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PRESENTATION

Operator

Good day, and thank you for standing by, and welcome to the Sprouts Farmers Market Fourth Quarter 2023 Earnings Conference Call. (Operator Instructions). Please be advised that today's conference is being recorded.

I would now like to hand the conference over to your speaker today, Susannah Livingston, Vice President, Investor Relations and Treasurer. You may begin.

Susannah Livingston - *Sprouts Farmers Market, Inc. - VP of IR & Treasury*

Thank you, and good afternoon, everyone. We are pleased you are joining Sprouts on our fourth quarter and full year 2023 earnings call. Jack Sinclair, Chief Executive Officer; and Curtis Valentine, Chief Financial Officer, are with me today.

The earnings release announcing our fourth quarter and full year 2023 results, the webcast of this call and financial slides can be accessed through the Investor Relations section of our website at investors.sprouts.com.

During this call, management may make certain forward-looking statements, including statements regarding our expectations for 2024 and beyond. These statements involve several risks and uncertainties that could cause results to differ materially from those described in the forward-looking statements.

For more information, please refer to the risk factors discussed in our SEC filings and the commentary on forward-looking statements at the end of our earnings release. Our remarks today include references to non-GAAP measures. Please see the tables in our earnings release to reconcile our non-GAAP measures to the comparable GAAP figures.

With that, let me hand it over to Jack.

Jack L. Sinclair - *Sprouts Farmers Market, Inc. - CEO & Director*

Thanks, Susannah, and good afternoon. As we review our year-end accomplishments, I'm once again pleased with our performance and encouraged about our future. We grew sales 7% for the year while maintaining our stable margin with a slight expansion in 2023.

Moreover, our adjusted diluted earnings per share rose 19%, demonstrating attractive profit growth. Our strategic approach and specialty positioning allow us to focus on a highly profitable slice of the \$1.6 trillion food-at-home space instead of competing with everyone for every customer. And we believe these results clearly indicate that this strategic shift is resonating with our target customers.

We are becoming a leading specialty food retailer. We continue to focus on our target customers, striving to deliver more of what they want, a broad assortment of differentiated, healthy, fresh, high-quality products that are hard to find anywhere else. Approximately 15% of our assortment was new, including 400 new Sprouts brand products. We ended the year with the company's best customer service scores by focusing on the customer experience through better service and improving our in-stocks.

As part of expanding access to our differentiated assortment, we opened 30 new stores in our new smaller prototype, and we experienced good momentum, especially so in Florida. We created capacity in the supply chain to support our long-term growth by establishing a new distribution center in Southern California, expanding our Texas DC and adding ripening rooms to improve product quality. None of this will be possible without our amazing team.

In 2023, we continued fostering a workplace culture that we believe will maintain a sustainable and profitable business for years to come. We enhanced our development programs for team members so that everyone can grow a great career at Sprouts. We created approximately 3,000 new jobs and promoted 20% of our 32,000 team members in 2023.

I'm also pleased to announce another internal promotion to our executive leadership team. Dustin Hamilton has replaced Dan Sanders as our Chief Stores Officer. Dustin had been serving as our original VP of California, delivering great results and building a team steeped in our values. Dan has decided to retire in March after 8 years at Sprouts and many more years in the industry. I want to thank Dan for his lasting impact on Sprouts.

In summary, our achievements in 2023 have positioned us well for the future, and we will continue working to unlock Sprouts full potential. I'll talk more about our journey in 2024 in a few moments.

For now I'll hand it over to Curtis to review our 2023 financial performance in the fourth quarter, the full year and our 2024 outlook. Curtis?

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

Thanks, Jack, and good afternoon, everyone. For the fourth quarter, total sales were \$1.7 billion, up \$122 million or 8% from the same period last year. This increase was driven by comparable store sales growth of 3.3% and the addition of new stores. Traffic was positive both in store and online throughout the quarter. As expected, average unit retails and units per basket continued to stabilize sequentially.

Our e-commerce sales grew approximately 17%, representing 12.4% of our total sales for the quarter. During the quarter, we also launched our partnership with Uber Eats to acquire new customers and expand their access to Sprouts. Along with Instacart and DoorDash, we now have 3 e-commerce partnerships performing well, highlighting the appeal of our differentiated assortment.

We continue to see strong performance in categories with the most differentiation, including grocery, dairy, frozen and meat. Sprouts has experienced exceptional growth in attribute-driven categories within these departments such as grass-fed beef and no-antibiotics-ever proteins. These categories have gained popularity due to their superior quality and health benefits, making them a top choice for our customers who prioritize healthy eating. This was true during the holidays with strong growth from the return of Sprouts brand seasonal favorites and our convenient attribute-based holiday meal bundles.

Sprouts brand made up 21% of our total sales in the fourth quarter as our unique products continue to appeal to our target customers. Our fourth quarter gross margin was 36.5%, an increase of nearly 20 basis points from the same period last year. Favorable merchandise margins were partially offset by the expected pressure from our new and recently expanded distribution centers.

SG&A for the quarter totaled \$513 million, an increase of \$41 million or approximately 25 basis points of deleverage from the same period of the prior year. We continue to see pressure from wages and benefits. This was partially offset by a positive impact from holiday pay with the New Year's Day shifting into fiscal 2024.

Store closure and other costs totaled approximately \$5 million for the quarter. This is primarily related to noncash store asset impairments and ongoing occupancy costs from store closures.

For the quarter, our earnings before interest and taxes were \$69 million. Interest expense was \$400,000 and our effective tax rate was 27%. Net income was \$50 million and diluted earnings per share were \$0.49, an increase of 17% from the same period last year.

For the fiscal year 2023, total sales increased 7% to \$6.8 billion driven by comparable store sales growth of 3.4% and new stores. Comp sales for the full year were also supported by an increase in basket due to retail inflation and positive traffic, partially offset by a slight reduction of items in the basket.

Our e-commerce sales grew 15%, which accounted for 12.2% of our total sales for the year. Our focus on innovation and assortment differentiation continues to resonate with our target customers and drive our sales. Attribute-driven products such as organic, grass-fed, vegan and keto, grew faster than the company average throughout the year.

Gross margin, both on a GAAP basis and adjusted to exclude the impact of special items, was 36.9%, an increase of approximately 25 basis points compared to adjusted gross margin in the prior year. The year-over-year increase resulted from continued promotion optimization and category mix shifts, slightly offset by pressure from higher distribution costs from our new and recently expanded warehouses.

SG&A expenses for the year, both on a GAAP basis and adjusted to exclude the impact of special items, totaled \$2 billion, an increase of \$136 million or approximately 15 basis points of deleverage on an adjusted basis. The increase in cost is mainly attributable to the opening of new stores, and increased investments in team member wages, restructured store bonuses and training.

In addition, we experienced higher e-commerce and credit card fees linked to higher sales. Labor efficiencies and contract savings partially offset this as the team continued to find ways to manage costs despite the challenging inflationary environment.

For fiscal year 2023, store closures and other costs totaled \$39 million, primarily related to the charges associated with the decision to close 11 stores earlier in the year. Excluding the impact of special items, store closures and other costs were \$11 million.

Depreciation and amortization, excluding depreciation included in the cost of sales was \$132 million. Excluding the impact of special items associated with the store closing decision, the adjusted depreciation and amortization totaled \$126 million.

For the year, our earnings before interest and taxes were \$350 million. Interest expense was \$6.5 million. Our effective tax rate was 25%. Net income was \$259 million and diluted earnings per share were \$2.50. Excluding the impact of special items, adjusted earnings before interest and taxes were \$396 million, and adjusted net income was \$293 million. Adjusted diluted earnings per share were \$2.84, an increase of 19% compared to the prior year.

During the year, we opened 30 new stores, acquired 2 previously licensed stores and closed 11 stores. All 30, 2023 openings were our new smaller format store. We ended the year with 407 stores across 23 states.

Our financial performance has been underpinned by a strong and healthy balance sheet. We generated \$465 million in operating cash flow, which allowed us to invest \$213 million in capital expenditures, net of landlord reimbursement to grow our business. With our robust cash flow, we also paid down \$125 million of our bank revolver and returned \$203 million to our owners by repurchasing 5.9 million shares.

We ended the year with \$202 million in cash and cash equivalents, \$125 million outstanding on our \$700 million revolver and \$22 million of outstanding letters of credit. Our diluted weighted average shares outstanding were down 5.3% compared to the last year, and we have \$208 million remaining under our current share repurchase authorization.

Since 2019, we have made significant improvements to our business operations. We changed our strategy, streamlined our store labor model and implemented key systems to support our growth. We also increased compensation and added training hours for our store team members, a critical investment to create the differentiated store experience our target customers love. As a result, our gross margins have improved by 300 basis points and our adjusted EBIT margins improved by approximately 190 basis points.

Our 4-year adjusted diluted earnings per share CAGR was 23%, and our adjusted EBIT per square foot increased by 59%. Our ROIC has also improved by 320 basis points, All in line with our strategic targets.

While we're pleased with our progress, significant opportunities remain. As we look ahead to our expectations for 2024, we remain focused on delivering earnings growth while investing to unlock our opportunities and drive sustainable growth for years to come. We are planning to invest approximately \$15 million, primarily focused on the build-out of our loyalty program. We also continue to invest in our technology and data foundation to improve our inventory management and scale our personalization capabilities.

For the full year, we expect total sales growth to be 5.5% to 7.5% and comp sales in the range of 1.5% to 3.5%. We plan to open approximately 35 new stores all in our current prototype. Adjusted earnings before interest and taxes are expected to be between \$397 million and \$412 million. And adjusted earnings per share are expected to be between \$2.85 and \$2.95 assuming no additional share repurchases. That said, we do expect to continue to repurchase shares opportunistically. We also expect our corporate tax rate to be approximately 26%.

During the year, we expect capital expenditures net of landlord reimbursements to be between \$225 million and \$245 million. To add a bit more color, we expect gross margins to be up and as we continue to focus on initiatives to improve shrink and annualize the promotional optimization work from 2023.

On the cost front, we expect ongoing wage increases and our strategic investments to pressure SG&A resulting in additional deleverage in 2024. Most of our CapEx spend will be for new stores with the remainder focused on technology enhancements, merchandising initiatives and store refresh and maintenance.

For the first quarter of the year, we expect comp sales in the range of approximately 2.5% to 3.5% and adjusted earnings per share between \$0.98 and \$1.02. Our SG&A will face additional pressure in quarter 1 due to strategic initiative investment and the timing shift of holiday pay for New Year's Day, which fell on the first day of fiscal 2024.

And with that, I'll turn it back to Jack.

Jack L. Sinclair - *Sprouts Farmers Market, Inc. - CEO & Director*

Thanks, Curtis. Our initiatives for 2024 will continue to strengthen our foundation while setting the table for sustainable long-term growth. This year, we plan to drive even more innovation in Sprouts brand and across the store, win more loyalty from our target customers, strengthen and improve our advantaged supply chain, develop a best-in-class team across the business and build exceptional stores.

Our intent is to become a leading provider in attribute, health-driven categories, such as organic, vegan, grass-fed and keto, prioritizing winning and gaining market share in these differentiated categories. To achieve this, our forging team is searching far and wide for new health trends and working with niche vendors to find differentiated products such as low caffeine InoTea, Popadelics, a snackable mushroom chip and Matcha bubble tea drops.

Looking ahead, we will continue launching new Sprouts brand products, expand our seasonal in and out programs, leverage our innovation centers in store and engaging more sampling to drive trial and basket. This focuses on our Sprouts brand continuing to deliver growth ahead of company performance and provide customers with products they value and trust.

In 2024, we have an opportunity to gain new health enthusiasts and increase our share of wallet among existing customers. We'll continue to prioritize store execution to provide great in-store experience and exceptional customer service while maintaining an omnichannel approach to meet customers wherever they are.

I'm particularly excited about our plans to introduce the first iteration of our new loyalty program this summer. We see a big opportunity to grow share of wallet with our target customers by getting them to visit more often and add additional items to their basket. The program is designed to grow our identifiable customer base and gather valuable data on their preferences, enabling us to personalize the experience to their specific needs.

We're also optimistic about how the data will potentially unlock value across our business by deepening our insights on customers, aiding Sprouts brands product development, improving customer acquisition and providing a new asset to utilize with our vendors to grow our mutual business.

We are investing to develop a long-term value driver for Sprouts. 2024 will be dedicated to testing the concept, listening to our customers' feedback and establishing a program ready for full launch in 2025.

We've made significant progress in creating an advantaged supply chain to support our future growth. In 2024, we will improve our in-stocks by adding PICA0 to our deli, meat and bakery departments. We will also enhance our supply chain data and technology foundation. Over the last years, we've improved our systems for production planning, computer-assisted ordering and produce replenishment. There's now an opportunity to connect the data and processes that rely on these systems to improve our overall forecasting and ordering. This will enable a more disciplined inventory management process, allowing us to further leverage our supply chain in the future.

Our team is the most important part of our business, and we have concentrated on building a best-in-class workplace, culture and values over the past few years. While it is always ongoing process, we have made significant improvements. As a result, our team member retention rate improved by more than 20% in 2023, which has led to improved store performance and supports our continued store growth. To provide more opportunities to our team while driving for results, we restructured our store bonus plan, prioritizing customer service, being in stock and faster growth.

This year, our main focus is to develop our leaders for growth. We will improve our training, focus on talent development and create clear career paths for leaders at all levels. This is critical for achieving our growth aspirations. We have blended fresh perspectives and external expertise with internal promotions at the Executive VP and Director levels to create a deep bench to support our growth. Our team is coming together to execute our strategic priorities and support our stores and customers.

Lastly, we will accelerate unit growth again in 2024. In the first quarter of this year, we have already opened 4 new stores and plan to open approximately 35 total for the year. We have a robust pipeline of over 100 approved stores and nearly 70 executed leases. And we intend -- continue to improve our site selection process to maintain a strong pipeline moving forward.

In closing, our main focus is executing our strategy to establish Sprouts as an exceptional specialty retailer with a differentiated better-for-you offering. Our results demonstrate that our strategic initiatives are paying off, and I'm confident these principles will guide us through another successful year. Our collected efforts are resonating well with our customers and our team is ready to face the many opportunities ahead. I'm excited to share our progress as the year unfolds.

And with that, I'd like to turn it over for questions. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question comes from John Heinbockel from Guggenheim Partners.

John Edward Heinbockel - *Guggenheim Securities, LLC, Research Division - MD & Equity Research Analyst*

So Jack, I wanted to start with -- you're adding assortment. At the same time, right, you're cutting square footage. So maybe talk about the foraging process and the planogramming process and sort of managing that in terms of taking out items that are not moving. And is there any -- I don't think you're going to more vertical with your space. So is it kind of one in, one out? Or how are you dealing with that?

Jack L. Sinclair - *Sprouts Farmers Market, Inc. - CEO & Director*

Yes, it's a great question. It's right to the heart of how we think about our business. When we reduced the square footage from 32,000 down to 23,000, we were very focused on losing not selling space, but actually cutting back on noncustomer-facing space, which allowed us to retain the SKU count that we had, apart from in our vitamins and [arbor] department, which we took a few out in that department.

Going forward with the foraging team, we introduced an innovation center in our stores, which is allowing us to move really fast with items that the foraging team are finding. And we put it into the stores into the innovation center. So that's extra skews to what we would have had without the innovation center. What that then does gives us a couple of months to see whether the products sell, how the customers react to that [section]. I've been delighted the way the customers have interfaced with that. It's creating this treasure hunt of new items coming into the store, customers looking at the items, checking and really being -- curating their own assortment from that and the discernment of our customers in that space is something that I think we're -- what we're doing there is appealing to us.

So in terms of the planograms, as those sales happen or don't happen on the innovation center, the ones that are selling really well automatically flow into the original planograms, other products fall by the wayside. But effectively, we're kind of -- we've got a little bit of an increased SKU count because of the innovation center as they get put in and come out the overall number. There are products coming out so that we can fit them into the planogram within the base fixture.

But -- that's -- so that's kind of part of how we've been operating this. And our business is all about broad assortment. It's really important that we don't compromise that assortment going forward. And so we're always kind of trying to get more into the stores, to be honest with you rather than less.

John Edward Heinbockel - *Guggenheim Securities, LLC, Research Division - MD & Equity Research Analyst*

Yes. No, that was great. And one quick one on the loyalty program. So the \$15 million, I assume that's an operating -- an OpEx item as opposed to capital. Is there a cost beyond '24 that kind of correlates to the \$15 million? And then I assume for the business case, you thought about what the top line uplift would be? You're probably not going to tell us, but I don't know if you can size it to get you comfortable with the ROI?

Jack L. Sinclair - *Sprouts Farmers Market, Inc. - CEO & Director*

So the way we -- the \$15 million isn't all about loyalty. There's some other things within that. But all of that is about investing in the business for the future, some infrastructure issues, some fundamental issues and investment in IT and the loyalty program that we're working on. We're very

excited about it. The benefits for that will flow through in 2025. We clearly do have the numbers around the benefits of that. And as you'd say, we're probably not going to share that with you today.

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

And John, it is all -- the \$15 million is OpEx. And as always as we go forward -- yes, we'll manage it and plan into it as we go forward.

Operator

And our next question comes from Mark Carden from UBS.

Mark David Carden - *UBS Investment Bank, Research Division - Associate Director and Associate Analyst*

So to start, you guys have now outgrown the broader census category for several consecutive quarters. At this stage, are you still seeing much pressure from mainstream players adding to the natural organic offerings? Has that largely played out at this point? And then what else jumps out at you with respect to your ability to really buck the trend and grow sales faster than the overall channel?

Jack L. Sinclair - *Sprouts Farmers Market, Inc. - CEO & Director*

Well, I think we've talked a lot about this over the last few quarters, Mark, is that we don't -- we try to have such a differentiated assortment that what the other guys are doing -- kind of we watch with interest. But what we found is that our niche, if you like, is something that we can really manage and be comfortable that we're leading the way in that niche, as I said in our remarks earlier.

What's happening with the other guys is, yes, they are bringing the odd keto thing in, they are bringing the odd item in. But they can't -- for the target customers that we have, they simply can't have the breadth of assortment to allow them to kind of be relevant to that customer. And it's such a small proportion of the overall total. It doesn't give the -- there's no real benefit for the conventional guys to chase after this too hard because it would mean compromising some of their planograms and compromising what they're able to do. And that's how we've observed this over the course of the last few quarters, that it's not something that we're seeing -- it's certainly been a dialogue and we watch it, but it's not something that we're seeing as compromising our ability to be very relevant with our assortment to our target customers.

Mark David Carden - *UBS Investment Bank, Research Division - Associate Director and Associate Analyst*

Got it. That makes sense. And then as a quick follow-up, how did your comp trend from month to month? And what have you seen in 1Q to date?

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

Yes. Comp trends through the fourth quarter is pretty stable, Mark. It's been a good solid performance, no major ups and downs, and we're pleased with the business and where it's running. We're not going to talk about the intra-quarter here, but it's certainly baked into our guidance.

Operator

And our next question comes from Edward Kelly from Wells Fargo.

Anthony Bonadio - Wells Fargo Securities, LLC, Research Division - Associate Analyst

This is Anthony on for Ed. So just taking a step back on the comp guidance, you guided to 2.5% growth at the midpoint this year, which looks like -- it's actually about in line with where you started guidance last year despite a less constructive inflation outlook. I know there's an idiosyncratic angle here and you'll likely see some elasticity benefit. But can you just talk a little bit more about what's giving you confidence there as we think about the underlying drivers?

Curtis Valentine - Sprouts Farmers Market, Inc. - CFO

Yes, we were just watching the business, it has been pretty solid for us, pretty steady. And so we're doing a nice job driving traffic, and you can expect that to continue. We're seeing the units in the AUR stabilize sequentially as we expected. And certainly, as you pointed out, the elasticity we're seeing the units come back and stabilize as the AUR comes down, well, the rate comes down from disinflation. So we're pretty pleased with where the business is running and expect that we can continue that forward. From a 2-year stack perspective, it's pretty steady to where we've been running the last couple of quarters.

Anthony Bonadio - Wells Fargo Securities, LLC, Research Division - Associate Analyst

Okay. That's helpful. And then just on the private brand growth. I know that's been a strength for you guys these last few quarters and beyond, really. But can you just give us your updated thoughts on where that can ultimately go? And as you think about new product launches or additional SKUs in the pipeline, just how to think about growth in that category in '24?

Jack L. Sinclair - Sprouts Farmers Market, Inc. - CEO & Director

Yes. Well, we're really pleased the way the Sprouts brand has been evolving and developing over the last few quarters. The focus is very much about playing to the attribute, the attributes that focus on our target customers. I've been pleased with how the seasonal programs come together, which has been a significant evolution and development for our Sprouts brand business. I've been pleased with the redesign that the team have put in place, which I think is working well for us, and we see pretty significant growth when we redesign items and make them look the way our modern Sprouts brand looks like. So I'm comfortable with that.

So -- and then the focus in terms of what will happen with our Sprouts brand going forward, we see -- we'll see it grow. We'll continue to launch products. The focus of our business isn't about the percentage of sales that is Sprouts brand. The focus of our business is, whether it be branded items or Sprouts branded items, how do we ensure that we're differentiated. So the products we're bringing to the marketplace. What I've been really pleased about on the Sprouts brand is, I think it's becoming -- if the right word is commoditized. We're becoming less commodity focused on the items that we sell. So the everything that we're selling is differentiated. And that's the focus of the team and they're doing a terrific job.

Operator

And our next question comes from Leah Jordan from Goldman Sachs.

Leah Dianne Jordan - Goldman Sachs Group, Inc., Research Division - Research Analyst

I first wanted to ask about gross margin. I'm seeing if you could provide more detail on the drivers to the merch margin expansion that you saw in the fourth quarter. And then you also mentioned that gross margin should be up in '24. Just any color on the magnitude we should expect there or any detail on puts and takes that you're thinking about?

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

Sure, it's Curtis. For Q4, yes, the difference there, we had -- shrink was a little bit challenged in Q3. And again, ours is a little different. It's more about the fresh than it is the broader retail trends you're seeing around, but had some challenges in the third quarter as we spoke about last time, and the team has done a nice job bringing that back in line. So that was really the difference from Q3 to Q4.

Outside of that, we're still experiencing the pressure from the expanded DCs and the merch teams are doing a nice job managing the product margins.

As we look ahead to 2024, expecting those things to continue as well, I think from how much will it expand in '24, I think we're probably looking at about 20, 25 basis points of the gross margin expansion for 2024.

Leah Dianne Jordan - *Goldman Sachs Group, Inc., Research Division - Research Analyst*

Okay. Great. And then for my follow-up, I just wanted to ask about labor. You had mentioned you're still seeing pressure there. Just any update on what you're seeing in the labor market overall? Maybe some color on California specifically would be helpful. And what are ways you're thinking through of mitigating that cost pressure as you move throughout the year?

Jack L. Sinclair - *Sprouts Farmers Market, Inc. - CEO & Director*

I'll let Curtis go through some numbers in a second, Leah. But in terms of how we think, they're such an important group of people, as obvious in terms of our team members, and we've been working hard as we identified in our remarks. That, when we changed the bonus program, which has given people significant opportunities to earn more than they would have done otherwise, and we're encouraged by the reaction to that.

As I said, when you get less -- when you don't have as much rotation than the team member workforce, it actually saves us a lot of money and builds up customer service as well. So part of it is how do we retain people more effectively. Part of it is how we do the bonus program.

And with specifics to California, with which clearly something we're watching. Most -- all of our people, we're north of the \$20 thing that is so prevalent in the conversations around California. So we're in good shape there. We're getting strong applications, more -- the applications for jobs in our company is a kind of all-time high and the quality of the applications we're getting is high, we're very encouraged by as well. So we think we're in good shape with that. Having said that, there's some numbers associated with what's happened, which I'll get at Curtis deal with.

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

Yes. So we're certainly carrying some additional cost into the year as it relates to the year-over-year and we'll expect that to continue. So we're planning into just slightly less mid-single digits on the lower end to mid-single digits for our year-over-year growth in wages. As it relates to kind of how do we mitigate? Well, we're constantly looking really under every rock as it relates to SG&A, looking for ways to be more efficient. The team works really hard at it, and we'll continue to work hard at it and look for offsets in our business.

Operator

And our next question comes from Rupesh Parkih from Oppenheimer & Co.

Rupesh Dhinoj Parikh - *Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst*

Congrats on a nice quarter. So just going back to your new store commentary, it sounds like [a lot of] the stores are doing really well. But as you look at your collective class of new store openings, just curious how they're performing? Any surprises thus far? And then are they meeting your expectations from a ramp perspective?

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

Yes. Rupesh, thanks. Yes, they're right in line with how we're expecting to perform. So the new stores, we're pleased with them. We've talked about it a little over the last few quarters, no major deviations from the trends we're seeing there. We're starting a little lower, particularly in the places we have lower awareness and we're ramping faster. That's really been the story in Florida. We're seeing really strong comps in Florida. Overall, they're performing as expected, and we're seeing good results across the country.

Rupesh Dhinoj Parikh - *Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst*

Great. And then my follow-up question. And again, I'm not looking for explicit guidance for 2025. But as you look at the business, I know your longer-term algorithm is for low double-digit earnings growth. Clearly, you have a headwind related to the loyalty program this year. But is this business now in the position to get closer to that low double-digit earnings growth in the coming years?

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

Well, certainly, we talked a lot in the script about sustainable long-term growth. And so that's our goal as we move through 2024. We need to make some investments to keep the forward progress we've got moving and to set us up for that in the long term. Certainly not guiding into 2024 here yet, as you mentioned. But we're moving in that direction, and those investments are an important piece of that.

Jack L. Sinclair - *Sprouts Farmers Market, Inc. - CEO & Director*

Yes, it's early to give guidance for 2025, Rupesh. But having said that, we're very confident about our future and the investments we're making this year will certainly help us in 2025.

Operator

And our next question comes from Ken Goldman from JPMorgan.

Kenneth B. Goldman - *JPMorgan Chase & Co, Research Division - Senior Analyst*

I didn't quite understand your response to the question about the \$15 million in OpEx that you're spending this year? And how you think about that from an ongoing perspective. Could you just kind of repeat your answer or clarify it? I just didn't know if that was something that continues after 2024. And maybe I just misunderstood.

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

No, I'll clarify, Ken. I think yes, \$15 million in OpEx here in 2024, and that's really to get the loyalty program going along with some technology foundational investments. So not expecting that level of investment to continue going forward.

Kenneth B. Goldman - JPMorgan Chase & Co, Research Division - Senior Analyst

So just to build on -- again, this is going to be a question you can't necessarily answer, but I'm just curious if we're wrong here. Just to build on the prior question there. You have less than \$15 million in terms of the investment for the loyalty card in '25. Wage inflation, you've talked about getting less -- becoming less of a headwind. Who knows where it is next year, but it's trending in that way. You'll have the benefits from the loyalty card. It just feels like you're setting up for an acceleration. And maybe you have better comps as well because you have these new stores that are accelerating this year, maybe at a lower base, that will help you with your comps next year. What are we missing in terms of -- there's a lot of tailwinds maybe as we think about '25? Are we wrong to think about that as kind of an accelerant year for you, even though it's way too early to really be specific?

Jack L. Sinclair - Sprouts Farmers Market, Inc. - CEO & Director

I think you said it with your last remarks there. I think it is a little bit early for us to get very buoyant about it. But we certainly believe that understanding our customers more and navigating our way through trying to drive a larger share of wallet of our target customers will provide growth for us in the future. And that's certainly why we're investing this money this year with the premise that it's going to come in terms of top line in 2025 and beyond.

And it's part of an ongoing process of how do we understand our customers better. If we're going to be a really great specialty grocer, we've got to understand that customer even better than we do at the moment. And that's the key work behind it. And we'll learn a lot this year from the work that we're putting in, in terms of what it will be able to do. And as we get towards the end of 2024, I think we'll be more able to have a conversation about what it's actually going to mean for us in '25 and '26.

Operator

And our next question comes from Scott Mushkin from R5 Capital.

Scott Andrew Mushkin - R5 Capital LLC - Founder, Managing Partner, CEO & Director of Research

And it's kind of along the same lines of what Ken and Rupesh were talking about. Kind of looking out at the kind of medium- and longer-term algorithm on growth here, especially with the new store builds, it's hard for me to kind of understand how you wouldn't normalize the comp at, at least 4%. And if the base stores are growing decently and with all the new stores coming in. And just trying to -- like talk me out of that, like why wouldn't that be the case?

Curtis Valentine - Sprouts Farmers Market, Inc. - CFO

Well, I don't -- Scott, I don't think we'll talk you out of that. I mean, certainly, we aspire to drive that type of comp as we look ahead. Again, a long ways off from 2025 and '26, some pressure on the consumer at the moment, and we've got to execute. We've got to deliver on the things that we're putting in and what we're investing in and do a good job here in 2024. But we're certainly angling to drive a sustainable comp for 2025 and beyond.

Scott Andrew Mushkin - R5 Capital LLC - Founder, Managing Partner, CEO & Director of Research

And you guys said you're happy with your new stores. I assume there's a maturation process going there and your -- and you're seeing that come through. But if you take a step back and now that you're getting a lot of the smaller box formats in the ground, like what's working better than maybe you thought? And maybe what's a little worse? And what are you going to tweak?

Jack L. Sinclair - *Sprouts Farmers Market, Inc. - CEO & Director*

Yes, I've been really pleased with frozen foods, which is something we talked about a lot when we introduced a new format. That's performing really well and I'm very pleased with the space that we invested in that. I'm very pleased with meals, how we're doing with prepared meals, and we put a lot of emphasis on that, in turn, new format stores, and that's flowing through well. We're encouraged by, as I said earlier, with our innovation center in terms of what that's doing for our stores. So there's kind of 2 or 3 high points in it. One of the areas that we invested in that hasn't been as strong maybe is the plant-based meat investment. Plant-based dairy is doing very well, and our dairy business is doing well. But plant-based meat was a big trend, and that's probably not come through as well as we would have liked it to do.

But overall, in total, it's coming through the way we'd like it. I like the fact that we've got to meet at front of the store in terms of what that's doing to drive center of plate. So I think, by and large, the things that we put in place have worked pretty well.

Operator

And our next question comes from Mike Montani from Evercore ISI.

Michael David Montani - *Evercore ISI Institutional Equities, Research Division - MD*

I was just hoping to unpack a little bit for the quarter and then in the guidance for the full year. If you could just unpack a little bit what you saw in terms of traffic and how you're thinking about the traffic. Would that be up next year? And then also in terms of inflation, is that kind of 2% to 3% in the fourth quarter? And how much of that do you have baked into the guide for the comp?

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

Yes. So I'll take it from the fourth quarter. Yes, I saw positive traffic again in the fourth quarter. Really, the shape of it didn't change materially from the third quarter other than AUR and units stabilizing a bit. AUR is a little -- slightly higher than what you were describing there, Mike, in the fourth quarter. As we look ahead to '24, it will be a slight positive traffic again. We are expecting inflation and AUR to be slightly up. And then we'll have slightly lower units as the offset there. We're expecting units to flatten out as everything kind of normalizes and stabilizes finally, hopefully, in 2024. We've said that a couple of years running now. And not all the way there yet, but pretty close, and that's what we're expecting for 2024.

Operator

And our next question comes from Bill Kirk from ROTH MKM.

William Joseph Kirk - *ROTH MKM Partners, LLC, Research Division - MD*

So I think you've lapped adding DoorDash as an incremental e-commerce partner. So if 4Q e-commerce was up 17% year-over-year, I guess, what happens to that growth rate now that the partners are mostly the same year-over-year?

Jack L. Sinclair - *Sprouts Farmers Market, Inc. - CEO & Director*

Well, we brought in another partner. So there's -- we've got the -- Uber Eats is coming -- sorry, I didn't remember that for a minute. We brought Uber Eats very recently into the business, so that will add to it. What I'm very encouraged about is how the omnichannel process that we're going through. It's really encouraging that when we get the kind of growth that we're getting in an e-comm environment because customers wouldn't be navigating to our assortment if there wasn't something differentiated in it. And the fact that we're -- we're doing so well in e-com gives me a lot of encouragement about the work that the merchants and the foraging team are doing in terms of bringing products to the marketplace.

In terms of going forward, it will be what it will be, the customer is going to take us where they want to take us. We're giving them now the option. They can do DoorDash, they can do Uber Eats and Instacart have been great partners for us as well. So we're very, very pleased with the partnerships we've got with all 3 of the e-com providers. So going forward, it will be what it's going to be, but it's within the guidance that Curtis talked. If you want to build on that?

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

Yes. I just think, Bill, the timing of it is pretty close, right? I think we launched Uber about 1 year after DoorDash and DoorDash ramped up throughout the year. And so they'll continue to contribute to the comp, not to the same degree, clearly, as last year. But Uber has basically launched rate 1 year later. So those 2 things should kind of neutralize themselves.

William Joseph Kirk - *ROTH MKM Partners, LLC, Research Division - MD*

Okay. Awesome. And then as a follow-up, it seems to me like produce input prices are a bit more deflationary than maybe your produce prices on the shelf. First, I guess, is that fair? And then if it is, is that dynamic in place as a way to refine a customer base towards more profitable households? Or would it be more of a like a temporary industry-wide dynamic and the two would eventually match?

Jack L. Sinclair - *Sprouts Farmers Market, Inc. - CEO & Director*

Well, as we've talked a lot about in projects, there's a lot of volatility in pricing, and it's difficult to kind of be very definitive about exactly what's happened from one week to the next -- never mind one year to the next on that. Our produce business has been very -- we've been really pleased with organic produce, and that's something that we can -- we kind of own the mix that we have in organic of our total produce business. It's very different to how you would see in a conventional grocer or even in Walmart or club channel.

We're seeing a really strong organic business. And that's where pricing -- we think we've got really good long-term relationships with the vendor base and in organic produce, and I think we're in a strong place to kind of manage the ups and downs effectively in terms of what happens to the volatility of prices. I'm not sure if I'm answering your question, but certainly, organic produce and the differentiation of price that we have in organic produce, we think stands us in good stead going forward. And we're doing a lot of work to improve the quality and freshness of our produce, both in terms of investment in physical distribution and investment in our systems and our replenishment systems and our forecasting systems, to make sure that we get even better in terms of freshness for our customers.

So again, it's probably too volatile for us to give a definitive kind of answer to your question there.

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

And I just add, Bill, we're going to look just a bit different because of that organic mix than everybody else. And so that will play a part in that, too.

Operator

And our next question comes from Kendall Toscano from Bank of America.

Kendall Belinda Toscano - *BofA Securities, Research Division - Research Analyst*

Congrats on a great quarter. My question was just basically about inflation and what you're seeing on center store. And I guess what you would expect heading into 2024, is there anything from suppliers that they're pushing back on price at all? Any color there?

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

And I think, I assume when you say center store, you mean in the nonperishables, which is different for us. But I think certainly, fresh is the more volatile piece, as Jack just alluded to. And so as we think about the nonperishables, I think that's a little bit more in line with what the macro newsprint is on that, and our fresh business tends to be the more volatile piece. As I mentioned earlier, we're on the higher end of low single digits is what we're experiencing current -- or in Q4, and we'll watch that stabilize here in 2024.

Jack L. Sinclair - *Sprouts Farmers Market, Inc. - CEO & Director*

And there remains a volatility in commodity pricing. I think if you look at things like cocoa and sugar, and people that are saying that those prices are going up pretty dramatically. And I think that will flow -- maybe flow through. Other commodities are going in the opposite direction. But certainly, the one difference with our business in center store, which is, again, it's not really a Sprouts expression center store. But for our nonperishable business, we have got a lot of differentiation in what we sell, and it's very unlikely that a lot of the drivers for commodities that are hitting the big CPG items being sold in conventional will affect us one way or the other. We've kind of managed to navigate our way through that without being dramatically affected by some of those swings and roundabouts.

Kendall Belinda Toscano - *BofA Securities, Research Division - Research Analyst*

Got it. That's really helpful. And then as a follow-up, just could you remind me of the 35 stores you're opening next year, what the focus is between new and existing markets?

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

Kendall, it's about 50-50, about half in kind of existing established markets and then half on really the East Coast and Florida and the Mid-Atlantic as the drivers there.

Jack L. Sinclair - *Sprouts Farmers Market, Inc. - CEO & Director*

We've opened 4 this year. One is that we -- when I think about it, we've just opened a really nice store, which we're very pleased with in [cuddy] Los Angeles. We've got a really nice store in Miami. So we're kind of opening stores all over the country at the moment, in Maryland. And so it's actually quite exciting to see us building the Sprouts brand from sea to shining sea.

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

I think the only other note, Kendall, on the new stores for this year is they're going to be back half loaded about 2/3 of them will open in the second half of the year.

Operator

And our next question comes from Krisztina Katai from Deutsche Bank.

Krisztina Katai - Deutsche Bank AG, Research Division - Research Analyst

I wanted to ask about the customer strategy. So you have a lot more insights into overall purchasing patterns, than you even did a year ago. So I was wondering if you could quantify, maybe how data is helping you in driving increased traffic or customer frequency? And just how do you think about the uplift opportunity, especially as you're gearing up for a loyalty program launch?

Curtis Valentine - Sprouts Farmers Market, Inc. - CFO

Well, we're still fairly immature in that space, right? We talked about kind of low double digits of identifiable customers and high double digits, call it, 19% of our transactions that we can identify. So -- we've got a long ways to go there. We're really excited for the opportunity with loyalty and getting the test out there in the middle of the year. But we've got a long ways to go on our ability to do that. I think the team has done some early work, some good work around some personalization testing. We've done some vitamins retargeting and things like that. We've gone after organic and attributes within segments of our customers. And so this year and part of the investment in loyalty about getting the foundation and the data foundation right to be able to really do that at scale. And so we'll be working hard on that this year, and we're excited for what that could do for us down the line.

Krisztina Katai - Deutsche Bank AG, Research Division - Research Analyst

And I was just wondering if you could give a bit more color in terms of what your actual mature stores are doing from a comp perspective. You obviously have a waterfall benefit. But just wondering how mature stores are comping versus the newer ones? And if there's any update on the waterfall benefit that we should keep in mind for the next couple of years.

Curtis Valentine - Sprouts Farmers Market, Inc. - CFO

Yes. No problem. So again, we've talked a lot -- good momentum in the newer markets and strong comps, especially in those places where we're not as established. They start a little lower and they're seeing a really strong comps. So it's contributing to our comp for sure, and the mature stores are comping well. I won't get into specifics per se. I think the only other thing to think about is just the newer stores, again, at a little bit lower volume as they start. Not as impactful on the comp base as the mature stores, so that will impact that kind of spread between the new and the comp stores or the mature stores.

Operator

And our next question comes from Kelly Bania from BMO Capital Markets.

Kelly Ann Bania - BMO Capital Markets Equity Research - Director & Senior Food Retailers Analyst

Wanted to go back to the discussion of gross margin, I believe your long-term plan there was kind of for a flattish gross margin. You clearly see some opportunity to take that up this year. But I was just curious if you could talk about if anything has changed long term? Do you see more opportunity to continue to take that up? And maybe can you just help us understand the opportunity? I think you called out shrink and promotional optimization. Maybe you could just elaborate on the factors driving that this year and maybe long term?

Curtis Valentine - Sprouts Farmers Market, Inc. - CFO

Sure. Well, long term, I think we're still thinking about it as stable from holding our margins steady. I think what we've got going on a little bit right now is really just a little bit of a shrink story. So we had a rough second half from a shrink perspective. Ops team has done a really nice job late in Q4, kind of getting that back in line. And so we feel like there'll be some opportunity, particularly in the second half as we lap those numbers next year on the shrink line. So that will be a driver of it.

And then we do -- merchants have done a nice job. So we continue to optimize promotions and manage the mix of the business, and that will have just a little bit of carryover from what's been working for us in 2023 in the first half of the year.

I think the last piece is that the supply chain pressure we've experienced in the second half from the expanded square footage, we'll lap that through the first half of the year, and then that pressure will ease as we get into the second half.

Kelly Ann Bania - *BMO Capital Markets Equity Research - Director & Senior Food Retailers Analyst*

And can I just also follow-up on the guidance range, it's a pretty narrow kind of range for the full year. I was just curious if you can kind of talk about the puts and the take. I mean at the low end of the comp range, is that really -- can you still get to flat earnings on that kind of comp? Maybe just help us think about how your -- how you plan to manage that.

Curtis Valentine - *Sprouts Farmers Market, Inc. - CFO*

Yes. I think, again, we'll have to -- we had a little bit of gross margin expansion. We'll have to work hard on the cost side, as we've mentioned, and look for opportunities to offset some of the pressures we're experiencing. It does get harder, obviously, as it goes towards the low end of the range as you're starting to deleverage against some of the fixed costs, but we feel comfortable with the guidance and the ranges we have out there and being able to deliver.

Operator

And thank you. And I'm showing no further questions. I would now like to turn the call back over to Jack Sinclair for closing remarks.

Jack L. Sinclair - *Sprouts Farmers Market, Inc. - CEO & Director*

Yes. Thanks, everyone, for spending some time with us this afternoon. We appreciate your interest in our company, and we look forward to bringing you up to date through the year as our business evolves. Thanks ever so much.

Operator

This concludes today's conference call. Thank you for participating. You may now disconnect.

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