2-year comp sales stacks were strong in both regions.

Moving on to our second quarter performance by segment on slide 14.

Net sales in the US grew by 2.7% at constant rates, to €11.1 billion. U.S. comparable sales ex gas were down 1.5%, against a tough comp of the year ago period, when COVID-19 related stock-up activity drove 20.6% comparable sales growth excluding gas.

Our U.S. online business continues to grow sales at solid double-digit rates, even as we lap triple digit growth in the year ago period, when COVID drove a step change in the way some consumers shop, favoring online purchases.

US online sales were up 61.0% in constant currency, driven by increased Click and Collect capacity as well our FreshDirect acquisition.

Thus, the early read-through suggests that elevated online grocery demand garnered during the COVID-19 pandemic is having a positive and sustainable effect on our business. And we stand ready to continue our strong execution in this environment and continue to increase our investments in our digital and omnichannel capabilities.

Our underlying operating margin in the U.S. was 5.0%, down 1.1 percentage points from the prior year at constant exchange rates, as margins lapped the unusually high levels of the prior year. Nonetheless, the Q2 2021 US underlying operating margin was elevated versus pre-COVID levels, due to strong sales leverage.

In Europe, net sales in the second quarter grew by 3.6%, to €7.5 billion and comparable sales increased 2.4%. Sales benefitted from sustained food at-home demand across our markets in aggregate, and further growth at bol.com. It should also be noted that Q2 comparable sales were negatively impacted by approximately 0.7 percentage points from calendar shifts in 2021.

Net consumer online sales in Europe grew 27% in Q2, on top of 64% growth in the same period last year. At bol.com, our online retail platform in the Benelux, which is included within the Europe segment results, net consumer sales grew 24.2% this quarter. Bol.com third party sales continued to grow and were up 26%, with nearly 47,000 merchant partners active on the platform.

Underlying operating margin in Europe was 4.2%, down 0.3 percentage points from the prior year at constant exchange rates, due to reduced operating leverage versus 2020 as well as continued costs related to COVID-19.

Moving on to free cash flow in the second quarter, which you can see on slide 15. Free cash flow in Q2 2021 was €428 million, which compares to €533 million last year. This development was largely impacted by lower operating cash flows in Q2 2021, when the business lapped record margins from the year ago period, that were induced by significant COVID-19 stock-up activity.

Moving on to our outlook for 2021 on slide 16.

We've mentioned more than once that COVID-19 continues to create significant uncertainty for the remainder of 2021, but our strong Q2 results provide us with confidence to again raise our full year 2021 EPS and operating margin outlook.

As a reminder, COVID-19, and to a lesser extent, a 53-week calendar, significantly distorted our 2020 financial results. 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, are creating challenging comparisons in 2021.

We continue to expect the comp sales trajectory to be better on a 2-year basis in 2021 compared to pre-COVID-19 levels. And while it doesn't affect our comp store sales, our Q1 acquisitions of Fresh Direct as well as stores from Southeastern Grocers, along with Deen Supermarkets later this year, will provide us with incremental sales.

We are raising our underlying operating margin outlook to approximately 4.3% versus at least 4.0% previously, reflecting the strong margin performance over the first half of the year. The margin outlook continues to embed balancing the effects of cost savings of over €750 million, offsetting cost pressures related to COVID-19, as well as the earnings dilution from increased online sales penetration.

As such, we are raising our full year 2021 underlying EPS outlook, which is now expected to grow by high-teens relative to 2019. This is up from our prior guidance range of low to mid-teens growth versus 2019.

Moving over to free cash flow, where we continue to expect approximately €1.6 billion, inclusive of net capital expenditure of around €2.2 billion. Free cash flow will be impacted by the unwind of working capital, such as inventories and accounts payables, due to lapping high levels of consumer stock-up activity related to COVID-19 in the prior year.

Today, we are also announcing our 2021 interim dividend of €0.43, compared to €0.50 in the prior year period, which is inline with our interim dividend policy of 40% of the year-to-date underlying income from continuing operations. That said, for the full year we remain on track to grow our full year 2021 dividend payment, with a 40-50% payout ratio.

I'll now hand it back over to Frans.

Frans Muller

President, Chief Executive Officer

Thank you Natalie.

So let me now wrap things up.

We are pleased with our Q2 results, which featured accelerating 2-year comp sales stack trends versus 2020 and continued growth in our online business.

These results are not only indicative of strong food-at-home demand, but also reflect the power of our accelerating our omnichannel platform capabilities.

It's also important to note that our top line performance is translating into solid profitability. Our Q2 underlying operating profit margin of 4.5% compares favorably to our pre-COVID margin profile and our first half results give us confidence to raise our full year 2021 underlying EPS and UOM guidance.

We have also announced an interim 2021 dividend of 43 cents per share, and remain on track to growing our full year 2021 dividend payment.

We have recently received approval from the Dutch regulation body for our pending acquisition of 38 Deen stores, which we anticipate closing in Q3.

And importantly, we are proud to be one of the leading signers of the EU code of conduct for Responsible Food Business and Marketing, which is in line with our ambition to elevate healthy & sustainable.

Ahold Delhaize

Before I pass it on to the operator for the Q&A, I would like to take this opportunity to thank Alvin Concepcion for his strong contributions to our organization over the last three years. Alvin will continue to support us and onboard JP in August, and Natalie and I want to wish you, Alvin, and your family all the best for the future.

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

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Cautionary notice

This communication includes forward-looking statements. All statements other than statements of historical facts may be forward-looking statements. Words and expressions such as in due course, would, committed, remain(s), on track, continue(d), focus, will, later this year, by year end, expect, anticipate, ambition or other similar words or expressions are typically used to identify forward-looking statements.

Forward-looking statements are subject to risks, uncertainties and other factors that are difficult to predict and that may cause the actual results of Koninklijke Ahold Delhaize N.V. (the "Company") to differ materially from future results expressed or implied by such forward-looking statements. Such factors include, but are not limited to, risks relating to the Company's inability to successfully implement its strategy, manage the growth of its business or realize the anticipated benefits of acquisitions; risks relating to competition and pressure on profit margins in the food retail industry; the impact of economic conditions on consumer spending; turbulence in the global capital markets; political developments, natural disasters and pandemics; climate change; raw material scarcity and human rights developments in the supply chain; disruption of operations and other factors negatively affecting the Company's suppliers; the unsuccessful operation of the Company's franchised and affiliated stores; changes in supplier terms and the inability to pass on cost increases to prices; risks related to corporate responsibility and sustainable retailing; food safety issues resulting in product liability claims and adverse publicity; environmental liabilities associated with the properties that the Company owns or leases; competitive labor markets, changes in labor conditions and labor disruptions; increases in costs associated with the Company's defined benefit pension plans; the failure or breach of security of IT systems; the Company's inability to successfully complete divestitures and the effect of contingent liabilities arising from completed divestitures; antitrust and similar legislation; unexpected outcomes in the Company's legal proceedings; additional expenses or capital expenditures associated with compliance with federal, regional, state and local laws and regulations; unexpected outcomes with respect to tax audits; the impact of the Company's outstanding financial debt; the Company's ability to generate positive cash flows; fluctuation in interest rates; the change in reference interest rate; the impact of downgrades of the Company's credit ratings and the associated increase in the Company's cost of borrowing; exchange rate fluctuations; inherent limitations in the Company's control systems; changes in accounting standards; adverse results arising from the Company's claims against its self-insurance program; the Company's inability to locate appropriate real estate or enter into real estate leases on commercially acceptable terms; and other factors discussed in the Company's public filings and other disclosures.

Forward-looking statements reflect the current views of the Company's management and assumptions based on information currently available to the Company's management. Forward-looking statements speak only as of the date they are made, and the Company does not assume any obligation to update such statements, except as required by law.