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Kenvue, Inc. (KVUE)

Q2 2024 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Hello and welcome to the Kenvue Second Quarter 2024 Earnings Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions] As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, Jim Giannakouros, Interim Head of Investor Relations for Kenvue.

Jim Giannakouros

Interim Head-Investor Relations, Kenvue, Inc.

Good morning, everyone, and welcome to Kenvue's second quarter 2024 earnings conference call. I'm pleased to be joined today by Thibaut Mongon, Kenvue's Chief Executive Officer; and Paul Ruh, our Chief Financial Officer.

Before we get started, I'd like to remind you that today's call includes forward-looking statements regarding, among other things, our operating and financial performance, market opportunities and growth. These statements represent our current beliefs or expectations about future events and are subject to various risks, uncertainties and assumptions that could cause our actual results to differ materially. For information regarding these risks and uncertainties, please refer to our earnings materials related to this call posted on our website and our filings with the SEC.

During this call, we will reference certain non-GAAP financial information. The presentation of this non-GAAP financial information is not intended to be considered in isolation or as a substitute for financial information presented in accordance with US GAAP. These non-GAAP financial measures should be viewed in conjunction

with the most comparable GAAP financial measures. A reconciliation of these items to their respected nearest US GAAP measure can be found in this morning's earnings press release and our presentation available on our IR website, investors.kenvue.com.

With that, I'll turn it over to Thibaut.

Thibaut Mongon

Chief Executive Officer & Director, Kenvue, Inc.

Thank you, Jim, and thank you to everyone for joining us today. This quarter, we made good progress against our strategy. We drove year-over-year organic growth of 1.5% on top of 7.7% organic growth last year and improved adjusted gross profit margin by 410 basis points to 61.6%. This huge investment in our brands, while not impacting our ability to deliver EPS as per guidance. With our first and second quarter performance, we are on track to deliver our year as we continue to execute our new strategy as an independent company. Earlier this year, I committed to you that you would see a new Kenvue, a bolder company that is moving quickly to advance all three priorities to reach more consumers effectively, invest further behind our brands, and build a culture of performance and impact.

Our first half results shows the value of our pure play model, with a carefully curated portfolio covering a full spectrum of consumer health needs with iconic brands. While still early days, our results demonstrate that our transformation efforts are beginning to drive our intended impact. These efforts include our work to improve productivity and reduce cost. We expect to deliver approximately 150 basis points of adjusted gross profit margin expansion in 2024, higher than we anticipated coming into the year as we drive greater value realization from favorable mix and stronger efficiencies in operations. In addition, we are actively reducing our cost structure through rigorous expense management and the on track execution of Our Vue Forward, our program to become a leaner, more agile and fast moving organization with a lower cost base.

Our significant progress on productivity gives us more strategic flexibility. We have now chosen to invest approximately 20% more behind our brands this year than we did last year, advancing our priority to free up resources to invest more behind our brands to drive future growth. We are targeting our investment [ph] toward (00:04:08) high yield strategies such as healthcare professional engagement, in-store prominence, and direct consumer engagement with an increasing focus on innovation and influences. This both strengthens loyalty among our existing consumers and expand our reach to new consumers, and we are beginning to see the impact on our brands across our portfolio. Core to our transformation is the culture we are building, while driving a heightened sense of accountability across the organization that is surely speeding execution to drive profitable growth.

In summary, halfway through our first full year as an independent company, we are on track to deliver our financial goals for 2024. In addition, while we would expect to continue to operate in a volatile environment, our progress to-date and our plans for the back half bolster our confidence to deliver on our long term value creation algorithm, targeting attractive total shareholder return in 2025 and beyond.

Now, looking at the key highlights of our performance this quarter, we have started to see the early impact of our work on our three priorities. After a slow start in allergy and sun earlier in the quarter, we saw a positive shift in US consumption in the month of June. This immediately translated to shipments due to the strength of our brands being top of mind for consumers and our ability to replenish low levels of retail inventory with agility.

In Self Care, organic growth was essentially flat year-over-year on top of 14.2% growth last year, which beat our internal expectations. Once again, we outperformed the market globally this quarter, having now maintained or

grown share every quarter for the last two years. Tylenol, the number one brand in pain relief globally, delivered its eighth consecutive quarter of share growth in the US, further widening the gap versus our closest competitor in both value and volume. Our consumer-centric innovations, including Tylenol Easy to Swallow, designed for those who hesitate to take a pill, benefited from our increased investments to reach more healthcare professionals and consumers and we expanded in-store presence and prominence.

In allergy, sales accelerated in June after a slow start to the spring season in the US. Kenvue is now the number one and fastest growing manufacturer in the allergy category in the US with our brands Zyrtec and Benadryl gaining share in value and volume. This growth has been driven in part by our expanded in-store presence and increased media to amplify innovation like Zyrtec Oral Dissolve Tablets.

Essential Health continued to perform well, with broad-based organic growth of 7.6% in the quarter, on top of 3.8% in the same period last year, and balanced growth between value realization and volume. Notably, Listerine grew approximately 10% globally. Listerine is another good example of how increased investment in the right areas drives returns. While the brand has historically been powered by our number one recommendation with dentist and strong clinical superiority, we are strengthening marketing spend to create higher visibility with consumers through digital media, influencers and in-store prominence, driving new consumers to the category. We are also amplifying high performing innovation, including Listerine Clinical Solutions, our new premium line in which each product is tailored to specific all health needs. As a result, Clinical Solutions is the number one mouthwash line innovation in the US today.

Our Skin Health and Beauty segment performed in line with our expectations in this first phase of our recovery plan. Organic growth declined 2.4% year-over-year, following the 3.4% organic growth in the second quarter last year. This is an improvement sequentially, and while this is a journey, we are on track to stabilize the business. Europe continues to perform well with the successful expansion of Aveeno and Neutrogena in the UK, Germany and Southern Europe. The teams are executing with excellence in store, with a significant increase in shelf presence through compelling brand blocks.

In China, the category continues to be soft and evolving consumer preferences are proving to be challenging for Dr.Ci:Labo brand, contributing to the impairment of assets we described in our press release. In the US, which is our priority, we continue to activate our plans to stabilize the business this year with expectations to resume consumption growth next year. As we've shared with you previously, we are working diligently to improve our in-store presence and prominence, increasing the number of our displays to augment growth. We activated our strategy this sun season, and as a result, Neutrogena confirmed its number one position and gained share into seasonal segments with our Ultra Sheer and Beach Defense lines.

We are also elevating healthcare professional and consumer engagements. We have doubled the size of our detailing salesforce and significantly increased our sampling efforts with dermatologists, already resulting in an increased share of dermatologist recommendations. And on social media, Neutrogena is making a strong pivot to reach Gen-Z consumers through influencers, partnering with Alix Earle or gold medalist Sydney McLaughlin-Levrone, to launch engaging content on social media. I hope you will join us in sharing [indiscernible] (00:09:50) during the 400 meter hurdle this week.

And we are amplifying innovation as well. For example, we are launching Neutrogena Collagen Bank in the US, the brand new pre-aging platform with a patented peptide technology developed with dermatologists to penetrate more than 10 layers deep within your skin. This innovation received 100% acceptance by our top retailers. To build demand before products arrive in store, Collagen Bank first launched on TikTok Shop, the first for Neutrogena. This approach generated tremendous buzz online and motivated one of our major customers to push

forward their retail launch. So, while we are in the early days of our journey, we are focused on executing our plan with precision, strengthened capabilities and increased investments across our portfolio.

A few final remarks on other areas where we are making progress as an independent company before I hand it over to Paul. First, I hope you all had a chance to read our inaugural Healthy Lives Mission Report, which we published in June. The report outlines our ESG strategy, goals and progress, and there is a lot we are proud of in year one. You may also have seen last week that we announced the implementation of a board succession process following the sale of J&J's stake earlier this year. The appointment of Kathy Pawlus and Kirk Perry as two new independent directors coincides with Joe Wolk and Peter Fasolo stepping down by the end of this year. I would like to express my deep gratitude for Joe and Peter's contributions to Kenvue as we executed a successful transition to become an independent company and welcome Kathy and Kirk, whose deep experience, expertise and capabilities will be valuable additions to the board.

Additionally, as an independent company with a deep commitment to shareholder value creation, we were pleased to announce earlier in July the board declaration of our first dividend increase. This is a testament to our strong balance sheet and cash generating capabilities, which will only improve as we continue our journey as Kenvue. All our efforts would not be possible without the performance of our people. I would like to thank Kenvuers around the world for leading a new culture and for their commitment to driving results this quarter again, demonstrating the power of Kenvue in action.

With that, I will turn it over to Paul.

Paul Ruh

Chief Financial Officer, Kenvue, Inc.

Thank you, Thibaut. And good morning, everyone. Overall, our Q2 performance came in ahead of our mid-quarter expectations, with strong sales in June and greater benefits from productivity and mix, generating higher than expected gross profit margin expansion. As a result, we have made the strategic decision to further increase our marketing spend. This strengthens Kenvue position to deliver our long-term value creation algorithm and does not impact our ability to deliver our EPS guidance for 2024.

Moving into more details. Second quarter organic growth was 1.5%, primarily driven by value realization across all segments and volume growth in Essential Health, partially offset by low single digit volume declines in both Self Care and Skin Health and Beauty. Value realization contributed 2.1% to growth, benefiting mostly from carryover and incremental pricing actions. While we expect volume to increasingly contribute to sales growth from here, value realization will continue to be an important part of our value creation algorithm. Volume was down 0.6% year-over-year, with sequential improvement during the quarter on the back of greater Essential Health performance, continued overall share gains in Self Care and steady progression toward stabilizing Skin Health and Beauty.

Now, let's take a look at our segments. Self Care organic growth was essentially flat on top of [ph] meeting its (00:13:53) growth last year, with continued share gains across the segment. Value realization contributed 1.1% of growth in the quarter, driven by both carryover and incremental pricing actions. This was offset by volume down 1.3% due to a shorter cough, colds and flu season versus last year. We entered the second quarter of 2024 experiencing a slow start to the allergy season and observing a continuation of tight inventory controls in retail through May. However, demand for allergy accelerated in June and we activated our Zyrtec and Benadryl brands successfully and gained share. Smoking cessation also had a strong quarter overall. So, as you heard from Thibaut, the segment continues to do very well, outgrowing the market and strengthening our leadership positions.

Moving to Skin Health and Beauty, organic growth decreased 2.4%, with 3.9% of volume decline, partially offset by 1.5% of positive value realization, driven by mix and carryover pricing. In the first phase of our recovery plan, we see signs of improvement as Skin Health and Beauty second quarter year-over-year volume trend sequentially improved 300 basis points from the first quarter.

For Essential Health, the segment had strong organic growth of 7.6%, with 4.1% of value realization and 3.5% of volume growth. Carryover pricing, primarily North America, and to a lesser extent, new pricing outside the US, drove value realization. Essential Health grew across all categories and all geographic regions. An effective combination of relevant innovation and increased marketing drove the volume gains.

Moving to adjusted gross profit margins, in the quarter adjusted gross profit margin improved 410 basis points, largely driven by supply chain efficiency gains, which includes favorable commodity costs and also value realization. Given our performance to date, we now expect full year 2024 gross margin to be closer to 60% or expand approximately 150 basis points versus last year. We are encouraged by the pace of improvements made by our supply chain and revenue growth management teams. The same teams are creating the building blocks to deliver continued gross margin expansion over the next several years. For modeling purposes adjusted gross profit margin is typically highest in Q2 and declines in the back half, with Q4 being the lowest due to annual planned maintenance. This year, lower value realization and progressively lower commodity inflation benefits are expected to accentuate this trend.

Now, on to adjusted operating income margin, which was 22.8% in the second quarter. A strong delivery of gross margin expansion, benefits of cost controls, as well as our confidence in the strength of our back half plans, enable us to further increase our brand investment by up to \$100 million this year. This advances our priority to further invest behind our brands, getting us closer to competitive levels without compromising our ability to deliver on EPS. As a reminder, this increased investment will be reflected in our advertising, consumer and product promotion, and healthcare professional spend. With regards to modeling the back half, we anticipate the combination of lower gross margins and increased spend will result in operating margin being down sequentially versus the high watermark set in the second quarter. And for the full year, we now expect adjusted operating margin to be in the range of 21% to 22% with no impact to our EPS delivery. We believe this is the right time to accelerate these investments, building on the momentum we are seeing to bolster our ability to deliver on our long term algorithm.

To close out the P&L, interest expense net for the quarter was \$92 million. Given our year to date net interest expense, we now expect it to be in the range of \$380 million to \$400 million for the full year 2024. For taxes, the second quarter adjusted effective tax rate was 25.7%. Regarding other income and expenses, in the quarter, we incurred a non-cash after tax charge of \$337 million to adjust the carrying value of long lived assets related to the Dr.Ci:Labo business. The impairment was a result of updates in our strategy to reach more consumers and appropriately address evolving market dynamics, including shifts in consumer sentiment in China, as well as changing shopping patterns in the region. We continue to believe in the strength of the brand and are actively investing in its long term opportunities. And finally, adjusted net income was \$611 million for the quarter and adjusted diluted earnings per share was \$0.32.

Moving to capital allocation, the quarter reflects our balanced approach. Our first priority is investing in the business, both in our brands and our operations with Our Vue Forward. As a reminder, Our Vue Forward includes a multi-year program of rebalancing our resources to improve our agility and speed, better positioning us for the future with a more efficient cost base. Our initiatives are tracking on plan with associated spending tracking to approximately \$275 million this year and we plan to maintain similar spending levels for 2025. By 2026, we expect

to have generated \$350 million in savings, or better stated, resources reallocated to future growth investment. In addition, we are committed to returning cash to our shareholders. In July, we announced our first increase in our dividend as a public company and intend to continue to deliver attractive dividends to our shareholders over the long run.

Now, to summarize our expectations for 2024, we are increasingly confident in our ability to deliver within the sales and EPS outlook ranges set at the beginning of the year. This includes organic growth expectations in the 2% to 4% range and adjusted EPS of \$1.10 to \$1.20. For the full year we expect foreign exchange to be a 1% headwind, also unchanged from prior guidance.

Thank you. And with that, we will take your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. At this time, we'll be conducting a question-and-answer session. [Operator Instructions] Our first question comes from the line of Anna Lizzul with Bank of America. Please proceed with your question.

Anna Lizzul

Analyst, BofA Securities, Inc.

Q

Hi. Good morning. Thank you so much for the question. I was wondering if you could elaborate on the new pricing actions that you mentioned in terms of the depth and the categories in which you took pricing. And then on volumes, the declines improved sequentially in Skin Health this quarter, so I was wondering if you could give us more detail on your expectations for the back half and how the innovation pipeline is shaping up here. Thank you.

Thibaut Mongon

Chief Executive Officer & Director, Kenvue, Inc.

A

Yes. Good morning Anna, thank you for your question. Regarding your first question on value realization, it's really the combination of carryover pricing, new pricing, as you stated, and mix. Regarding new price actions, remember that our philosophy at Kenvue is to offset inflation and FX conditions with pricing, so typically we take these price actions in markets in categories where we still see inflation and FX impact. We expect value realization to continue to be part of our value creation algorithm, but as the year continues, you will see less and less impact of carryover pricing and you will see more impact of mix and new pricing actions.

In terms of your question on the sequential improvement in volume for our Skin Health segment, we are pleased with the early signs of impact of the recovery plan we have put in place since the beginning of the year. I'm encouraged with these early signs. As you said, we see a sequential improvement from Q1 to Q2 in terms of year-over-year trends. We are reaching more consumers and HCPs successfully. We saw an increase in household penetration for Neutrogena in the US, particularly with millennials and Hispanics, which is encouraging, and we have strong building blocks for the back half. So, we are executing a thoughtful plan. This will be a journey, but I'm encouraged with what we have seen so far.

Operator: Thank you. Our next question comes from the line of Stephen Powers with Deutsche Bank. Please proceed with your question.

Stephen Powers

Analyst, Deutsche Bank Securities, Inc.



Hey, guys. Good morning. Thank you. I want to ask on the 20% aggregate increase in spending behind your brands that you call out this year. I'm curious as to how much of that has already been deployed versus is something that you're targeting to come in the second half.

And then, I guess, as you contemplate that 20% increase, where does that bring you relative to what you view as kind of the optimized level of aggregate brand support? It sounds like from Vue Forward contemplation, we should expect more investment in the years to come. But I'm just – I guess, I'm curious as to where you think you are today relative to what is ultimately optimal. Thank you.

Paul Ruh

Chief Financial Officer, Kenvue, Inc.



Thank you, Steve. Let me take the first part of your question, which is about the 20% marketing spend. We started the year with a 15% year-over-year increase. Remember, it was \$300 million that we talked about. As we have seen the acceleration of initiatives take hold and we have seen the benefits of gross margin enhancement, now we feel more confident in investing 20% more instead of 15% more so we added another \$100 million that we are starting to deploy as of Q2 and going forward. We believe that this is a step in the right direction. And as we continue to see efficiencies in our gross profit margin and we continue to see the benefits of Our Vue Forward programs, we will continue to invest more. That will not only happen in 2024, but we are preparing the building blocks along those lines into 2025 and beyond. Thibaut, do you want to comment where are we going and how far?

Thibaut Mongon

Chief Executive Officer & Director, Kenvue, Inc.



Yeah. Steve, as you can tell, we are getting closer to industry standard faster than we anticipated. Having said that, as you heard from Paul, we'll continue to invest. One of the reality of the consumer health space is that we are talking about categories that are underpenetrated and where we have many opportunities to expand usage occasions. So, as long as we see opportunities to do that, we will raise our investment level. We have many consumers to talk to and to recruit into a portfolio with our innovation for many years to come. Having said that, we'll continue to do that with discipline, always with an eye on strong return on investment. But as long as we see strong returns on our investments, we will continue to free up resources to invest behind our brands and reach more consumers.

Operator: Thank you. Our next question comes from the line of Andrea Teixeira with JPMorgan. Please proceed with your question.

Andrea Teixeira

Analyst, JPMorgan Securities LLC



Hi. Good morning to all and thank you for the question. Thibaut, you mentioned that the Skin Health and Beauty division delivered according to expectations and is on track for the plan in the year. Would that imply a positive inflection in organic sales growth? I mean, more specifically, I know, to a previous question, you were very positive about that support and the innovation that is coming online. But I think investors wanted to see some sort of like reassurance into the second half. Understandably, you have much easier comps and good set-ups on, as you mentioned before, a lot of sales force improvement there as well.

And then related to the comments about the retail destocking and thinking about Self Care as well, is there any update on that in particular? I understand it's mostly into the US, but if you can, given that your business is a lot international, we are focusing a lot in the US right now. But if you have half of your business outside the US, so wondering if you can comment on how you're seeing Europe, how you're seeing Asia and across the board in Self Care. Thank you.

Thibaut Mongon

Chief Executive Officer & Director, Kenvue, Inc.

A

Yeah. Let me start with the second one very quickly. Andrea, we saw some destocking happening in the US in the first half. We mentioned at the beginning of the year that it impacted Q1. It would continue to impact Q2. That's what happened. And we've seen these levels stabilizing and we don't expect further impact in the back half of the year as we communicated earlier in the year. Outside of the US, we see healthy levels of inventory and don't expect any major movement in that area.

On your question on Skin Health and Beauty, it's really the early stage in our recovery plan in the US. As I said, I'm encouraged with what I see. I see that our US team is executing with precision the plan that they outlined at the beginning of the year. We are on track to stabilize the business in 2024. We see volumes continue to improve sequentially as we get into the back half of the year as we continue to increase our presence and our prominence in-store with more displays. I gave you the example of the sun season. You will see similar activity in the back half, but also how we reach and engage with dermatologists and consumers in a bigger way, amplifying innovation, especially on social media, with influencers. So, we will continue to execute this plan. It will not happen overnight, but we will see sequential improvement as the year unfolds.

Operator: Thank you. Our next question comes from the line of Nik Modi with RBC Capital Markets. Please proceed with your question.

Nik Modi

Analyst, RBC Capital Markets LLC

Q

Yeah. Thank you. Good morning, everyone. I guess two questions on the beauty business, Skin Health and Beauty business. Maybe we could get an update on leadership, any progress there. And then, the second question is just, I'm hearing a lot of tactical initiatives in terms of improving the business, more spending, more displays. But Thibaut, I was hoping you can maybe talk about the brands themselves in terms of the architecture of the brands, SKU rationalization that needs to happen to kind of streamline and kind of make it less of a confusing line-up. Any perspective around that would be helpful. Just kind of understand kind of the core dynamics of that, that you need to do to really get this business to turn around. Thank you.

Thibaut Mongon

Chief Executive Officer & Director, Kenvue, Inc.

A

Yeah, Nik, great question. So, on the leadership, we are making progress to fill the segment leadership position, so we will inform you when we are ready to do so. In the meantime, things are happening fast and furious within Kenvue. Our Chief Growth Officer, Charmaine England, is leading the segment in interim and making great progress there. I talked about how the US team is focused on execution, the same thing outside the US. So, the entire team around the world is mobilized to execute with precision against all three priorities, and that includes Skin Health and Beauty, and you start seeing the impact of their work.

Now, talking about your second question on our brands, our focus is on making sure that our brands are more relevant every day and reach more consumers in multiple ways. And that's why we are so focused on executing

with precision, making sure that we reach more consumers with social media and influencers, we reach more dermatologists, so they can recommend the brand more. Through these activities, we are not only reaching more consumers, but we are more relevant.

This is also the case with innovation. Innovation is, every time we launch a new product, and Collagen Bank is a good example, it's an opportunity for a brand like Neutrogena to advance its relevance with our target audience and demonstrate our superiority. So, our brands are strong, highly penetrated. I talked about the improvement we have seen in the first half in household penetration for Neutrogena in the US, which is great. We are focused on improving the relevance of our brands and innovation plays a big role there.

Operator: Thank you. Our next question comes from the line of Filippo Falorni with Citi. Please proceed with your question.

Filippo Falorni

Analyst, Citigroup Global Markets, Inc.

Q

Hi. Good morning, everyone. Thanks for taking the question. So, I wanted to ask about the Essential Health business. It's been an area of strength in your portfolio. Maybe, what drove the strength in the quarter, bigger improvement in volume growth compared to Q1? Maybe you can elaborate on that and some of the expectations into the second half for Essential Health. And then, a second question, I have a quick follow-up on the Skin Health and Beauty business, maybe you can comment about the China portion of the business, what you saw in the quarter, what are your expectations in the second half. Thank you.

Thibaut Mongon

Chief Executive Officer & Director, Kenvue, Inc.

A

Okay. Filippo, good morning. So, let me start with your question on Essential Health. We are pleased with the performance of the Essential Health segments. Strong quarter two, strong first half, broad-based growth across every region and every category on top of growth last year. Also balanced growth between value and volume. We talked about the very strong performance of Listerine, growing double digit. When you see that this brand is a global brand, more than five times bigger than our next competitor, it's a very strong showing. But we have similar momentum going on across the segments with strong innovation. We launched BAND-AID Pro Heel in the US, which is up to a good start. We talked last quarter about Aveeno Kids in the US, which is our expansion from babies into kids to grow the category. This continues to do extremely well. We are also doing very well with our premium Stayfree napkins in India.

So, really, the theme for us across Essential Health is to expand the category, to bring new users to the category, to give them the very strong leadership positions we have in each of the category in which we compete. And that's what you see happening across the portfolio this quarter and the first half. Longer term, that's what we intend to continue to do, driving category growth. We have a lot of room to grow in these directions, bringing new users in the category with solutions that help them take better care of their health. And that's what we intend to do moving forward.

On the second question regarding China, China is a positive contributor to our growth in Q2 and we expect it to continue to be the case in 2024. Remember that the majority of our business in China is in Self Care, with very strong position in allergy, analgesics, antifungals, pediatrics and we continue to see Chinese consumers looking for science-based efficacious solutions in the Self Care space and we are extremely well positioned to respond to this increasing demand. So, we remain committed to the China market from this perspective and would expect China to continue to be the positive contributor to our growth.

Then we have a small part of our business that is in the other segments. And here, as everybody else, we see in the Skin Health part that you mentioned, the soft category, the consumer is more cautious. You have evolving consumer preferences, and that's an area where we are more cautious in our investment. Having said that, it's an area where we see the beauty of our model and the strength of our portfolio. While we see Dr.Ci:Labo, a brand of Japanese origin being negatively impacted this year, we see a very strong demand and very strong growth for our local Chinese brand called Dabao. And so that's where you see the beauty of the portfolio, where multiple brands allow us to cater to the different needs of different consumers.

Operator: Thank you. Our next question comes from the line of Susan Anderson with Canaccord Genuity. Please proceed with your question.

Susan Anderson

Analyst, Canaccord Genuity LLC

Q

Hi. Good morning. Thanks for taking my question. I was wondering if maybe you could give some more color just on the promotional environment, particularly in the US. I think both Walmart and Target have talked about lowering prices. I know the drugstore channel has been tough. So, I'm just curious if you're really seeing it across all of your categories. And then also, how much have you put into the gross margin for the back half of the year? Thank you.

Thibaut Mongon

Chief Executive Officer & Director, Kenvue, Inc.

A

Okay. I'll start with telling you a little bit about what we see with the consumer, and then I will let Paul answer your question on gross margin in the back half of the year. So, when we look at the consumers in the US, and frankly, around the world, we see that consumers continue to be thoughtful and choiceful on where they make trade-offs. One area where they are not making trade-offs is their health and the health of their loved ones. They are – we see consumers, I would say, increasingly prioritizing their health and the health of their family.

We have in our portfolio different price points and different brands to meet them where they are and cater to the different needs of different consumers. But we see that in consumer health, consumers are willing to pay a premium for brands that are science backed and recommended by their doctors and brought to them by brands they trust, and that's what Kenvue is all about. So, in my prepared remarks, I talked about Tylenol Easy to Swallow or Listerine Clinical Solutions. I just talked about BAND-AID Pro Heel. These are all premium solutions that are 10%, 15%, 20% more expensive under base offering, and they are extremely well received by consumers. Why? Because they bring an efficacious solution to real need for consumers. We are not in the impulse buying categories at Kenvue. We are providing efficacious solutions to respond to the needs of our consumers.

Another data point that I would give you is that we don't see a change in the penetration of private label in our categories in the US and around the world. If I take the US Self Care category, which is probably one of the most penetrated categories we have in terms of private label, the private label penetration is down so far this year. So, we don't see in our categories and at Kenvue what you see in other categories. Having said that, we don't take it for granted and our teams work very hard every day to make sure that we understand our consumers, are close to our consumers, and bring them the data, the solutions, the products, the brands they trust and they need to take care of their health.

Paul Ruh

Chief Financial Officer, Kenvue, Inc.

A

Thank you, Thibaut. Let me talk about a couple of things, promotional intensity, promotional environment in the US, and the potential impact that has on the gross margins. So, promotional intensity, for us, promotion is more part of our strategy and it's a way to provide more visibility and prominence in store for our products. It's not necessarily about price discounting. And I can tell you that in 2024, we have not seen us increase promotional intensity or our portion of volume or sales sold on deal. Above our peer sets. So, we are very judicious about how we manage our promotional intensity. It's an ROI-based approach and we continue to do that.

So, when it comes to gross profit margin, let me step back and tell you about our Q2 performance. We're pleased with our Q2 performance. It was driven by value realization, mix, supply chain efficiencies, and it's typically – Q2 is typically the highest GP quarter due to seasonal builds and also the mix that we have. If I look at the balance of the year, it will go down from that high watermark of Q2 and Q4 is expected to be the lowest, as I mentioned in my prepared remarks, due to factory and plant maintenance, with Q3 being about in line with Q1. We're also seeing commodity pricing edging up, although it's still deflationary, but we're continuing to work on productivity and continue to advance our productivity enhancements. As we look at gross margin going forward, we look at it holistically; value realization, efficiencies, etcetera. We're preparing building blocks for 2024 and 2025 and beyond. So, that's how I look at it. And promotions are something we consider, but it's a holistic analysis on how we drive our gross profit margins going forward.

Operator: Thank you. Our next question comes from the line of Jeremy Fialko with HSBC. Please proceed with your question.

Jeremy Fialko

Analyst, HSBC Bank Plc

Q

Hi, there. Thanks for taking the questions. A couple for me. First one is a follow-up on the previous question. We've heard a number of peers talk about a slowdown in US skincare, particularly on the dermatological side. So I wanted to hear whether that is something that you are seeing and where the slowdown that they referred to is happening. And then secondly, just a bit of a follow-up on the seasonal businesses, talk about sun care, the trends that you're seeing through Q3, and then the setup for the cold and flu season. My assumption is that you've now got a pretty normal quarter, i.e., normal inventories, a normal basis of comparison, therefore, we should expect to see some sort of year-on-year growth in line with the historic averages. But again, your perspective on that would be very helpful. Thanks.

Thibaut Mongon

Chief Executive Officer & Director, Kenvue, Inc.

A

Yes. Jeremy, so your first question on what we see in the Skin Health category, we see units about flat in Q2, I would say. You have differences between bodies and hair and face. Within face, we see some softness recently in moisturizers, but offset by growth in acne as an example. So, I would say that, from a Kenvue point of view, we are focused on executing the plan I highlighted and we don't see category dynamics impacting the precision in the execution of our plan moving forward. If you think about the back half of the year, I'm not going to start reporting on Q3, but I would say that sun, we saw a positive shift in consumption in June. And basically, the season is almost – is basically done by the end of the second quarter in terms of shipments for us and I would not expect replenishment happening in Q3.

For the upcoming cough, cold and flu season, that's in front of us. As we said at the beginning of the year, we are planning for normal season this year. What we are seeing is more in terms of phasing of shipments between Q3

and Q4. What we see is retailers reverting to their historical ordering pattern of ordering what they need more in Q4 than in Q3. So last year, when we were still recovering from the pandemic in 2022 and there were questions on supply chain resiliency around the world, we saw some retailers anticipating their purchase in Q3. This year, we don't see that happening. We see retailers reverting to their historical ordering pattern, capitalizing on the fact that supply chain are more resilient. And that's certainly the case with Kenvue. But as always, we will be ready to respond to the demand regardless of the season.

Operator: Thank you. [Operator Instructions] Our next question comes from the line of Peter Grom with UBS. Please proceed with your question.

Peter Grom

Analyst, UBS Securities LLC

Q

Thanks, operator, and good morning, everyone. Hope you're doing well. Maybe just to start a bit more of a housekeeping, I think, Thibaut, you mentioned in response to Andrea's question that you expect sequential improvement in volume performance in the back half of the year for Skin Health and Beauty. Do you anticipate returning to growth at some point in the back half of the year? Just trying to make sure we think about the trajectory correctly, just given all the moving pieces.

Thibaut Mongon

Chief Executive Officer & Director, Kenvue, Inc.

A

Peter, yes, good morning and thanks for the question. So, we see sequential improvement in volume in the second half. It will turn to positive. We expect it to happen more towards the fourth quarter, both in terms of volume and also growth. Also, keep in mind the comps versus last year. So Q4, we'll certainly see a positive showing in Skin Health and Beauty.

Operator: Thank you. We have reached the end of our question-and-answer session. I would now like to turn the floor back over to Thibaut Mongon for concluding comments.

Thibaut Mongon

Chief Executive Officer & Director, Kenvue, Inc.

Right. Thank you all for all your questions this morning. I would just end by repeating, right, that earlier this year, I committed to you that you would see a new Kenvue in action this year, one that – a company that is moving quickly to advance all three priorities, to reach more consumers effectively, invest further behind our brands, and build a culture of performance and impact. And while we are still in the early stages of implementing our strategies, we are confident that we are on the right path to deliver on our near-term targets. But as importantly, setting up Kenvue to deliver on our long-term value creation algorithm.

So, with that, I wish you all a great day. Thank you for joining us on the call. And thank you.

Operator: Thank you. This does conclude today's teleconference. We appreciate your participation. Have a wonderful day. You may disconnect your lines at this time.

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