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Lancaster Colony Corp. (LANC)

Q1 2018 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Joey, and I will be your conference call facilitator today. At this time, I would like to welcome everyone to the Lancaster Colony Corporation Fiscal Year 2018 First Quarter Conference Call. Conducting today's call will be Dave Ciesinski, President and CEO; and Doug Fell, Vice President, Treasurer and CFO. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer period. [Operator Instructions] Thank you. Now, to begin the conference call, here is Dale Ganobsik, Director of Investor Relations for Lancaster Colony Corporation.

Dale N. Ganobsik
Director-Investor Relations, Lancaster Colony Corp.

Thank you, Joey. Good morning, everyone. Thank you for joining us today for Lancaster Colony's fiscal 2018 first quarter conference call. Let me begin by reminding everyone that our discussion this morning may include forward-looking statements, which are subject to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995. These statements are subject to a number of risks and uncertainties that could cause actual results to differ materially and the company undertakes no obligation to update these statements based upon subsequent events. A detailed discussion of these risks and uncertainties is contained in the company's filings with the SEC. Also note that the audio replay of this call will be archived and available at our website lancastercolony.com later this afternoon.

With that said, I'll now turn the call over to Lancaster Colony's President and CEO, Dave Ciesinski. Dave?

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

Thanks, Dale, and good morning, everyone. It's a pleasure to be here with you today as we review our first quarter results for fiscal year 2018. Doug and I will provide comments on the quarter and our outlook, and following that, we'll be happy to respond to any of your questions.

During the first quarter, the company completed changes to our organization structure as I succeeded Jay Gerlach as Chief Executive Officer effective July 1. This change has resulted in modifications to have the company who manages our business and allocates our resources. Consequently, the company's segment reporting structure has been amended to align with these changes and our Specialty Foods segment results will now be presented as two reportable segments, Retail and Foodservice.

Additional details regarding this change in reporting structure are provided in the company's 8-K filing this morning in conjunction with our fiscal first quarter earnings results.

For the quarter, we're pleased to report consolidated net sales increased 2.6% to a first quarter record of $298.9 million versus $291.4 million last year. Retail net sales grew 6.2% to $162.1 million as our organic sales advanced 4% and sales from Angelic Bakehouse, acquired in November of 2016, added 2.2%. Organic sales growth was led by volume gains from Sister Schubert's frozen dinner rolls, Marzetti caramel dips, Olive Garden dressings, and New York Bakery (sic) [New York BRAND Bakery] (03:11) frozen garlic bread products.

Net sales of Marzetti produce dressing also showed a slight uptick in the quarter as competitive promotional practices in the category have started to abate. Overall trade spending and coupon expenses as a percentage of net sales were flat compared to the prior year quarter.

Foodservice net sales decreased 1.4%, reflecting continued overall softness in the restaurant industry. Sales volumes to our national chain restaurant accounts were below the prior-year amount, partially offset by a modest level of inflationary pricing.

Sales attributed to limited-time-offer programs with our national chain customers were nearly equal to last year. Consolidated gross profit declined $5.1 million to $75.5 million, driven by the impact of increased commodity costs, most notably soybean oil, dairy ingredients, eggs, garlic and higher freight costs. Supply chain cost savings realized from our lean six sigma program and inflationary foodservice pricing served to partially offset the higher freight and commodity costs in the quarter.

Also note that the historically high gross margins reported in the prior-year quarter reflect the benefit of unusually low commodity and material costs. This is particularly true in our Foodservice segment where the timing of input costs and related price recoveries to our national customers will often lag and overlap each other and occasionally will give rise to larger than normal margins in a given quarter. That was the case during the second half of our fiscal year 2016 – our first half of our – our second half of our fiscal year 2016 and first half of our fiscal year 2017.

Selling and general, administrative expenses rose $1.3 million due to the incremental amortization expense and other recurring non-cash charges attributed to Angelic Bakehouse, along with the recent investments in business initiatives and personnel dating back to our third fiscal quarter of last year.

Consolidated operating income declined to $44.3 million to (sic) [from] (05:24) $50.8 million in the prior year on lower gross profit and increased SG&A expenses. Both Retail and Foodservice segments were unfavorably influenced by the higher freight and commodity cost referenced above.

Retail operating margin decreased from 22.8% to 20.3%, including the full impact of Angelic Bakehouse noncash charges totaling $800,000. Foodservice operating margin dropped 14.4% to 10.7%. The prior-year margin reflects a significant benefit from lower ingredient costs that were only partially offset by deflationary pricing. The reduction in corporate expenses is primarily due to nonrecurring costs incurred in the prior-year quarter related to closed business operations.

Net income was $29.4 million or $1.07 per diluted share, compared to $33.4 million or $1.22 per diluted share last year. The regular quarterly cash dividend was continued at the higher level of $0.55 per shares at November of 2016.

Turning our attention to Retail sell-through data from IRI for the 12 weeks ending October 1, 2017, we maintained our leadership position in all six of our key categories and we're able to increase our share in three out of six of those categories.

With that, I'd like to now turn it over to Doug to make some comments on the balance sheet and other related items.

Douglas A. Fell

Vice President, Chief Financial Officer & Treasurer, Lancaster Colony Corp.

Thank you, Dave. Overall, our balance sheet continues to remain strong and not much has changed since our last earnings call. I will comment on some of the larger line items within our balance sheet compared to last year.

From a high-level perspective, the increase in our cash balances of $14 million since June can be summarized as follows: Cash provided by operating activities of nearly $39 million, offset by regular dividends of $15 million; treasury stock repurchases of nearly $1 million; and property additions of $8.5 million. In general, accounts receivable remain in line with expectations and largely reflect increased sales volumes for the quarter. Consistent with past quarters, our collections and agings remain solid.

The increase in our inventory balances since June reflect stronger sales volumes for the quarter, as well as the normal [indiscernible] (07:59) seasonal inventories with shift during our second fiscal quarter. As I mentioned, cash expenditures for property additions totaled $8.5 million in Q1, with the largest amount spent on new processing equipment to accommodate growth and plant improvement projects to enhance productivity.

At the present time, we anticipate capital expenditures to be in the range of $30 million for fiscal 2018, and in general, we'll focus on projects to increase capacity and productivity. As we mentioned in our prior commentary, a notable project will involve increasing our warehousing and production capacity at Angelic Bakehouse. This project is now underway and progressing as scheduled. It is projected to wrap up towards the end of fiscal 2018.

Depreciation and amortization expense totaled $6.4 million for Q1 and we expect similar quarterly levels for the balance of fiscal 2018. With respect to our balance sheet capitalization, we continue to have no debt and over $590 million in total shareholder's equity.

We ended the quarter with $157 million in cash and equivalents, and we have available borrowing capacity under our credit facility of nearly $150 million. Given our balance sheet posture and overall liquidity, we continue to possess considerable flexibility to address our foreseeable cash requirements. In general, our plans for capital allocation in fiscal 2018 are expected to remain consistent with our best practices.

Finally, while our effective tax rate at 34.2% for the current quarter is in line with the prior year of 34.3%. We do wish to point out the adoption to the new accounting standard for the tax treatment of equity awards lowered our effective tax rate by 20 basis points in the current quarter. As we further described in the footnotes to our financial statements, looking forward, the adoption of the standard could create some level of volatility in our quarterly effective tax rate. Excluding its impacts, we expect our effective tax rate to be in the range of 34.4% for fiscal 2018.

Thanks again for your participation with us this morning, and I will now turn the call back over to Dave for our concluding comments. Dave?

David A. Ciesinski

President and Chief Executive Officer, Lancaster Colony Corp.

Thanks, Doug. Building upon our growth in Retail segment sales this past quarter, we will continue to rely upon our strengths and investments in innovation and product development to drive top line growth. A recent example of this is our new Marzetti Simply 60 line of refrigerated dressings with only 60 calories per serving, made with simple ingredients such as real buttermilk and extra virgin olive oil.

Although this new product line has only been in the market six weeks, early data shows an encouraging start. We look forward to sharing additional information with you about Marzetti Simply 60 and other new Retail and Foodservice products in the quarter ahead.

Looking ahead to our fiscal second quarter, historically our biggest sales quarter of the year, we expect higher freight cost to persist due to higher freight premiums resulting from the constrained capacity in the aftermath of the recent hurricanes in the southern U.S.

We also anticipate commodity cost to remain a headwind with eggs, soybean oil, dairy ingredients and garlic showing notable cost increases over the prior year and even since our last call with you. We intend to address this inflation with supply chain cost savings realized from our new lean six sigma program, inflationary pricing in Foodservice and net pricing initiatives now underway in Retail, as we continue to leverage our recent investments and trade optimization in category management. Joey, we can now take any questions from the call participants.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Frank Camma from Sidoti. Your line is open.

Frank Camma
Analyst, Sidoti & Co. LLC

Q

Good morning, guys.

Dale N. Ganobsik
Director-Investor Relations, Lancaster Colony Corp.

A

Good morning.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

A

Good morning, Frank.

Douglas A. Fell
Vice President, Chief Financial Officer & Treasurer, Lancaster Colony Corp.

A

Good morning, Frank.

Frank Camma
Analyst, Sidoti & Co. LLC

Q

Hey. I appreciate the color on the second quarter that you gave there. I was wondering if you could talk a little bit about the cadence in the second half though since some of these commodity costs will be built in, I assume, in the pricing of the Foodservice side. So, if you could just walk us through that and how we should think about that?

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

A

Sure. I guess I would probably think of it, Frank, in – as three drivers. The first of which is the fact as mentioned in the comments in the release earlier, for this quarter and Q2, we're going to continue to lap that record high level of gross margins that we had in prior period. Okay. [ph] At some point (12:52), if you look at this quarter last year, we would have been up 22%, driven by this sort of precipitous drop. This quarter, we're down 11%. In the last period of that, that we're going to lap is next is, is upcoming quarter Q2. So that's the first thing that you're going to want to sort of look at. And if you go back to our segment resulting, you look at the last few years, I think you'll get an idea of what's going on there.

The second thing that you're going to want to factor into the equation is, is inflation and probably the newest news of inflation for Q2 versus the back half of the year, as we've seen a pretty steep increase in egg cost. You may have heard it from others that you're covering, there's an issue with supply [ph] in Europe (13:34) that's driving a lot of export demand here from the U.S., which we're factoring in.

And then the last question is, how are we going to be addressing things with pricing? We do have Foodservice inflationary pricing that's underway and now there's going to be a second tranche of that that becomes effective at the very beginning of Q3.

And then, finally, we're also actively participating in pricing and trade rationalization efforts on the Retail business, the early of which are beginning right now actually, and there'll be another tranche that go out in the not too distant future.

Frank Camma
Analyst, Sidoti & Co. LLC

Q

Okay. And so, you are being able to push through some of this price increasing on to Retail, which is obviously interesting. Can you talk about sort of like – you really haven't been impacted by this, but obviously, with the Amazon buying Whole Foods, but sort of trend there, the competitive alignment and pushback you're seeing from your major customers on the Retail side, on pricing specifically?

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

A

We're in the very earliest stages of that. So, I think it's a TBD. What we would tell you is [ph] at the end of the (14:44) day, as a management team, we have three levers to address it, list price increases, net price realization by trade reduction, and then ultimately taking cost out. We're going to work all three levers, but given the magnitude and the steepness of the increases that we're seeing, particularly in core commodities like eggs, like dairy, butter, garlic and wheat, and transportation, when they start to move like this, you have no choice but to take the list price increase and have those conversations.

Frank Camma
Analyst, Sidoti & Co. LLC

Q

Okay. My last question and then I'll hop back is, Sister Schubert's, was that surprising how strong it was given, I mean – I know you've had some innovations there, but it's really not on trend per se in the frozen category and sort of not really particularly healthy living, et cetera? So, I just wonder if you can make some comments on that.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

A

That's a great question. It's – and it's a great story actually. I won't say I'm surprised because I've been watching the team that's been working on this for the year plus that I've been here and they've really done a terrific job. They've done a couple of things. They [ph] brought (15:53) to the market consumer-relevant innovation, one. They've also done a great job of simplifying the range of products.

They [indiscernible] (16:01) non-performing SKUs, focusing on seven items and getting retail execution right. And candidly, if you look at our portfolio brands, that may be the very most beloved brand that we have in our portfolio. It's grown in Retail and parenthetically, it's also growing in Foodservice. We usually don't break it out and talk about it, but it's actually a strong performer in our Foodservice business.

Frank Camma
Analyst, Sidoti & Co. LLC

Q

Well, it's very convenient, I guess, to take out the rolls and do it that way, so – well, congratulations.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.
A

Yeah, well, thank you. And I think the only other thing I'll note on that is, what we're finding is, if you look at the ingredients panel on that, it's actually pretty clean. There isn't a lot of bad stuff in that. And the consumers particularly in the south were the strongest. It is very much a beloved brand.

Frank Camma
Analyst, Sidoti & Co. LLC
Q

Okay. Good. Thanks, guys.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.
A

Thank you, Frank.

Douglas A. Fell
Vice President, Chief Financial Officer & Treasurer, Lancaster Colony Corp.
A

Thanks, Frank.

Operator: Your next question comes from Alton Stump from Longbow Research. Your line is open.

Alton K. Stump
Analyst, Longbow Research LLC
Q

Good morning, guys.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.
A

Good morning, Alton.

Dale N. Ganobsik
Director-Investor Relations, Lancaster Colony Corp.
A

Good morning.

Douglas A. Fell
Vice President, Chief Financial Officer & Treasurer, Lancaster Colony Corp.
A

Hi, Alton.

Alton K. Stump
Analyst, Longbow Research LLC
Q

Just at a higher freight costs and sort of how quickly – looking at Foodservice business in particular, are you able to pass through [indiscernible] (17:14) help offset some of the cost pressure coming from higher freight?

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.
A

I guess I would answer it in a couple of ways. There's one question, Alton, which is how long do we think that the increases are likely to persist, particularly driven by the two hurricanes that we've seen. And clearly, it was an impact in the latter part of our first quarter and we expect it to be an impact into the second quarter and then really taper and dissipate thereafter. If you look at prior-year hurricanes, that's essentially the pattern that it's taken.

As it pertains to our ability to pass along those increases, that stuff that were trying to affect right now into the marketplace, so we're hoping to recover some of those costs into Q2. And we'll see how we're able to deal with that. And if you're thinking about the overall magnitude of the increase here, and I would think of it in terms of a high six figure approaching seven figure number.

Alton K. Stump
Analyst, Longbow Research LLC

Q

Okay. Great. That's helpful. Thank you. And then I guess just one follow-up. That's 4% organic growth in Retail quite impressive. I just kind of look out, kind of rest of the full-year 2018, but also coming years – I mean, are there maybe sort of handful of categories that you see as being the key growth drivers, whether it's frozen breads, which is [indiscernible] (18:38) for quite some time now or [ph] are there smaller (18:40) categories that you can see kind of come at big players as far as driving overall growth in Retail?

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

A

Sure. We'd say across the waterfront, the way we've talked about our growth algorithm on the top line historically has been low mid-single digits and that's typically the target that we're going after. We're seeing balanced growth to-date, back to Frank's earlier question, if you look at dinner rolls, several years ago, 18 months ago, the category as a whole is down probably 100 basis points, maybe 150 basis points.

Now, the category overall is probably closer to up 50 basis points, if not more than that, and we're leading that overall category growth. Frozen garlic bread is another one of those that continues to grow. I think if you look over a longer period of time, we would expect to see an even greater amount of growth coming from the perimeter, particularly dressings and dips and fresh bakery items like Flatout and Angelic. But if you're in a sort of modeling across the next 18 months, I would look for balanced growth across all those segments.

Alton K. Stump
Analyst, Longbow Research LLC

Q

Great. Thanks so much, guys.

Douglas A. Fell
Vice President, Chief Financial Officer & Treasurer, Lancaster Colony Corp.

A

Thanks, Alton.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

A

Thanks, Alton.

Operator: Your next question comes from Brett Hundley from the Vertical Group. Your line is open.

Brett Hundley
Analyst, Vertical Trading Group LLC
Q

Hey, good morning, guys.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.
A

Good morning, Brett.

Dale N. Ganobsik
Director-Investor Relations, Lancaster Colony Corp.
A

Good morning.

Douglas A. Fell
Vice President, Chief Financial Officer & Treasurer, Lancaster Colony Corp.
A

Good morning, Brett.

Brett Hundley
Analyst, Vertical Trading Group LLC
Q

I actually wanted to follow on to that line of questioning that was just asked. We've been doing some store checks here in our market and have noticed a fair amount of assortment changes in numerous stores. So we're seeing some space being taken away from center of the store – condiments for instance – and we're seeing space expanded in the produce section, fresh. We're seeing space expanded in frozen to an extent, beverages and some other areas. And I'm curious kind of what you guys are seeing or experiencing if you're seeing any assortment changes for the specific categories that you play in either positive or negative?

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.
A

Sure. So, Brett, I guess I'd start by answering your question from a macro perspective and then I'll drill it in closer to maybe our business. If you look at things in the aggregate, we also are seeing the very same things that [ph] you're reflecting (21:10) in the marketplace, particularly at the retailers you're talking about and others. And I think if you are to sort of look over the range of, say the next two to five years, I think you're going to continue to see the center of the store shrink in particular categories and you're going to see incremental space devoted to the perimeter.

Having said that, as we look and plan near end, we still have and a lot of our retailers [indiscernible] (21:38) for example on produced dressings, and that hasn't really changed for years. So, as we're seeing these things happen, what we haven't necessarily seen is greater incremental space devoted to things like produced dressings. Our hope is that eventually we see that. We anticipate over time that we will see that.

Having said that, bringing it closer into where we are today and how we think about it, managing it, it's probably a two-part question. One is, we're trying to line up our strategy so that we're able to participate in that growth, so making incremental strategic investments in things like Angelic Bakehouse, Flatout in dressings and dips, because we feel like that's just going to become more relevant as more traffic runs around the racetrack.

But as we manage the business day-in and day-out in execution, what we're really focusing on is just getting the right assortment, having very clear what we call maps or gold standards for what we want our shelves to look like,

make sure that we have the right items on the shelf. And one of the things you'll note if you look at our data, Brett, is that we're actually down in GDPs in some of our categories and some of this work is of our own doing.

We talked about Sister Schubert's for example. That's a category where – or a business for us that probably 12, 18 months ago, we started to actually prune the number of SKUs because we had a number of slow movers and focused on what we called the [ph] Sister 7 (23:04), which were the top items and making sure that we were just nailing what the shelf needed to look like on those. And as a consequence, we've seen the business lift.

So one thing you will see in our business over time, and we're actually addressing this now in our dressing business is, we're going to be bold and go after underperforming SKUs and clip those before the retailers do. We believe it creates enhanced credibility for us and then come back with items that we think are winners and are going to grow our business in the category.

Brett Hundley
Analyst, Vertical Trading Group LLC

Q

I appreciate that. I want to ask you a follow on to that related to M&A but just real quick. Just to make sure I understand this correctly. The higher freight in Q1 that was partially called out related to hurricane activity that continues in Q2. You said that, that effect – I think you said was high six figures approaching seven figures. Is that the entire effect across Q1 and Q2? And if so, can you give us a sense of maybe what was in Q1 or was that just the effect in Q1?

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

A

That was a Q1 effect that we're talking about there.

Brett Hundley
Analyst, Vertical Trading Group LLC

Q

That was a Q1 effect.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

A

And if you think about that, there is just core inflation as it pertains to transportation costs that are in excess of that. But as you try to peel apart and you isolate that which we can attribute more towards the hurricane, that gets us – the hurricanes, that gets us closer to the six figures.

And what's happening is when we have a disaster like this, [indiscernible] (24:40) basically goes and secures all sorts of trucks and drivers, and they pay huge premiums because obviously they're not planned for, and it puts a ripple effect through the entire industry as we all go out, we try to secure transportation.

And often times you would expect, I mean, intuitively you'd say the hurricane is over, why are we [ph] seeing (25:01) the premiums? What happens is often times to load those tractor trailers with all sorts of relief supplies and they remain parked down there for months, if not quarters. So, it takes a while for that sort of capacity to kind of enter back into general distribution and that's why you see a bit of this tail.

Brett Hundley
Analyst, Vertical Trading Group LLC

Q

Okay. That's really clear. Thank you. My last question then I'll [indiscernible] (25:25) floor is just on your balance sheet. Cash continues to build. You guys continue to maintain zero debt. And I really wanted to ask you, Dave or Doug, a two-part question here. So, kind of – number one, kind of goes back to the assortment discussion that we're just having. And I wanted to ask you about the M&A market and perhaps both opportunities small and large that you might be seeing. And how you feel the need to react or position Lancaster Colony against that changing retail/consumer environment that we've been talking about? So, that's kind of the first part that I wanted to get an update on.

And secondly, I wanted to get a sense of how mindful you guys are against public valuation changes and the need to manage return for shareholders, right? So, this has been a tough year for packaged food investors, both on an absolute and a relative basis. And I'm curious how you balance this dynamic alongside the internal, external asset investment dynamic that you have to maintain, of course?

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

A

Well, absolutely. So, why don't I start with the first question about M&A, and what I would tell you there is, I would submit they were as active and probably more active than we've been in any number of years with the number of things in the pipeline, both, I would say small and medium size. So, suffice it to say, very, very active and continuing to look at our range of opportunities. It seems like often times just when you get close, things start to slip away a little bit.

Sometimes, it's driven by value, but sometimes it's just driven by the intrinsic nature of the business and you find things about it that don't necessarily make strategic sense for one reason or another. But what I would assure you is that we're extremely active and committed to the M&A market.

And your second question is, how do we think about leveraging our balance sheet overall, and I think historically what we've said is priority one is M&A, priority two is CapEx against the business, three would be dividend, and then four would be normal, either [ph] repo (27:45) or a special dividend and that general guidance remains true.

As you've seen compression in our valuation, we have started to entertain things like stock buyback and [indiscernible] (27:58) with that I can talk to Doug. As you know, looking at a lot of our peers, most of our peers are leveraging their balance sheet as a means by which to do buybacks and things like that. But with that, I'll turn it over to Doug to help you think about how we frame this internally. Doug?

Douglas A. Fell
Vice President, Chief Financial Officer & Treasurer, Lancaster Colony Corp.

A

And thanks, Dave. And Brett, I think in the past, we've shared with everyone that we tend to be opportunistic with our share repurchases and we will continue that policy as we move forward. We did see during the quarter a little bit of a dip in the price. And we thought that was based on our internal modeling, a price that was opportunistic for us, and so we did take advantage of that. We will continue to monitor that in the future, and the board has authorized [ph] us to (28:46) purchase a fair number of shares. And I think that number is about [ph] 1.4 million (28:51). So, we still have that available to us, looking out into the future.

Brett Hundley
Analyst, Vertical Trading Group LLC

Q

Thank you, both. I appreciate it.

Douglas A. Fell
Vice President, Chief Financial Officer & Treasurer, Lancaster Colony Corp.
A

Absolutely.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.
A

Thanks, Brett.

Operator: Your next question comes from Michael Gallo from C.L. King. Your line is open.

Michael W. Gallo
Analyst, C.L. King & Associates, Inc.
Q

Hi, good morning.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.
A

Hi, Mike.

Douglas A. Fell
Vice President, Chief Financial Officer & Treasurer, Lancaster Colony Corp.
A

Hi, Mike.

Dale N. Ganobsik
Director-Investor Relations, Lancaster Colony Corp.
A

Hi, Mike.

Michael W. Gallo
Analyst, C.L. King & Associates, Inc.
Q

Yeah, just two follow-up questions. First, I was wondering, Dave, if you can give us your view on how you plan to expand your presence within the dips category, as you kind of broaden, how you think about that category in terms of what kind of items you're selling? And then also if you can give us an update on how we should expect the increased capacity at Angelic to start to roll through the numbers and how you should expect us to think about that? Thanks.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.
A

Okay. So, why don't we first – on dips and our thinking about it, and we're really going on two separate tracks. One is an aggressive track on organic innovation and we're readying some pretty exciting items in this space that would help us move into some of the more contemporary dips that are out there. Things like hummus. They are not exactly hummuses but moving in that direction, but very exciting. They would move us out of dairy dips. And those are relatively close, and if things line up, we would expect to be in a position to talk about that in the back half of this upcoming year.

And then of course, we're also looking at M&A and this would be one of the prime spaces where we're looking in M&A. So, whether we can get there through M&A faster or whether we go there organically on our own, we're looking at both tracks.

Your second question is one around Angelic Bakehouse and where do we stand on the build out of the plant. We broke ground. The work is actively underway as Doug mentioned in some of his earlier comments. We expect to be in a position to have that wrapped up by the end of this fiscal year. That would more than double the capacity and give us optionality to increase it yet again with minimal investment, just basically by changing the crewing that's in there.

To that end, what we're also doing is obviously continuing to sell. We have had a couple of new account wins. We've had distribution in Hannaford, [indiscernible] (31:20) and a few other places in the Northeast and we're continuing to work with other retailers.

So really, it's near end. We're focusing on refining the [ph] selling presentation (31:31). We have hired a new sales leader for that business that has deep expertise in that channel. We've engaged a new agency to work with us as recently as yesterday. Actually, we had an innovation summit there with our core team and their team to develop new product ideas. All the while in the backdrop, we're expanding capacity.

Michael W. Gallo
Analyst, C.L. King & Associates, Inc.

Q

Thanks very much.

Douglas A. Fell
Vice President, Chief Financial Officer & Treasurer, Lancaster Colony Corp.

A

Thanks, Mike.

Operator: Your next question comes from Jason Rodgers from Great Lakes Review. Your line is open.

Jason A. Rodgers
Analyst, Great Lakes Review

Q

Yes, good morning.

Douglas A. Fell
Vice President, Chief Financial Officer & Treasurer, Lancaster Colony Corp.

A

Good morning, Jason.

Jason A. Rodgers
Analyst, Great Lakes Review

Q

I wondered if you could talk about the six sigma initiatives, the progress you're making there, and if you could quantify a range of potential savings for the second half there? Thank you.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

A

Sure. Great question. Jason, it's fully operational now, up and running. So, we have our black belts that are actively underway. We've completed our second range of green belts, so if you add those up, we probably have

50 internal resources that we've trained on our own. And we've added five people from the outside. The other thing that we put in place is a means by which to track all of these initiatives and organized in three core buckets. Operation savings that are coming out of our factories. Procurement savings through formula changes, et cetera. And then the last bucket would be savings that are coming through logistics and we're getting yield from all three of those areas.

We're expecting to see in all of the planning that we have in place is that it's just going to continue to grow sequentially as we continue to progress through the year. In the most recent period, it was a sort of a low-mid seven figure number, is what we're looking at now, sort of low-mid seven figure number and that's just going to continue to pick up pace as these projects come on line.

Jason A. Rodgers
Analyst, Great Lakes Review

Q

That low seven figure number, that's the estimate for the second half, is that right or is that the full year?

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

A

No, that was just in our first quarter.

Jason A. Rodgers
Analyst, Great Lakes Review

Q

Okay. Great.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

A

And so that was in our first quarter. So if you think about it from a standstill, we really – we started – if I kind of run back sequentially, we actually engaged Ohio State University to help us develop a curriculum for greenbelt training and we hired our greenbelts in what would have been last year's, let's call it, the third quarter. And we started to set up initiatives and means by which to track those initiatives in our fourth quarter. And if you look at that first quarter benefit, so this is early days. These are projects that are just getting going, that's in the, let's call it, the low mid-seven figure range and as you might – and that's just the impact in the first quarter and then the impact of that will just continue to build as sequentially we go through other quarters.

Jason A. Rodgers
Analyst, Great Lakes Review

Q

Sounds good. Also, you mentioned the IRI data picking up share in three categories. What were those categories?

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

A

Sure. Let me get those for you. They were produced dressings and garlic bread and frozen dinner rolls.

Jason A. Rodgers
Analyst, Great Lakes Review

Q

A few other number questions. Do you have the organic growth for the company in total in the quarter?

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.
A

Let's see, it was 6.2%, back out Angelic. It's 4.2% between the two, I would assume.

Douglas A. Fell
Vice President, Chief Financial Officer & Treasurer, Lancaster Colony Corp.
A

On the Retail side, that is correct.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.
A

And then if you...

Douglas A. Fell
Vice President, Chief Financial Officer & Treasurer, Lancaster Colony Corp.
A

And then if you total that all up, it was largely all driven by volume. If you look at it in that way, Jason. And so, you're looking at the overall [ph] about (35:36) 2.6%, think about it in terms of almost all of that same volume growth.

Jason A. Rodgers
Analyst, Great Lakes Review
Q

All right.

[indiscernible] (35:48)

Jason A. Rodgers
Analyst, Great Lakes Review
Q

Sorry. Go ahead.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.
A

I was going to say, I will just try to do some quick computing in my mind. If you wanted to back out Angelic out of the Retail, Foodservice mix, if those two – Doug, correct my math. If we were 2.6% overall, you back out Angelic and you say Angelic was 1.1%, It's like a 1.5% of organic growth.

Douglas A. Fell
Vice President, Chief Financial Officer & Treasurer, Lancaster Colony Corp.
A

That's right.

Jason A. Rodgers
Analyst, Great Lakes Review
Q

Yeah, helpful. And then finally, the Angelic Bakehouse, the charges outside of the amortization expenses, is that anything material in the quarter?

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.
A

Yeah, I would say, it's the $800,000 that we described. Part of it's amortization and part of it's an earn-out that we have in place for the sellers. Both are noncash charges and we'll begin to lap those as we go past the third quarter.

Jason A. Rodgers
Analyst, Great Lakes Review

Q

All right. Thank you very much.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

A

In fact, we made a good deal in the second quarter. So, $800,000 is a number that we were talking about.

Jason A. Rodgers
Analyst, Great Lakes Review

Q

Thank you.

Operator: As there are no further questions, we will now turn the call back to Mr. Ciesinski for his closing remarks.

David A. Ciesinski
President and Chief Executive Officer, Lancaster Colony Corp.

Thank you for joining us all today and we look forward to talking with you later this winter, as we review our second quarter results.