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The Marzetti Company

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Earnings Call

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Call Participants

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Scott Michael Marks

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Presentation

Operator

Good morning. My name is Kathy, and I will be your conference call facilitator today. At this time, I would like to welcome everyone to The Marzetti Company's Fiscal Year 2026 First Quarter Conference Call. Conducting today's call will be Dave Ciesinski, President and CEO; and Tom Pigott, CFO. [Operator Instructions] Thank you.

And now to begin the conference call, here is Dale Ganobsik, Vice President of Corporate Finance and Investor Relations for The Marzetti Company. Please go ahead.

Dale N. Ganobsik

Vice President of Corporate Finance, Investor Relations & Treasurer

Good morning, everyone, and thank you for joining us today for The Marzetti Company's Fiscal Year 2026 First Quarter Conference Call. 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 an audio replay of this call will be available on our website investors.marzetticompany.com later today. For today's call, Dave Ciesinski, our President and CEO, will begin with the business update and highlights for the quarter. Tom Pigott, our CFO, will then provide an overview of the financial results. Dave will then share some comments regarding our current strategy and outlook. At the conclusion of our prepared remarks, we'll be happy to answer any of your questions. Once again, we appreciate your participation this morning.

I'll now turn the call over to Marzetti Company's President and CEO, Dave Ciesinski. Dave?

David A. Ciesinski

President, CEO & Director

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 2026.

In our fiscal first quarter, which ended September 30, consolidated net sales increased 5.8% to a record \$493 million. Excluding noncore sales attributed to a temporary supply agreement, or TSA, adjusted net sales increased 3.5% to \$483 million. I am also happy to report that we achieved first quarter records for gross profit, which reached \$119 million and operating income, which grew to \$59 million.

In our Retail segment, net sales increased 3.5%. This was led by our category-leading New York Bakery frozen garlic bread products, including notable contributions from the delicious gluten-free Texas Toast that we launched last fall. Volume gains for our successful licensing program also contributed to the increase in Retail segment sales, driven by Chick-fil-A sauces, Buffalo Wild Wings sauces and Olive Garden dressings.

Circana scanner data for the quarter ending September 30 showed strong performance for several of our core brands and licensed items. In the Frozen Dinner Roll category, our own Sister Schubert's brand in our licensed Texas Roadhouse brand combined to grow 27.4%, resulting in a market share increase of 650 basis points to a category-leading 66.5%.

In the Frozen Garlic Bread category, our New York Bakery brand grew sales 8.6%, adding 350 basis points of market share for a category-leading share of 44.1%.

In the Produce dips category, sales of Marzetti brand increased 4.1%, adding 220 basis points of market share for a category-leading 82.1%.

In the Shelf Stable Sauces & Condiments category, sales of Chick-fil-A sauces grew 9.6%, well ahead of the category, 0.2% growth rate, resulting in 17 basis points of share growth. Chick-fil-A sales benefited from both expanded distribution into the club channel that began during our fiscal fourth quarter and increased sales of the iconic sauces with traditional retailers.

In the Foodservice segment, excluding the noncore TSA sales, adjusted net sales grew 3.5%, while volume measured in pound shifts increased 0.5%. In addition to the benefit of inflationary pricing, the increase in Foodservice segment sales reflects increased demand from several of our core national account customers. During the period, we are pleased to report a 7.2% increase in gross profit to a first quarter record of \$119 million. Our focus on supply chain productivity, value engineering and revenue management, all remain core elements to further improve our margins and financial performance.

I'll now turn the call over to Tom Pigott, our CFO, for his commentary on our first quarter results. Tom?

Thomas K. Pigott

VP, Assistant Secretary & CFO

Thank you, Dave. Overall, the company delivered against this growth algorithm. Both the top line and gross margin performance improved and investments were made to continue to drive growth. First quarter consolidated net sales increased by 5.8% to \$493.5 million. Breaking down the revenue performance, higher core volume and product mix drove a 210 basis point increase. Net pricing was accretive by 140 basis points.

In addition, the company reported \$10.7 million or 230 basis points of growth that resulted from a temporary supply agreement with Winland Foods, the seller of the Atlanta-based manufacturing facility that we acquired in mid-February. We entered into this agreement to facilitate the closing of the transaction. It's important to note that these temporary and noncore sales are expected to conclude during the quarter ended March 31, 2026.

Consolidated gross profit increased by \$8 million or 7.2% versus the prior year quarter to \$118.8 million and reported gross margin expanded by 30 basis points. The gross profit growth was driven by our ongoing cost savings programs and volume growth. Note that excluding the \$10.7 million in sales from the temporary supply agreement, which did not contribute meaningfully to gross profit, adjusted gross margin expanded by 80 basis points.

Selling, general and administrative expenses grew \$3.5 million or 6.3%. The increase reflects a higher marketing spend as we invested to support the continued growth of our Retail brands, higher brokerage expenses as well as increased compensation and benefits.

During the quarter, the company recorded \$1.1 million in restructuring and impairment charges. The charges are attributed to the planned closure of our sauce and dressing facility in Milpitas, California that we previously announced. This closure was part of our ongoing initiative to optimize our manufacturing network. Production at that facility has concluded and the property is currently being marketed for sale.

Consolidated reported operating income increased \$3.4 million, driven by the strong gross profit performance, partially offset by the higher SG&A expenses and the restructuring and impairment costs. Excluding the restructuring and impairment charges, adjusted operating income grew by 8.1%.

Our tax rate for the quarter was 22.4% versus 22.8% in the prior year quarter. We estimate our tax rate for fiscal '26 to be 23%. First quarter diluted earnings per share increased \$0.09 or 5.6% to \$1.71. The restructuring impairment charges I mentioned reduced diluted earnings per share by \$0.03 in the current year quarter.

With regard to capital expenditures, our payments for property additions totaled \$15.6 million for the quarter. For fiscal '26, we are forecasting total capital expenditures of between \$75 million and \$85 million. We will continue to invest in both cost savings projects and other manufacturing improvements as well as the newly acquired Atlanta facility.

In addition to investing in our business, we also returned funds to shareholders. Our quarterly cash dividend of \$0.95 per share paid on September 30 represented a 6% increase from the prior year's amount. Our enduring streak of annual dividend increases stands at 62 years. Our financial position remains strong with a debt-free balance sheet and over \$182 million in cash. During the quarter, the company generated \$69.5 million in operating cash flow, an increase of \$49.6 million versus the prior year quarter.

To wrap up my commentary, our first quarter results demonstrate strong execution across a number of areas that drove top line and bottom line growth in a difficult operating environment. In addition, we continued to make investments to support further growth and cost savings.

I will now turn it back over to Dave for his closing remarks. Thank you.

David A. Ciesinski

President, CEO & Director

Thanks, Tom. Suffice it to say, it's a dynamic and some might add challenging time in the food industry, tariffs, stubborn inflation, GLPs, MAHA and consumers under financial pressure often make it difficult to generate organic growth. Against this backdrop, I couldn't be more proud of our team at Marzetti, which continues to leverage our portfolio of trusted brands and our industry-leading innovation capabilities to make great-tasting, consumer-relevant products and deliver sustainable growth for our shareholders.

As we look ahead, The Marzetti company will continue to leverage the combined strength of our team, our operating strategy and our balance sheet in support of the 3 simple pillars of our growth plan, to: one, accelerate core business growth; two, to simplify our supply chain to reduce our cost and grow our margins; and three, to expand our core with focused M&A and strategic licensing.

Looking ahead to our fiscal second quarter and the remainder of our fiscal year, we anticipate Retail segment sales will continue to benefit from growth from our licensing program, including expanding distribution for the popular Texas Roadhouse Dinner Rolls and contributions from our own brands.

In the Foodservice segment, we expect to benefit from sales to select quick service restaurant customers in our mix of large national accounts. Like many of you, we continue to monitor external factors, including U.S. economic performance and consumer behavior that may impact the demand for our products.

With respect to input costs, in the aggregate, we anticipate a modest level of cost inflation in the quarters ahead that we plan to offset through contractual pricing and our cost savings programs as we remain focused on continued margin improvement.

In closing, I would like to thank the entire Marzetti Company team for all their hard work this past quarter and their ongoing commitment to grow our business. This concludes our prepared remarks for today, and we'd be happy to answer any questions that you may have. Operator?

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Alton Stump from Loop Capital.

Alton Kemp Stump

Loop Capital Markets LLC, Research Division

Great. Congrats on the quarter. Obviously, it was great to see volume growth exceed expectations in both of your segments during the quarter. I guess I want to ask you about the inflationary front on your Foodservice business specifically. Could you remind us sort of how the pass-through mechanism works in a segment. It's obviously different versus Retail operations. Just how much of a lag there is, if anything, when you're passing through what appears to be an inflating environment on the Foodservice side?

David A. Ciesinski

President, CEO & Director

Yes, Alton, I'd be happy to answer the question. So as you recall, 75% of our business or so is tied to large national accounts. And every one of those customers have an agreement whereby on a quarterly basis, we sit down and we mark-to-market on their key ingredients. So usually, what we'll see happen is if, let's say, in said quarter, we start to see one of our commodities inflate, we'll sit down with them and we'll document that. And that's passed along right into the price of the product.

And it's true as we inflate and it's also true as we deflate. In the current environment, what we're seeing, Alton, is that we're seeing things like soybean oil back off a little bit. We're seeing eggs back off a little bit. Shelled eggs are moving up, but the eggs that we buy, which are yolks and whole eggs are backing off of some of their historical highs. So what we continue to see in this environment is modest inflation that we feel more than comfortable that we can cover by way of pricing and then value engineering work that we have.

Alton Kemp Stump

Loop Capital Markets LLC, Research Division

That's great, Dave. And then I guess just one follow-up and I'll hop back in the queue. But just on a quick reference to Chick-fil-A sell-through data, being up almost 10%, I mean, obviously, this has been a huge home run for you guys when it first came out some years ago, but that I think is one of the bigger growth numbers that we've seen from Chick-fil-A over the last 2 quarters, as you obviously are up against, of course, tougher and tougher comparisons each year. And of course, you referenced the increased club channel distribution. Was that really the key driver of that? Or was there any sort of core underlying strength that you saw to drive that almost 10% sell-through number?

David A. Ciesinski

President, CEO & Director

Yes. Great question. A lot of that was expanded distribution into club. And we did see some growth also in our core Retail business as well. And I think it's worth stepping back, it was in April of 2019 that we flew to Chick-fil-A and we met with that great partner. We talked about the idea of taking the product into Retail, and they very excitingly got behind it. And we did all the work necessary to bring in into the market. So here we are 5 years on.

And if you combine the Retail sales of both the sauce and the dressings, we're talking a \$200 million, \$220 million in Retail sales business. So with a lot more that we both believe, we being The Marzetti team and Chick-fil-A that we can do with this great brand platform. So we're very excited.

I think the other notable thing with club is that it's allowing us to further improve our household penetration and reach more customers. So we believe that channel is going to be an important long-term way for us to reach consumers in addition to mass and retail.

Operator

Your next question comes from the line of Jim Salera with Stephens.

James Ronald Salera

Stephens Inc., Research Division

I wanted to drill down a little bit more on Foodservice. Given the strong results there, even when we strip out the TSA, particularly given what a lot of restaurant companies are reporting right now. Can you just walk us through where the outperformance there came from, again, as kind of restaurant commentary across the industry is pretty downbeat. Is it the type of products that you're supplying to your restaurant partners are kind of more in demand? Is it the brands that you're servicing? Just any color you can provide there would be helpful.

David A. Ciesinski

President, CEO & Director

No, I'd be happy to. So I think you understand as well as anybody else that the core of our Foodservice business, our large national accounts. If you look at the most recent period, 5 of our 7 largest national accounts were actually growing sales and traffic in the period, led -- in that group led by Chick-fil-A, which is doing an amazing job with pretzel club sandwich that they launched that LTO, which we were more than happy to provide the sauce for. Domino's is another very important strategic customer for us, and they've been growing in this period. Taco Bell grew in the period and then others did as well.

So I think part of what's happening here, Jim, if you kind of ladder back and you look at the challenging backdrop, I would point to 2 things. One is we are blessed enough to be able to win with the winners. The people that have a value proposition in this environment that consumers continue to find relevant and they're willing to spend their hard-earned money against. The second is we're playing in categories that are relevant for these customers. They're all looking for ways to differentiate themselves and cut through this noisy backdrop and screen flavor. And that really is our wheelhouse. So that's how we feel like we've been able to do it in the quarter. It helped us offset a bit of a gap that we had that we've been talking to you guys about with some discontinued items.

And it sets up, I think, for us to continue to be able to grow and it highlights part of the durability of our overall business strategy, which is flavor, flavor, flavor on consumer-relevant forms that our customers in Foodservice continue to see as important and their consumers, the end-using consumers ultimately enjoy eating.

James Ronald Salera

Stephens Inc., Research Division

Great. And Dave, if I remember correctly, when you talked in fourth quarter, the expectations for Foodservice for full year '26 were kind of flattish. Any update to that outlook given the outperformance in 1Q and then some of the dynamics you just referred to?

David A. Ciesinski

President, CEO & Director

Yes. If you remember, we were a bit cautious about the volume outlook because we had a couple of big customers that discontinued items. And we thought we were going to get flattish on sales by way of a little soft volume and a little bit of inflationary pricing that got us there. And I think if anything, what we're seeing in this environment is that the Foodservice outlook has improved modestly based on what we're seeing.

Operator

Your next question comes from the line of Scott Marks with Jefferies.

Scott Michael Marks

Jefferies LLC, Research Division

I wanted to ask on the profitability side. You made some comments in the prepared remarks about some increased marketing spend. Just trying to gauge how much that impacted the Retail segment. I think profit for that segment came in a little light of what folks were looking for. And I know you've been playing a little bit with some of the marketing, some of the promotional spend. So just wondering if you can share an update on that and how we should be thinking about that.

Thomas K. Pigott

VP, Assistant Secretary & CFO

Sure. So overall, when you look at Retail profitability, it was down in the quarter as you highlighted. Three main drivers to that. First, as eggs prices have gone up considerably, we price for that. But we've priced for the longer-term outlook. So right now, in this particular quarter, PNOC was negative for Retail and that impacted the margin profile this quarter.

The second thing on the margin aspect of Retail is we've done a lot of efforts on the network to close the Milpitas facility to activate the College Park. A lot of those savings are flowing more to the Foodservice P&L. So over time, we'll begin to get more productivity savings on Retail. But right now, as you look at the Foodservice profitability, it's getting the main benefit.

Now getting to your -- the core of your question, the investments in marketing, we see an opportunity to continue to elevate our marketing in Retail. We're below a lot of the peers in what we've spent. And we're getting great response in terms of the programs we're putting in place with the marketing team. So we're going to continue to invest in that space.

When you look at the SG&A in Retail, the majority of that increase was that marketing spend. We also had slightly higher brokerage costs relative to the higher volume performance for the segment. So overall, we feel good about the investments we're making into the Retail segment and the overall profitability outlook.

Scott Michael Marks

Jefferies LLC, Research Division

Appreciate the color there. A follow-up question would be, there's been a lot of commentary from some of your peers recently around a softer U.S. consumer. Obviously, your business seems to be bucking the trend a little bit, have some benefits from some of the distribution initiatives. But just wondering if you can kind of help us understand how you're seeing the consumer today? And how are you feeling about kind of the core underlying business relative to some of those distribution wins that you noted?

David A. Ciesinski

President, CEO & Director

Yes. No, Scott, we're seeing the same thing that everybody else is. We're looking at a consumer that's under pressure. All that being said, the consumers are still eating and flavor still matters. And I think what we're choosing to do is really leverage our innovation capabilities and bring to the market products that they're finding relevant. Maybe I could kick off a couple.

I would, on the Retail side, point to New York Bakery, which is in a bit of a sleepy category, right, garlic toast. If you look at it sequentially, we've been growing that business quarter after quarter, at least to 44.1% share in the most recent period. That's behind our own toast. It's behind the new gluten-free item which has increased in velocity and a value pack of bread sticks that we have. So great item even in this economy that consumers are finding relevant -- as it pertains to our roll business here, again, I think we were up about 650 basis points, if I recall, or thereabouts in overall market share.

We're growing our share. We're also growing the category considerably. Our own Sister Schubert's brand was roughly flat, and the real growth there is coming from the Texas Roadhouse roll, which is terrific. We love to repeat on that item, great tasting roll, affordable price point, where consumers can treat themselves.

If you move around and you look at our Marzetti brand, we've had a great season so far in our dips and caramel dip. And I think all of these are just affordable luxuries that even against a challenging backdrop, consumers can afford. So is it challenging? Yes. Do we see pathways to leverage innovation and good

execution to continue to grow? Yes. Would we like the growth to be even faster? Absolutely. But -- and we're going to continue to press for it. But we continue to see against all of our different owned brands and licensed brands, the ability to, even against this backdrop, grow because flavor matters and we believe that our innovation capabilities around flavor is among, if not the best in the industry.

Operator

If there are no further questions, we'll now turn the call back to Mr. Ciesinski for his concluding comments.

David A. Ciesinski

President, CEO & Director

Well, thanks, everybody. It's been a short call, but a good call. We enjoyed sharing our results with you. We look forward to seeing all of you guys on the road during the course of the next quarter and look forward to getting together when we announce our next earnings in February. Have a great rest of the day.

Operator

Thank you, and thank you for your participation. This does conclude the program. You may now disconnect.

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