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The Kroger Co. (KR)

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, and welcome to The Kroger Co. Fourth Quarter and Full Year 2024 Earnings Conference Call. [Operator Instructions] . Please note this event is being recorded.

I'd now like to turn the conference over to Rob Quast, Vice President, Investor Relations. Please go ahead.

Rob Quast

Vice President-Investor Relations, The Kroger Co.

Good morning. Thank you for joining us for Kroger's Fourth Quarter and Full Year 2024 Earnings Call. I am joined today by Kroger's Chairman and Chief Executive Officer (sic) [Chairman and Interim Chief Executive Officer] (00:00:38), Ron Sargent; and Interim Chief Financial Officer, Todd Foley.

Before we begin, I want to remind you that today's discussions will include forward-looking statements. We want to caution you that such statements are predictions, and actual events or results can differ materially. A detailed discussion of the many factors that we believe may have a material effect on our business on an ongoing basis is contained in our SEC filings.

The Kroger Company assumes no obligation to update that information. After our prepared remarks, we look forward to taking your questions. In order to cover a broad range of topics from as many of you as we can, we ask that you please limit yourself to one question.

I will now turn the call over to Ron.

Ronald L. Sargent

Chairman & interim Chief Executive Officer, The Kroger Co.

Thanks, Rob. Good morning, everybody. Thank you for joining our call today. Before we begin, I'd like to just share a few comments.

Kroger has always been committed to its enduring values. This has been true for Kroger since my first job in the summer of 1974, working in the Fort Mitchell, Kentucky store. In many ways, I grew up at Kroger, working summers in college and then full-time for 10 years following business school. I've held various roles in stores and manufacturing, human resources, marketing strategy and sales. Kroger has really been a special place throughout my career in retail, and I'm just as proud to be a Kroger associate today as I was then.

I will be serving as the interim CEO as we search for a leader for our next phase of growth. The board has formed a search committee and has engaged a nationally recognized search firm. We look forward to updating you as we have more information.

As a board member, I know Kroger's strong leadership team well, and they support the unique culture that powers the company's long-term success. We care for people, and we love food, the most important elements of successful grocery retail.

Today, Kroger operates from a position of strength. We delivered strong financial results in 2024 and have positive momentum in our business. We're confident in our plans for 2025, and our commitment to deliver total shareholder return of 8% to 11% over time. I will be especially focused on executing with speed and confidence, keeping our teams working toward the priorities that create long-term growth.

We're delivering on our go-to-market strategy, providing families across America with fresh and affordable food. In my retail career, I understood that an outstanding customer experience comes from best-in-class store conditions, friendly associates and great products at low prices. That's who Kroger is today and that's who we will be tomorrow.

I'll turn the call over to Todd to recap our 2024 performance, and how our value creation model allows us to deliver on our goals. He will then recap our financial results for the fourth quarter and full year 2024, and then cover 2025 financial guidance. Todd?

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

Thank you, Ron, and good morning, everyone. Kroger achieved solid results in 2024, demonstrating our value creation model, strength and diversity. Our performance improved as the year progressed, and our momentum positions us well for growth, as we head into 2025.

Offering fresh, high-quality products with personalized offers through a unique seamless shopping experience led to strong customer engagement trends, including growth in both households and loyalty.

As a result, we are growing sales and generating traffic, which accelerates growth opportunities in other areas, including alternative profit businesses. We are confident in our ability to build off this base from 2024 and deliver growth in 2025.

Before we get to 2025, I'd like to start with a recap of last year, beginning with our customers. We saw customers adjust their spending habits, responding to ongoing macroeconomic factors. The effects of multi-year inflation and higher interest rates pressured spending from budget-conscious households.

Meanwhile, spending from less budget conscious households was more resilient and our most favorable household trends were driven by our core mainstream customers. Our go-to-market strategy positioned us well to meet our customers' needs growing households and enhancing loyalty.

We helped customers save in multiple ways through fresh affordable products and promotions, including loyalty discounts, personalized offers and fuel rewards, also through Our Brands products, which are priced well below national brands at equal or greater quality.

Our focus on operational excellence through our full Fresh and friendly strategy brought our strategic pillars to light, meaning our customers can have value, selection and convenience. We will continue to improve our customer experience to drive traffic and increase volumes because it powers our value creation model and is critical to our long-term success. Fresh is one of the primary determinants of where customers shop and we continue to invest to offer more days of freshness.

In 2024, we reduced dwell time in or distribution centers, which meant most customers, had extra days of freshness in their homes on key fresh items. As a result, we saw strong year-over-year identical produce sales improvement above our total company identical sales without fuel results. Going forward, we see more opportunities to enhance our sourcing capabilities and supply chain to deliver additional days of freshness.

On to Our Brands. Our Brands is an important differentiator for our business, providing Kroger the ability to offer unique and high-quality products at an exceptional value. We expanded our multiyear Our Brands product portfolio in 2024, resulting in more than 90% of customer households purchasing Our Brands items last year. Overtime, we built distinct brands that are customer favorites. We're always listening to our customers to understand how we can create more offerings to better meet their needs. Our proprietary customer insights drive our innovation and led to more than 900 new Our Brands products released last year alone, including 370 Fresh items.

We look to create destination items that can only be found at Kroger, differentiating ourselves from competitors and national brands. Last year, we introduced Field & Vine, a new brand offering regionally grown berries. We also began refreshing existing product lines and rolling out new packaging, which reinforces product quality and improve shopability.

Turning to Seamless, digital sales were strong in 2024 with more than $13 billion in sales. As our digital business grows, so does its impact on our financial results. As a result, we're making improved profitability a key priority through automation, new technology and improved density and volumes. We are encouraged by our fourth quarter results, which delivered the best digital profit improvement quarter we've seen yet.

Seamless is an important growth accelerator in our business. Capturing more digital households is important to accelerating growth in our model because these households are more loyal and spend nearly 3 times as much as non-digitally engaged households. The additional households in traffic in turn create more growth opportunities in our alternative profit in health and wellness businesses.

Kroger's alternative profit businesses are high growth and margin rich. Alternative profit businesses delivered solid results in 2024, generating $1.35 billion in operating profit, driven by a 17% increase in media, excluding the 53rd week in 2023.

While our pool of alternative profit businesses fell short of our initial growth expectations in 2024, in part due to slower growth in advertiser spend, we expect both near- and long-term growth to exceed our 2024 results. 2025 is off to a strong start with increases in upfront commitments from both CPGs and agencies.

KPM's mission is to be the most trusted and transparent media company by offering advertisers more effective ad spending through a compelling combination of custom audiences and ad effectiveness measurement. KPM continues to make strategic decisions to sign to further this mission such as their holistic brand building approach with clients. We expect a long runway for growth, which will be supported by continued innovation and growth in our digital sales.

Health and wellness delivered solid sales results, gaining momentum in the second half of the year, as strong vaccine performance in the second half helped offset margin pressures from growth in GLP-1 sales.

Last month, we announced a new agreement with Express Scripts, which will provide ESI customers access to prescription medications and health services at Kroger pharmacies. While exiting this relationship in 2022 was a difficult decision, we are pleased to renew this relationship under a fair and more equitable contract, which enables us to operate on a sustainable basis and keep prices low for customers.

As our teams begin to welcome these patients back into our stores, we know it will take time to build the ESI business back up. As a result, our 2025 guidance does not assume any benefit from our recently signed agreement with ESI.

Improving productivity is a core competency for Kroger and essential to our value creation model. We are focused on productivity initiatives, which preserve and enhance both the customer and associate experience.

For example, we introduced a virtual AI-powered assistant for associates last year. Today, almost 70,000 associates engage with this tool for more than 70 use cases. It provides personalized service to associates for common HR and associate interactions, including training and onboarding. It also provides leaders real-time and convenient access to labor data, ensuring fully staffed stores.

Our efforts to improve strength provide another example where productivity improvements directly connect to our strategy and improve customer experience. Last year, we launched a new generative AI-powered sell-through tool that uses real-time sales and shipment data, that empowers associates to better manage Fresh and center store inventory. As a result, our products are fresher, we prioritize sell-through, and that optimizes both sales and margins.

I'll now walk through our financial results, beginning with the fourth quarter. We achieved identical sales without fuel growth at 2.4%. These results reflect positive momentum in our grocery business, along with strong pharmacy and digital sales growth.

Our Brands had another strong quarter, with sales outpacing national brands, led by growth in our most premium brand, Private Selection. Encouragingly, our positive sales trends were broad-based across many of our food categories during the quarter.

The FIFO gross margin rate, excluding rent, depreciation and amortization, fuel and the 53rd week of 2023 increased 54 basis points in the fourth quarter compared to the same period last year. The improvement in rate was primarily attributable to the sale of Kroger Specialty Pharmacy and lower shrink, partially offset by lower pharmacy margins.

The operating general and administrative rate, excluding fuel adjustment items in the 53rd week, increased 16 basis points in the fourth quarter, compared to the same period last year. The increase in rate was primarily attributable to the sale of Kroger Specialty Pharmacy, increased incentive plan costs and investment in associate wages, partially offset by the continued execution of cost savings initiatives.

After adjusting for the effect from the sale of Kroger Specialty Pharmacy, our OG&A rate improved this quarter, demonstrating our ability to leverage expenses when achieving our long-term sales algorithm.

Our adjusted FIFO operating profit was $1.2 billion. We had a LIFO charge for the quarter of $30 million compared to a credit of $18 million for the same period last year. Adjusted EPS was $1.14, which is flat compared to the same period last year, excluding the 53rd week.

I'll now walk through our full year 2024 results. Kroger achieved identical sales without fuel growth of 1.5%. Digital sales grew 10% compared to last year, excluding the 53rd week, and delivery solutions led sales growth with an 18% increase.

Demand across our Kroger delivery network continue to be strong with an increase in both households and traffic. Customers enjoy the premium experience of our delivery service reflected by consistently strong Net Promoter Scores.

Health and Wellness was also a strong driver of sales this year, led by growth in GLP-1s. The FIFO gross margin rate excluding rent, depreciation and amortization, fuel in the 53rd week of 2023 increased 32 basis points. The improvement in rate was primarily attributable to the sale of Kroger Specialty Pharmacy, Our Brands performance and lower shrink, partially offset by lower pharmacy margins.

The improvement in FIFO gross margin rate reflects progress on our long-term margin enhancement strategies. Going forward, we continue to see more opportunity for improvement through Our Brands, growth in alternative profits, utilizing technology through our supply chain, enhancing our product mix through Fresh and improving digital profitability.

The OG&A rate, excluding fuel, adjustment items in the 53rd week of 2023, increased 31 basis points. The increase in rate was driven by the sale of Kroger Specialty Pharmacy, increased incentive plan costs, an increase in costs due to the severity of general liability claims and investment in associate wages, partially offset by the continued execution of cost savings initiatives.

Our adjusted FIFO operating profit was $4.7 billion. Our LIFO charge for the full year was $95 million, compared to LIFO charge of $113 million last year. Adjusted EPS was $4.47 per diluted share. Excluding the 53rd week in 2023, EPS declined 2%.

Fuel is an important part of Kroger's strategy and offers an important way to build loyalty with customers due to fuel rewards in our Kroger Plus program. Fuel sales were lower this quarter compared to last year, attributable to fewer gallons sold and lower average retail price per gallon.

Fuel profitability was also behind the same period last year, as a result of fewer gallons sold, and lower cents per gallon margin. On both the fourth quarter and full year basis, fuel was a headwind to our results.

I want to provide a brief update on our inflation expectations. Inflation in 2024 increased throughout the year and was in line with our expectation. And as we look ahead to 2025, we expect inflation to be 1.5% to 2.5%, which does not include the effects from tariffs announced earlier this week.

External factors continue to pressure certain Fresh commodities, including eggs. Notably, the Avian flu resulted in egg inflation of approximately 70% during the quarter. Inflationary pressures are not new to our business, and we're confident in our ability to navigate any inflationary environment. We will remain focused on keeping prices low for our customers.

I'd like to take a moment to talk about our associates. We respect and reward our associates because their success enables the success of the company. Ensuring they are successful, means improving wages and benefits, focusing on associate well-being and developing talent to create fulfilling careers. This approach improved retention as our store and enterprise retention rates reached record levels this year.

Creating a better associate experience has benefits for our business. When associates stay longer, they're better operators and deliver a better customer experience. In 2024, we raised the bar on our customer experience metrics and our associates exceeded those higher expectations to deliver an exceptional customer experience that drove sales growth.

These associate investments include associate wage increases in 2024, resulting in an average hourly rate of more than $19 an hour and a rate of more than $25 with comprehensive benefits factored in.

Over the last seven years, Kroger has increased wages by 38%. Kroger remains committed to supporting our associates with investments in wages and comprehensive benefits that are sustainable and will allow us to keep prices low for our customers.

Similar investments in associates are incorporated in our 2025 guidance and long-term growth model. During the fourth quarter, we ratified several new labor agreements, including our Fred Meyer, Alaska stores with the UFCW.

I'd like to now turn to capital allocation of financial strategy. Our strong balance sheet and free cash flow provide a significant financial flexibility to invest in our business and drive returns for our shareholders. At the end of the fourth quarter, Kroger's net total debt-to-adjusted EBITDA ratio was 1.79, compared to our net total debt to adjusted EBITDA target ratio range of 2.3 to 2.5.

Our capital allocation priorities remain consistent and are designed to accelerate our value creation model to deliver on total shareholder return at 8% to 11% over time. We are focused on investing in projects that will maximize return on invested capital over time, while remaining committed to maintaining our current investment-grade rating, growing our dividend over time, subject to board approval, and returning excess capital to shareholders.

In 2024, we announced our plans to significantly increase our investment in major storing projects, including new stores to accelerate sales growth and improve share, while supporting our long-term growth model. We delivered on that commitment in 2024, completing 29 major storing projects focused in higher-growth geographies that have track record for generating strong cash flows and returns. We expect to complete 30 major storing projects in 2025.

We also expect new storing to continue to be a meaningful contributor to our long-term growth model and would expect new store openings to accelerate beyond 2025. In December, we delivered on our commitment to return excess capital to our shareholders. We announced a new $7.5 billion repurchase authorization. Under this authorization, Kroger entered into an accelerated share repurchase program for $5 billion of common stock.

During the fourth quarter, Kroger initially purchased 65.6 million shares as part of the ASR. The ASR program is expected to be completed by no later than the third quarter of Kroger's fiscal 2025. After completion of the ASR, we expect to resume open market share repurchases under the remaining $2.5 billion authorization that will further enhance shareholder value.

Last year, Kroger issued $10.5 billion in new debt financing, of which $4.7 billion was redeemed when the merger terminated, leaving Kroger with $5.8 billion of new debt. Given this higher debt load, we expect interest expense to increase in 2025. Assuming current interest rates, we expect full year net interest expense to be between $650 million and $675 million.

The net impact of our financing and the share reduction from ASR created $0.01 of accretion to adjusted net earnings per diluted share in the fourth quarter.

Turning now to 2025 guidance. We expect to achieve identical sales without fuel of 2% to 3%, adjusted FIFO operating profit of between $4.7 billion and $4.9 billion and adjusted net earnings per diluted share of $4.60 to $4.80. We expect the LIFO charge to be approximately $130 million, assuming inflation is in line with current expectations.

In terms of quarterly cadence, we expect identical sales without fuel to be consistent throughout the year, building slightly as the year progresses as we continue to improve our volumes. We expect first quarter adjusted net earnings per diluted share to be similar to last year, and we expect quarter two through quarter four to be consistently above each quarter compared to the same periods of last year.

In terms of margin rates, we expect FIFO gross margin and OG&A rates, excluding fuel and adjustment items, to be relatively flat on a year-over-year basis after excluding the effects of our sale of Kroger Specialty Pharmacy business.

In closing, we're happy to deliver another year of solid results which reflect the strength of our model. Investments made to diversify our model has strengthened Kroger, positioned us well to deliver now and invest in the future. We're a more diverse business, and we are excited about the opportunities across our business to deliver future growth.

The strength of our model and the momentum in our business support our confidence in achieving our 2025 guidance and our ability to continue delivering for our customers, investing in our associates and generating attractive and sustainable returns for our shareholders.

I will now turn it back to Ron.

Ronald L. Sargent

Chairman & interim Chief Executive Officer, The Kroger Co.

Thanks, Todd. As you heard from us today, Kroger operates from a position of strength, and I'm very optimistic about our future. We delivered solid results in 2024, and our performance improved throughout the year.

Looking to 2025, we have aggressive plans to build more stores and improve our share results, attract new households and increase loyalty, which will accelerate growth and create shareholder value.

We continue to have a strong balance sheet, which positions us well for the future, allowing us to invest in our business for growth while remaining disciplined on returning cash to shareholders.

Given our ongoing search for a CEO, Kroger has postponed its planned Investor Day in April of 2025. We will update investors at a later date when it has been rescheduled. In the interim, Kroger remains committed as always to being accessible and updating you on our strategic priorities.

Before we open up for any questions, I want to take a moment to welcome David Kennerley. He will be joining us next week, and he will succeed Todd as Chief Financial Officer on April 3. David is joining us from PepsiCo Europe and brings broad and extensive financial experience. We are confident that David's expertise and leadership will help us to continue to deliver on our strategic and financial priorities.

We'll now open it up for questions. And as you might imagine, Todd will handle questions related to strategy and results.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question for today comes from Simeon Gutman of Morgan Stanley. Your line is now open. Please go ahead.

Simeon Ari Gutman
Analyst, Morgan Stanley & Co. LLC

Q

Thanks. Good morning, everyone. So, my question, at the highest level, if you look at the 2025 guidance, it looks like EBIT is expected to grow in the low single digits, 2% to 3%.

Within that, can you share how much is coming from the core business versus alternative? And then one follow-up, I don't know if we're able to ask Ron questions, but good to hear from you, Ron.

I wanted to ask, as you and the Board approaches the succession of CEO, you're obviously sitting on a treasure trove of great operators within the organization. How are you looking at an outside perspective?

Because the traditional supermarket channel, not just Kroger, has had mixed market share results over time. And it's obviously becoming more complex and the stakes are growing, so thinking about looking at outside talent versus the treasure trove of folks that you're sitting on internally. Thank you.

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Yeah. Thanks, Simeon. Appreciate the questions. I'll – let me talk about the guide first, and then I'll turn it over to Ron, for your CEO, succession question. Yeah. The operating profit growth estimates, if you look at the middle of the range, it's – you're right, it's probably in the 3% range.

And we see growth both on the core business and from our alternative profit business, again, we talked in the comments where we didn't quite hit our expectations for alternative profit, but we do expect that to continue to contribute back in advance of what we saw in 2024 next year.

But Ron alluded to it, I alluded to it on the call, we do have momentum in our core business and do expect solid growth in our operating profit to come from the core part of the business across the store, both center store. Pharmacy, we expect a little bit of growth in alternative profit to contribute to that as well.

So, Ron, I'll turn it over to you.

Ronald L. Sargent
Chairman & interim Chief Executive Officer, The Kroger Co.

A

Hey Simeon, great to work with you again. I'll tackle the succession planning question. Just to give you a little bit of background, the Board updates our specs for CEO every year. It's just part of our annual succession planning process.

And the reason we do that is because our business changes every year and the environment we operate in changes every year as well. So, we are in the process of updating that again.

And in terms of the process, the Board has formed a Search Committee. We have begun the search process. We have hired a nationally recognized firm. We are going to be looking at both internal candidates as well as external candidates.

But I think most importantly, we're focused on identifying the right leader to drive Kroger's growth and enhance shareholder value. I am proud to serve in this role for as long as needed. But I am absolutely confident that our Board will select the right next CEO, whether from inside the company or outside.

Simeon Ari Gutman
Analyst, Morgan Stanley & Co. LLC
Q

Thanks everyone. Good luck.

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.
A

Thank Simeon.

Operator: Our next question comes from Leah Jordan of Goldman Sachs. Your line is now open. Please go ahead.

Leah Jordan
Analyst, Goldman Sachs & Co. LLC
Q

Good morning. Thank you for taking my question. I just wanted to dig into digital a little bit. It sounds like it continues to be a strong channel for you, and profitability improved notably this quarter. Just looking a bit longer term over the next couple years, seeing if you could provide more detail on the path of improvement from here?

And I guess, how much more can lower costs in the retail media growth that seems to be accelerating here, can offset other ongoing investments you're making, like price investments in the channel?

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.
A

Yeah. Thanks, Leah. I'll start with the digital piece. Again, and you're right, we were really pleased to see the sequential improvement in our profitability in the digital channel in the fourth quarter. And it was really in both of the key elements. We saw it in pickup. We continue to make progress, in improving our cost-to-serve within our stores. And we also saw it in the delivery channel. We've talked a lot over time about some of the things that we're doing inside our sheds and in the last mile relative to our sheds in conjunction with Ocado and working with them to improve that. And so again, we saw it in both spots.

We're not where we want to be, we've alluded to that. We're not where we need to be. But I think the green shoots that we had seen prior to the quarter and the progress we made on those during the quarter, I think, puts us on a trajectory that if we maintain that consistently and string a few quarters together, I think that will help get us where we want to be over the long term. So again, we're encouraged, and I think we're on the right path to string a few of those quarters together to be where we want to be long term.

Your other question, if I caught it correctly, was around how we generate value in the business to continue to be able to invest. So, we've talked a lot about the levers that we have. And the way we go about our strategy, we have as many levers – probably more levers today than we've ever had to try to drive that value in the business.

We talk about margin enhancement initiatives like alternative profit, and again, the consistent meaningful growth that it provides.

Our Brands is a margin enhancer. And particularly in this environment around – all customer cohorts are looking for value. We've talked about how successful that has been for us over the last several quarters. And we continue to find opportunities in productivity in all elements of our business. There's productivity in store. But we're such a vast business with so many opportunities, whether it's in our supply chain business, in the DCs or transportation, we continue to unlock opportunities to create that value, and that's essential to our model to be able to invest in price and to continue to invest in associates.

And so, every year, and 2025 is no different than years in the past, our level of investment in both prices and associates is pretty consistent with what we've seen year-to-year, but that commitment remains because it's essential to be able to deliver key prices to our customers and invest in our associates. Our associates are the ones that deliver that amazing shopping experience and connect with those customers in all realms. And so, we still see a very meaningful runway from all of the opportunities that we have and the levers to create value.

Leah Jordan
Analyst, Goldman Sachs & Co. LLC Q

Great. Thank you.

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co. A

Thanks, Leah.

Operator: Thank you. Our next question comes from Michael Lasser of UBS. Your line is now open. Please go ahead.

Michael Lasser
Analyst, UBS Securities LLC Q

Good morning. Thank you so much for taking my question. Ron, it's been too long.

Ronald L. Sargent
Chairman & interim Chief Executive Officer, The Kroger Co. A

Yeah.

Michael Lasser
Analyst, UBS Securities LLC Q

Yeah. But my question is that if we look at your ID sales guidance for this year, you're basically assuming that volumes are flat to probably even down given that your inflation expectation, along with what will likely be outperformance from your health and wellness business, due in part to GLP-1s. So, A, why is that? And B, Ron, is there anything that you can do now that you're in the CEO seat to address maybe some of the shortcomings of the business that you observed as a board member?

And just a quick logistical question, Todd. What is driving EPS to be flat year-over-year in the first quarter? Thank you very much.

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.
A

Great. Yeah, Michael, let me touch on those. I think I can hit on each of the pieces that you have. The ID guide, I think, fundamentally have the pieces right when you look at our inflation expectations for next year and relative to volumes.

When you look at the whole year and think about it flat to maybe slightly up, I think that's the right way to about it. Obviously, coming into the year, we're still slightly negative, but we're driving off what's been continued sequential improvement quarter-to-quarter, and that trajectory is why we expect that during the year, we'll flip that over to positive.

So, I think the combination of those two, when you think about the business without pharmacy, gets us to nice growth in the core business. And then, when you do layer pharmacy on that, I think that's what puts us right into the middle of the range. So, I think, you're thinking about those pieces consistently.

And then, I'll talk too about quickly the flat in Q1, to that part of your question. Really what we saw Q1, it was a couple of things. One, we had some OG&A items when you look at a year-over-year comp that is really driving that. There were a few there but the biggest I think the call out is around some union pension relief that we had a year ago, where we had almost like a pension holiday last year. Where now we're back to more normal cadence of union pension expenses, and so we're kind of back on our normal case. And I think that's a piece of it.

Again, there were a few other puts and takes around that. But I think that's – when you look at that and if you go – if you did apples-and-apples on that, I think the growth that we have in the first quarter would be similar and approximate what we're seeing for the rest of the quarters.

Ronald L. Sargent
Chairman & interim Chief Executive Officer, The Kroger Co.
A

And Michael, great to talk to you again, great to work with you also. At this point in the year, our 2025 plans are really nailed down. They've been approved by the board. We spend a lot of time in January as a board kind of going through the strategy. And I can assure you at this point that Kroger's go-to-market strategy remains unchanged. We will remain focused on creating long-term shareholder value.

And on a more personal basis, as CEO, I'm going to be focused on making sure our experience and our really talented management teams. And I've really seen that, are able to continue to execute with clarity, with speed and with consistency on those existing strategic objectives.

But Michael, you know me for a long time, I certainly don't plan to be a status quo CEO. But on the other hand, our plans are really solid for 2025. And I'm looking forward to being a part of that.

Michael Lasser
Analyst, UBS Securities LLC
Q

Thank you very much and good luck.

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.
A

Thanks, Michael.

Operator: Thank you. Our next question comes from John Heinbockel of Guggenheim. Your line is now open. Please go ahead.

John Heinbockel
Analyst, Guggenheim Securities LLC

Q

Hey, Todd, couple of things on digital. When you think about growth going forward, particularly in 2025, do you think it ends up being very similar to 2024 in total and in delivery?

And then when you think about improving the losses, what are the biggest buckets or two, right? Is throughput through the sheds, how do you look at that versus delivery density, right? Because I think those are two of the biggest buckets.

And then lastly, right, when do you guys think about you'll be at a place where you want to reaccelerate shed openings from a profit standpoint that you can now go ahead and do that?

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Yeah. Great questions, John, I appreciate that. Yeah, when you look at 2025, we do expect to see continued improvement in 2025. And again, particularly given with the results we saw in the fourth quarter. That's a nice momentum going into the year. And when you really talk about whether it's throughput in the sheds or delivery density, I think, it's a little bit of everything.

We've talked a lot about there are a lot of pieces of that puzzle that we're working to get better. And every single piece of that is contributing. And again, it's what we saw in the fourth quarter. There wasn't one magical thing. It wasn't just cost to serve. It wasn't just the last mile. Every single piece of the puzzle continues to incrementally improve, and that's what we're seeing deliver.

So over time, it's that trajectory. I think, we have several quarters to string together that look like the one that we had. We've talked about sheds, until we get profitability to where we need it and where we expect it to be, one. And two, what comes along with that is making sure that when we open the next shed, we're able to do it at a volume level that kind of enables us to hit the ground running. And I don't think that was always the case when we opened sheds in the past.

And so, the combination of starting in a volume that matters and at a scalable level of profitability based on what we've been able to execute on our existing sheds, I think that will be the point in time when we get there. Again, I don't think – it's not imminent, John, but I think it's something that we have momentum towards and that we continue to work towards. Those will be the key factors that we look at in determining when we open that next shed.

John Heinbockel
Analyst, Guggenheim Securities LLC

Q

Thank you.

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Thanks, John.

Operator: Thank you. Our next question comes from Michael Montani of Evercore ISI. Your line is now open. Please go ahead.

Michael David Montani
Analyst, Evercore ISI

Q

Yes. Hi. Good morning. Just wanted to see if you could unpack a little bit more the ID sales in terms of traffic versus ticket? What kind of inflation did you have in the quarter? And then also on GLP-1, how much of an impact was that on ID sales?

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Great. Thanks, Michael. And I presume – it sounds like you're referencing back to Q4. I think, when we look at Q4 I think we had contribution from both, ticket and traffic, during the quarter. And it might have skewed a little bit towards the ticket side of it because we did have a little bit of a tick up on the inflation side, but I do think both contributed to that.

And GLP-1, I think, we haven't quantified what that looks like relative to GLP-1, but I think there's been some talk about what the industry impacts have been on that. And I think our experience have been very similar to what others have talked about.

Michael David Montani
Analyst, Evercore ISI

Q

Should we be thinking inflation at food at-home levels of close to 2%, absent any more detail?

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Yeah. I think, we talked about in the script, Michael, about 1.5% to 2.5% inflation next year. And if you peel that down maybe one layer, there are certainly some key commodities or categories where you're seeing some outsized inflation. I think, eggs are getting a lot of the headlines, but there's a couple of other fresh categories, maybe beef and some of the other protein categories where you're seeing that.

But really, you take those kind of extreme or outlier inflation commodities, and I think the vast majority of our overall portfolio is pretty steady on inflation. We would expect that, that kind of core of the portfolio to see a little bit of a tick up in inflation for next year. This year played out the way we kind of thought and ended the year a little north of 1%, which is what we thought.

And I think that moving up from there in 2025 is pretty much our expectation, to get to that 1.5% to 2.5%, and then it will just be those outsized categories, I think that maybe pushes more towards the middle of that range.

Operator: Thank you. Our next question comes from Rupesh Parikh of Oppenheimer. Your line is now open. Please go ahead.

Rupesh Parikh
Analyst, Oppenheimer & Co., Inc.

Q

Good morning and thanks for taking my questions. Just on the tariff, I know your guidance or at least for inflation, does include the impacts of tariffs. But since it's starting to happen now, I just wanted to get a sense of exposure there. I'm guessing produce you have some exposure in Mexico, but just any color there. Thank you.

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Yeah. No, great question. Certainly, a hot topic of late, Rupesh, so I appreciate you asking. And you're right. As a domestic retailer, I think we have less exposure to some of the international tariffs that some of our peers will see. You think of China, where we're really, really small single-digit exposure, I think, from some of the things that we buy from China.

One category that maybe has a little bit of exposure in the tariff space is our Fresh business, particularly if you think about produce. But even in that space, when you think about some of the produce we might get from Mexico or Canada, those are still pretty kind of mid-single-digit effect. So, it's not a massive impact.

One thing we are doing though, especially in that Fresh space, in that produce space, we're really – we're closely monitoring that. And where we can, with our merchandising and our sourcing teams are trying to be proactive and looking in those commodities where we have the ability to diversify our supplier base. Maybe to suppliers that are in other geographies that won't be affected by tariffs, they'll be less affected by tariffs, to do what we can in some of those commodities to keep it down. Because being able to do that gives us the opportunity to keep prices low in our stores.

So, the teams are being proactive. Even though it's not a huge impact overall in our business, maybe certainly relative to our peers, it's a great opportunity for us to be proactive and stay out front of it.

Operator: Thank you. Our next question comes from Ed Kelly of Wells Fargo. Your line is now open. Please go ahead.

Edward Kelly
Analyst, Wells Fargo Securities LLC

Q

Yeah. Hi. Good morning, everyone.

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Good morning, Ed.

Edward Kelly
Analyst, Wells Fargo Securities LLC

Q

And, Ron, it's good to hear from you. A couple questions for you, first is related to share repo on the balance sheet. As we've heard from you guys for a while now that there really is no good business reason to run below your leverage target ratio. Ron, I'm curious, do you still agree with that? And then as we think about guidance this year, Todd, what specifically is in guidance this year for share repo, if you could just clarify that, please?

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Yeah.

Edward Kelly
Analyst, Wells Fargo Securities LLC

Q

And then the last – the second question I have for you is just around SNAP and the exposure you have to SNAP and what you've seen historically, if there's been cuts there? Thank you.

Ronald L. Sargent
Chairman & interim Chief Executive Officer, The Kroger Co.

A

Thanks, Ed. I appreciate the question. But given my short tenure with the company, I'm going to defer to my good friend, Todd.

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Yeah. No, you bet. Thanks, Ron. Relative to the guide on the share repo, we obviously have the finalization of the accelerated share repurchase in the plan, which we expect to wrap up in the third quarter. We do have that incremental $2.5 billion authorization on top of that, which we do continue to pick up and execute through open market purchases at the back part of the year.

So, depending on our volumes and presuming that our volumes are consistent with what the repurchases under the ASR are going to be, we expect to use the majority of that, that $2.5 billion, at the back part of the year. So that's the case.

Relative to our leverage ratio, obviously, with the borrowings that we took on for the ASR, we've bumped that up to around 1.8%. It gives us a little bit of flexibility there versus the top end of our range there at the 2.3% to 2.5%. Keep in mind, we do have that $2.5 billion of share repurchase later in the year, that some of that will be dedicated towards using some of the cash that we have on our balance sheet. And we also have a debt refinancing that we'll finance with that. So, we do have some business uses for some of that cash.

Relative to your last comment on SNAP, you're right. It hasn't been that long since I think we had some SNAP pullbacks a few years ago. And typically, when we see the impacts from SNAP in our business and especially coming out of the gate, we'll see the customers prioritize spending on essentials like food initially coming out of the gate, and you'll see more of the reduction in spend in more discretionary categories.

So, as we keep an eye on what's going on in monitoring what's happening in that space, we'll keep that in mind. But as we experienced two or three years ago, when we had the SNAP challenges, we just – we have the ability to flex and pull the levers in our model to make sure we absorb that. But at this stage, there's, I think, a variety of proposals out there on exactly what an impact to SNAP would be, if any. And so, I think, it's premature to project what's going to happen there. But I think, we have our eyes on it and we'll lean on our recent experiences on what that might mean for our business when the time comes.

Operator: Thank you. Our next question comes from Ken Goldman of JPMorgan. Your line is now open. Please go ahead.

Kenneth Goldman
Analyst, JPMorgan Securities LLC

Q

Hi. Thank you. I appreciate the guidance on inflation and the details there. I wanted to broaden it out a little bit. As we look just at food at home and retail and wholesale pricing trends, CPI and PPI. It certainly seems to some observers that the industry, the food retail industry is holding back on maybe passing through some of the wholesale inflation. I realize that PPI is not a pure measure of wholesale prices.

But I was just wondering what you guys are seeing out there in terms of the competitive environment, your peers price investments versus your expectations and how that kind of informs your decisions to pass along inflation this year?

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Yeah. Good question, Ken. Couple of thoughts. Relative to most of our suppliers, we're not seeing a ton of price increases come through yet. I think, maybe we have seen some select price increases, particularly, again, as I alluded to earlier, in some of the Fresh categories that you would expect, like eggs and, again, a couple of the proteins we have seen that. But by and large, across the broad portfolio, we're not seeing or hearing a lot of chatter about those price increases at this stage.

So, and that's reflected in some of the thoughts that we gave relative to our inflation guidance and whatnot for later in the year. As far as, again, relative price investments and whatnot, it's a great question. I mean, the way that customers are thinking about value, we talked about that earlier, competitive pricing is as important today as it's ever been. And you've heard us say before, we always assume the next quarter and the next year is going to be more competitive than the last because that's typically the way that it plays out.

But we do continue to monitor where our pricing is at relative to our competitors and where those gaps are at because we're always striving to keep our prices low. We had nice progress in the fourth quarter. We did improve our gaps with our competitors in the fourth quarter and we continue to monitor that and our strategy is to continue to drive those investments in price to narrow those gaps. So, I think, we've had nice momentum in that space over the past couple of quarters.

Operator: Thank you. Our next question comes from Karen Short of Melius Research. Your line is now open. Please go ahead.

Karen Short
Analyst, Melius Research LLC

Q

Hi. Thanks for taking my question and good to speak to you. So just on that last comment, I wanted to clarify where you think your price gaps are now versus where they were, say, 10 years ago. Because in the Kroger heydays, you were within 5% to 8% of your largest big box competitor on like-for-like items.

And then, my second question is just when you look at your operating profit, and obviously, we can see the contribution from alternative streams, how do you think about the four-wall operating profit? And I know, it's getting increasingly hard to separate the two. But four-wall operating profit versus the alternative because four-wall obviously needs to grow as does the alternatives.

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Yeah. Thanks, Karen, great questions. On the first, relative to price gaps, we measure it at two or three different levels. There's obviously like the prices gaps that are observable by looking at shelf tags. And let me even take a step back from that. My comments around being able to narrow those price gaps that I just made applies to each of the scenarios that I'll describe.

But we look at it at that level, at the shelf tag level, for what the customer will see looking at the shelf. But the other one that we look at because of our promotional offerings, our loyalty offerings, our fuel rewards, we'll look at kind of that all-in price that our customers get total value from Kroger.

And what we see when you look at that all-in level, it's favorable to the 5% to 8% range that you used earlier. So, we continue to look at that and look at it on an all-in level and measure how we're able to continue to reduce that gap.

One of the things that we're paying attention to there is, that's based on our measurements and what we see. But we continue to work and make sure that our customers and what our customers perceive our values are and our price spreads are more closely matches to what that actual value is.

And I think, we've got some feedback. I think, we have some opportunity there from our customers. So really trying to focus on being a little bit more simpler in the promotions that we put out there. So, it's very clear to them and they give us the credit for the value that we deliver to them to make sure that they understand that. So that's an important part of what we're doing today.

And then relative to operating profit, great question on four-wall and – versus operating profit, and a very astute observation that they do – they are very intertwined, especially the way that we operate our model. But I think that we see growth in both of those. And I think it's a pretty even balance when you think about – when we look at our operating profit growth, both are contributing, I think, in a reasonably similar range to our overall operating profit growth, particularly as we look at 2025.

Operator: Thank you. Our next question comes from Chuck Cerankosky of Northcoast Research. Your line is now open. Please go ahead.

Chuck Cerankosky
Analyst, Northcoast Research Partners LLC

Q

Good morning, everyone.

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Good morning, Chuck.

Chuck Cerankosky
Analyst, Northcoast Research Partners LLC

Q

Can you talk a little bit about accelerating your new store openings? The conventional retail food industry has lost market share over the last few years, but Kroger is definitely something more aggressive than the rest of the industry. And can you talk about the strategic thoughts behind that, please?

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Yeah. No, great, great, good color, Chuck. One of the reasons as we think about – there's a couple pieces of that. One, three or four years ago, as we were ramping up our digital capabilities, some of our incremental capital went into building out those capabilities to get them where we are today. And we're pretty happy with how that's played out. So we're not done with that. We're in continual enhancement mode and maintenance mode to make sure we're delivering where the customers are at.

But now that we've got to that mode, we're able to take that incremental capital and put it back into our store. Because I think that's an area where when you look at some of our share and our opportunity for growth, I think building out that footprint is an important piece of what we're trying to do. So, we talked about where we're at this year, where we expect to be next year and accelerating off of that.

The two of those comments go hand-in-hand. Because more and more, our most loyal customers and our most profitable customers are the ones that engage with us in both modalities, those that engage with us digitally – and those that – and they also engage with us in store. And so having the right balance between the two of those, I think, gives us an opportunity to build loyalty with our customers. But I also think having those additional – that additional physical footprint is a great lever for us to drive our share.

So, the two go hand-in-hand, digital and physical footprint. But because we took a couple of years off there from some of that growth, I think it's an opportunity to get back in and build that out.

Operator: Thank you. Our next question comes from Krisztina Katai of Deutsche Bank. Your line is now open. Please go ahead.

Krisztina Katai
Analyst, Deutsche Bank Securities, Inc.

Q

Hi. Good morning. Thanks, and congrats on a good quarter. So, I had a question regarding Own Brands, you launched more than 900 new items in 2024. Can you talk about your plans for the Own Brand business in 2025? How much newness should we anticipate for the year? What does that distribution look like across maybe opening price points versus your more premium items? And then just lastly, how do you anticipate that they will continue to contribute to gross margin in 2025? Thank you.

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Yeah, great question. We've talked a lot about Our Brands this year. Again, it's been a staple in what we go-to-market with because it hits so many sweet spots. It delivers great quality at a value to our customers. And especially in this environment, that's huge. It's a margin enhancement mechanism for us because of the spread with national brands on all of those and it gives us a point of differentiation, and distinction with the innovation being able to give our customers something they can't get anywhere else. So, it's kind of the ultimate triple play relative to Our Brands.

And so, because of that, we talk about the 900 items this year. I don't recall what 2023 was, but I believe it was a similar number. This year was not an unusual year for innovation and new items in Our Brands. So, I would expect to see us continue to innovate in that space.

And again, when you talk about how much of that newness comes from opening price point or Private Selection or those kind of things, our team does and continues to do deep dives in each category, because each category is a little bit different. But to make sure we understand where we stack up against national brands and where there's substitutability or replaceability relative to national brands where Our Brands might be able to be featured.

So, it's hard to answer that specifically other than to say we've been doing these deep dives in on a category-by-category basis, really trying to understand where we need an opening price point or where we can introduce innovation in Private Selection.

And we're probably maybe a third or 40% of the way through those category deep dives. I expect those to extend through 2025 and beyond to be able to drive that growth. But I think it will be an important pillar of what we do for years to come.

And I even think we see opportunity in the right categories to really push to expand our penetration in those categories over time. So, it's a story you'll continue to hear us talk about.

Operator: Thank you. Our next question comes from Joe Feldman of Telsey Advisory Group. Your line is now open. Please go ahead.

Joseph Isaac Feldman
Analyst, Telsey Advisory Group LLC

Q

Yeah. Thanks guys for taking some questions. I wanted to ask about – is there anything – you mentioned the pension issue being in the first quarter. Can you share a little more color on that for the rest of the year?

And are there any other like big pensions this year that you do have to negotiate? I feel like every year, there's always one or two that come up? And I just wanted a little more color on that. Thanks.

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Yeah. Sure, Joe. Yeah, I wouldn't even call it a pension issue. Actually, it was an opportunity from last year, where based on contributions that we have made up to that point in time, we didn't have the need to make required contributions for an early part of last year. So last year, we didn't have contributions.

And now we're kind of back on our normal cadence. And so that's just created that Q1 comp that was a little bit different than what we expect to see for the remaining quarters of the year. So, it was just – it was a – it's actually an opportunity from last year as opposed to a concern or an issue.

Operator: Thank you. Our next question comes from Kelly Bania of BMO. Your line is now open. Please go ahead.

Kelly Bania
Analyst, BMO Capital Markets Corp.

Q

Hi. Thanks for taking my question. I had a couple. I wanted to ask just about your core kind of underlying gross margin. It's had a pretty solid expansion really for the last few years. I think, this quarter and this year even came in ahead of plan, but it sounded like this year is planned flat.

So just curious if you could talk about what may be different about this year versus the last couple years? And I guess, if you can incorporate kind of your plans for your alt profit growth, sorry, if I missed that, but what you're planning on that for this year?

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Yeah. Good question. I think, when you look net of Specialty Pharma for this quarter, I think, it was about 13 basis points ahead. So, it was a little bit ahead in the quarter, and I think that was – that, too, was reflective of the year. I think, what we saw this year – which was good.

We've been doing a lot of work in the shrink space this year. And because we've talked for years the pressure with organized crime and some of the other issues that we've had from a macro space and the shrink space.

So this year was a year where a lot of our efforts in that space have really paid off not only in strategies around organized retail crime, but you heard us talk in the prepared script about the way we're using technology to drive sell-through and help us reduce shrink.

And so I really think – the answer to your question on why was this year such a benefit to budget? I think shrink was one of those. We've talked a lot about Our Brands and whatnot. I still think we have a little bit of run rate in the shrink space, but I think we'll probably start to cycle that as we get into the middle of the year and whatnot. And we continue to invest in price and whatnot.

And we use those margin expansion opportunities to continue to invest in price there. And then the second part of the question did I – I might have missed. I didn't catch the second part of the question.

Ronald L. Sargent
Chairman & interim Chief Executive Officer, The Kroger Co.

A

Alt profit growth.

Todd A. Foley
Interim Chief Financial Officer, The Kroger Co.

A

Oh, sorry, and the alt profit growth. Yeah. We don't specifically guide to alt profit, but we do expect 2025 to see dollar growth better than what we had come through in 2024.

Operator: Thank you. At this time, we'll take no further questions. I'll hand back to Ron for any further remarks.

Ronald L. Sargent
Chairman & interim Chief Executive Officer, The Kroger Co.

Okay. Thank you, Alex. Thanks for all your questions this morning. They're really much appreciated and it's also great for me personally to reconnect with some old friends this morning.

As you know, before we conclude our earnings call, we'd like to take the time to share just a few comments with our associates who are listening in. I'd first like to send the message of encouragement to all of our associates. As CEO, I will keep our company focused on retail fundamentals, running great stores and online delivery, while taking great care of our customers.

Kroger is steady, because of you. The work you do everyday matters. And it is what makes the customers coming back and makes Kroger the place they trust. Kroger is strong, and we have great momentum going into 2025.

Thanks, everybody, for joining us today. It's great to be back home. And I look forward to our future together.

Operator: Thank you all for joining today's call. You may now disconnect your lines.