Q3 2022 Earnings Call

Company Participants

- Andre Schulten, Chief Financial Officer
- Jon R. Moeller, President and Chief Executive Officer

Other Participants

- Andrea Teixeira
- Bryan Spillane
- Chris Carey
- Dara Mohsenian
- Jonathan Feeney
- Kaumil Gajrawala
- Kevin Grundy
- Lauren Lieberman
- Mark Astrachan
- Nik Modi
- Olivia Tong
- Peter Grom
- Robert Ottenstein
- Wendy Nicholson

Presentation

Operator

Good morning, and welcome to Procter & Gamble's Quarter End Conference Call. Today's event is being recorded for replay. This discussion will include a number of forward-looking statements. If you will refer to P&G's most recent 10-K, 10-Q and 8-K reports, you will see a discussion of factors that could cause the company's actual results to differ materially from these projections. As required by Regulation G, Procter & Gamble needs to make you aware that during the discussion, the company will make a number of references to non-GAAP and other financial measures. Procter & Gamble believes these measures provide investors with useful perspective on underlying business trends and has posted on its Investor Relations website, www.pginvestor.com, a full reconciliation of non-GAAP financial measures.

Now I will turn the call over to P&G's Chief Financial Officer, Andre Schulten.

Andre Schulten {BIO 22079652 <GO>}

Good morning, everyone. Joining me on the call today are Jon Moeller, President and Chief Executive Officer; and John Chevalier, Senior Vice President, Investor Relations. We will keep prepared remarks brief and then turn straight to your questions.

This was another strong quarter, strong top-line growth across categories and regions, sequential earnings growth progress in the face of significant and still increasing cost headwinds. Starting with a few highlights on the March quarter. Organic sales grew 10%, volume contributed 3 points of sales growth, pricing added 5 points as additional price increases began to reach the market, mix added 2 points to sales growth for the quarter.

These strong company results are grounded in broad-based category and geographic strength. Each of the 10 product categories grew organic sales in the quarter. Personal healthcare grew more than 30%, Fabric Care was up low teens, Baby Care and Feminine care grew double-digits, Oral Care and grooming up high singles, Home Care and Family Care up mid-single digits, Hair Care and Skin and Personal Care each grew low singles, focused markets grew 9% and enterprise markets were up 12%.

In focused markets, U.S. organic sales were up 11% on 7% growth in the base period. On a two-year stack basis, U.S. organic sales up 18%. Focused markets in Europe were up 10% and Asia Pacific up 8%. Greater China organic sales were down mid-single digits versus a comp period that was up 22%. Market condition continued to soften in the March quarter due to COVID driven lockdowns.

In enterprise markets, Europe grew 18%, Latin America up 16% and Asia, Middle East, Africa grew 8%, broad-based growth across geographies with six of seven regions growing organic sales high singles or better.

Global aggregate market share increased 50 basis points. 36 of our top 50 category country combinations held or grew share for the quarter. Our superiority strategy continues to drive strong market growth and in turn share growth for P&G. All channel market value sales in the U.S. categories in which we compete grew nearly 9% this quarter. P&G value share continued to grow up 1 point versus same quarter last year. Importantly, this share growth is broad-based. 9 out of 10 product categories grew share over the past 3, 6 and 12-month periods in the U.S. and globally. Consumers continued to prefer P&G brands recognizing their superior performance and value.

On the bottom line, core earnings per share were $1.33, up 6% versus the prior year. On a currency neutral basis, core EPS increased 10%. Within the EPS results, we estimate Ukraine, Russia was a negative impact of about $0.01 per share. Core gross margin decreased 400 basis points and currency neutral core gross margin was down 380 basis points. Higher commodity and freight cost impacts combined were 490 basis points hit to gross margins. Mix was 130 basis point headwind mainly from product form and pack size mix impacts. Pricing and productivity savings of 260 basis points partially offset the gross margin headwinds.

SG&A as a percentage of sales decreased 380 basis points due to strong top-line leverage. Advertising investments remain strong as we continue to communicate the superiority and value of P&G offerings across price tiers. Core operating margin decreased 10 basis points. Currency neutral operating margin increased 20 basis points. Productivity improvements were 170 basis points help to this quarter.

Free cash flow productivity was 74%, as receivables and inventories increased due to strong sales results. We returned $3.4 billion of cash to share owners, approximately $2.2 billion in dividends and $1.2 billion in share repurchase. Last week, we announced the 5% increase in our dividend, reinforcing our commitment to return cash to share owners, many of whom rely on the steady reliable income earned with their P&G investment. This is the 66th consecutive annual dividend increase and 132 consecutive year P&G has paid a dividend.

So, three quarters into the fiscal, organic sales up nearly 7% on broad-based growth across categories and geographies, solid global value share growth, sequentially improving EPS growth, strong cash productivity, and an increased income commitment to owners of P&G shares.

Moving on to strategy. Our team continues to operate with excellence and stay focused on the strategies that enabled us to create strong momentum prior to the COVID crisis and to make our business even stronger since the crisis began. We continue to step forward into the challenges and to double down on our efforts to delight consumers. The strategic choices we've made are the foundation for balanced, top and bottom line growth and value creation, a portfolio of daily use products many providing cleaning, health and hygiene benefits in categories, where performance plays significant role in brand choice. In these performance driven categories, we have raised the bar on all aspects of superiority, product, package, brand communication, retail execution and value.

Superior offerings delivered the superior execution drive market growth. This drives value creation for our retail partners and builds market share for P&G brands. Noticeable superiority is perhaps the most important inflationary environment we are now facing -- the most important in the inflationary environment we are potentially facing. A great example is the formula innovation we've launched on Tide and Ariel laundry detergent to enable superior cleaning performance in cold water washing. We're strengthening the communication of the cost benefits to consumers and the environmental benefits for the planet on the package and in our advertising.

For consumers the savings from switching from hot to cold washing can nearly offset the cost of Tide or Ariel liquid detergent in each load. The superior cold water performance is a strong competitive advantage, enables immediate energy cost savings for our consumers and avoids the cost of rewashing, which may be necessary with less effective detergents. In addition, washing with cold water improves sustainability by reducing the energy required to heat water in the process and by improving garment life spans.

Superior innovation delivering multiple benefits and improved value for consumers even while we've price to offset a portion of the cost increases we are absorbing. We've made investments to strengthen the health and competitiveness of our brands across innovation, supply chain and brand equity and we'll continue to invest to extend our margin of advantage and quality of execution improving solutions for consumers around the world.

Building on the strength of our brands, we are thoughtfully executing tailored price increases. We closed couple price increases with innovation to improve consumer value along the way. The strategic need for investment to continue to strengthen the superiority of our brands, the short-term need to manage through these challenging cost environment and the ongoing need to drive balanced top and bottom-line growth, including margin expansion underscore the importance of ongoing productivity.

We're committed to driving cost savings and cash productivity in all facets of our business. No area of cost is left untouched. Each business is driving productivity within their P&L and balance sheet to support balanced, top and bottom-line growth and strong cash generation.

Success in our highly competitive industry requires agility that comes with a mindset of constructive disruption, a willingness to change, adapt and create new trends and technologies that will shape our industry in the future. In the current environment that agility and constructive disruption mindset are even more important. Our organization structure yields a more empowered, agile and accountable organization with little overlap or redundancy flowing through new demands, seamlessly supporting each other to deliver against our priorities around the world.

Going forward, there are four areas in which we need to be even more deliberate and intentional to strengthen the execution of our strategies: leveraging environmental sustainability as an additional driver of superior performing products and packaging innovations; increasing our digital acumen to drive consumer and customer preference; reduce cost and enable rapid and efficient decision making; next level supply chain capabilities to enable flexibility, agility, resilience and a new level of productivity adapting to a new reality and our employee value equation for all gender identities, races, ethnicities, sexual orientations, ages and abilities for all roads to ensure we continue to attract, retain and to develop the best talent.

These are not new or separate strategies. They are necessary elements in continuing to build superiority and reducing cost to enable investment and value creation in strengthening our organization. They are part of the constructive disruption we must continue to lead. These strategic choices on portfolios, superiority, productivity, constructive disruption and organizational structure and culture are not independent strategies. They reinforce and build on each other. When executed well, they grow markets, which in turn grows share, sales and profit. These strategies were delivering strong results before the pandemic and have served us well during these volatile times. We're confident they remain the right strategic framework as we move forward.

Moving on to guidance. We set each quarter that we will undoubtedly experience more volatility as we move through the fiscal year. We've seen another step in cost pressures and foreign exchange rates have moved further against them. Transportation and labor markets remain tight. Availability of materials remain stretched in some categories and markets. Inflationary cost pressures are broad-based and continue to increase with little sign of near-term relief and have resulted in consumer price increases across CPG categories and beyond.

A recent spike in virus cases in China and resulting lockdowns are affecting consumption and have caused temporary work stoppages in our operations and those of our suppliers. These cost and operational challenges are not unique to P&G and we won't be immune to their impacts. However, we think the strategies we've chosen, the investments we've made and the focus on execution and excellence have positioned us well to manage through these challenges over time. Based on the current spot prices, we now estimate a $2.5 billion after-tax commodity cost headwind in fiscal '22.

Since our last update, we've seen continued cost increases in nearly every type of material we use and in diesel and in natural gas. Freight costs have continued to increase. We now expect freight and transportation costs to be a $400 million after-tax headwind in fiscal '22. Foreign exchange rate have also moved further against us since our last guidance. We now expect FX to be a $300 million after-tax headwind to earnings for the fiscal year. We are offsetting a portion of these cost pressures with price increases and with productivity savings.

Since start of the fiscal year, we've taken price increases in each of our 10 product categories in the U.S. You may recall it was one year ago, when we announced price increases in the Feminine Care and Baby Care categories. Over the last year, input costs have continued to increase substantially and as a result, the Feminine Care business has announced an additional price increase in the U.S., which may be effective in mid-July.

Also, as a result of these increased costs headwinds, we recently announced price increases on certain items in the U.S. Home Care category that will be effective at the end of June and in the U.S. Oral Care business that will be effective mid-July.

As always, each category in each market is continually assessing the cost impacts they face and the potential need for pricing since there are decisions to price the degree and timing of those moves will be very specific to the category, the brand and sometimes to the individual SKU. This is not a one-size-fits-all approach. Also, just as we've done over the past year, we'll look to close couple price increases with new innovation that offers our consumers more value, continue to drive category growth and maintain our competitive superiority advantage.

As we said before, we believe this is a temporary bottom line rough patch to go through, not a reason to reduce investment in the business. We're sticking with the strategy that has been working well before and during the COVID 19 crisis.

Moving to key guidance metrics. We now expect organic sales growth in the range of 6% to 7% for the fiscal year, a 2-point increase versus our prior guidance of 4% to 5%. Pricing was sequentially stronger contributor to top-line growth in the third quarter and will continue to be a driver again in the fourth quarter, as we get the full effect of increases taken over the past few months. We are closely monitoring consumption trends for signs of changes. So far, elasticities have been in line or better than our expectations. Demand for our best performing premium priced offerings remain strong as to our market share trends.

On the bottom line, we're maintaining the core earnings per share growth range of 3% to 6%, but given cost challenges we are facing, we now expect to be at the low end of the range at 3%. Within this guidance, we expect an additional $0.04 per share of negative impact in the fourth quarter from higher costs and limited operations in Ukraine and Russia.

The impact from commodities, trade and foreign exchange has increased significantly since the start of the fiscal year. Our initial guidance in July assumed $1.8 million after-tax or about $0.70 per share. This increased to $2.3 billion in our October outlook, $2.8 billion in January, now $3.2 billion after-tax headwind to fiscal '22 earnings.

On an EPS basis, the headwinds are now approximately $1.26 per share, or a 22% headwind to core EPS. So, in the face of an incremental $0.56 per share of negative cost impact since the start of the year, we've held our growing in EPS range and we maintained strong investments and superiority with new product innovation and fully funded advertising programs. Of note, the majority of the recent $400 million increase in cost and foreign exchange headwinds will impact us in the fourth quarter.

We continue to expect adjusted free cash flow productivity of 95% for the year. We continue to expect to pay $8 billion in dividends and now expect to repurchase approximately $10 billion of common stock combined to plan to return $18 billion of cash to share in this fiscal year. This outlook is based on current market growth rate estimates, commodity prices and foreign exchange rates. Significant additional currency weakness, commodity costs increases, geopolitical disruptions, major supply chain disruptions and store closures are not anticipated within these kind of ranges.

To conclude, our business continues to exhibit strong momentum and we believe P&G is well positioned to grow through and beyond the immediate issues we are facing. We will manage through the near-term cost pressures and market volatility with the strategy we've outlined many times. We'll continue to step forward toward our opportunities and remain fully invested in our business. We remain committed to driving productivity improvements to fund growth investments, mitigate input cost challenges and to maintain balanced, top and bottom line growth.

With that, we'll be happy to take your questions.

Questions And Answers

Operator

(Question And Answer)

(Operator Instructions) Your first question comes from the line of Lauren Lieberman with Barclays.

Q - Lauren Lieberman {BIO 4832525 <GO>}

Great. Thanks so much and good morning. Andre, I was curious this quarter's revenue numbers surely show that there isn't really much is happening in the way of trade down and you just commented on the elasticity. But I just was curious kind of what is anything P&G is doing to prepare for what feels like an inevitability for consumer becoming more sensitive to the pricing that is prevalent not just in your products, but across everything that they need to buy. So, anything that you guys are doing proactively to help mitigate or think ahead to when trade down or substitution may become more of a factor? Thanks.

A - Andre Schulten {BIO 22079652 <GO>}

Sure. Good morning, Lauren. Yes, so as you said in the data, at this point we continue to see favorable price elasticities relative to historic. Elasticities we've observed, elasticities are better by about 20% to 30% versus what historical data would have indicated. That's good. But looking forward, we certainly have our eyes wide open and watch for any change in terms of consumer behavior. And as you say, we prepare on multiple fronts.

I think the first level of protection here is the portfolio we've chosen to play in. We've moved out of discretionary categories into categories that are daily use health and hygiene focused, where performance truly drive brand choice. That allows us to continue to invest in superiority, which we are doing consistently. Even though we see cost pressures, we continue to invest in superiority and every category and every proposition. That is probably the best protection and consumers are rewarding us with continued trade-in and continuous trade up, which is in the share numbers to date.

The superiority also allows us to translate product superiority, for example, into value superiority more directly for the consumer, so that's second intervention I would describe. So, we are more proactively turning true product superiority into value claims that we put on tech using our advertising. One example is the Ariel cold -- Ariel and Tide cold-water wash that I have mentioned in the prepared remarks. There are other innovations like the ADW, the automatic dishwasher myth buster, stating that even with eight dishes, it's more efficient to use the dishwasher than cleaning the dishes under running water.

The latest EZ-Squeeze innovation on Dawn that allows the consumer to use every last drop without any compromise on performance. So, those are examples that we're turning into value claims to have consumers understand more easily the value that is coming by using P&G propositions.

We have intentionally built price ladders in every brand and across brands to ensure that we have offerings for consumers. If they feel they are budget constrained, they can trade within the P&G brand offerings. So, on diapers, we have multiple offerings starting with Pampers Pure at about $0.40 a diaper, Swaddlers at $0.35 a diaper, Baby Dry at $0.30 and Luvs at $0.20. These price levels exist in all categories and offer the consumer a choice within the P&G portfolio.

We are also -- which is part of our pricing execution, protecting key price points, key value price points for each offering, so consumers can choose different cash outlays as they shop based on their available cash at the moment of shopping.

The last element, we intentionally built distribution across all channels and invested in all channels. And that includes channels that consumers that are more budget constrained would migrate to, like hard discounters in Europe, like the dollar channel in the U.S., for example. So, building distribution across those channels to be able to serve the consumer, where they want to shop, is the last element I would call out. So, all of those leave us in a better position than we've ever been to deal with a potential consumer that is more budget constrained. To date, we're not seeing that come through.

Operator

Your next question comes from the line of Bryan Spillane with Bank of America.

Q - Bryan Spillane {BIO 2147799 <GO>}

Hey, good morning, everybody. And thanks for taking the question. So, my question is about just the -- I guess, the path to stabilizing gross margins in particular. And I guess if we look at the quarter, right, the pricing and productivity covered about half of the inflation. So, if you take the mix effect out of gross margins. And so, I guess, as we're modeling going forward, what are the levers that are going to -- that we should look to stabilize gross margins? Will they be a lot more incremental pricing? I know you've talked a little bit about that in the prepared remarks, a step-up in productivity. I'm just trying to understand what the levers are going to be, as we kind of look forward over the next couple of quarters on gross margins.

A - Andre Schulten {BIO 22079652 <GO>}

Yes. Thanks. Good morning, Bryan. You're right. Over the past three quarters, you see pricing and productivity continue to increase a bigger portion of the commodity, foreign exchange and T&W gross margin impact. In quarter one this covered 37%; in quarter two, we covered, I believe, 43% and now we're at 53%. So, you see a bigger portion being covered over time via those effects.

We will continue to drive all three levers to recover the dollar impact of commodity cost increases, foreign exchange and T&W. Productivity will continue to play a significant role. We have a lot of runway left on productivity, and as the supply situation stabilizes here over time, we have more line time and more resources available to reinvest in cost of goods savings. And that will allow us to strengthen our productivity muscle here sequentially, hopefully, over the next few quarters.

We will continue to drive innovation. We have prioritized innovation in our resource and line time allocation to ensure that we can continue to offer superior value to our consumers, which also enables us to take pricing and see these relatively benign elasticities at this point in time. So, you continue to see us invest in innovation. With innovation, we will try to take pricing at a very granular level by market, by brand. A lot of the price increases that we have announced are yet to flow through. So, you will see an incremental contribution to the top-line and to gross margin recovery over the future, the other price increases already announced. And we will have to carefully evaluate more opportunities to take pricing.

It will take time to recover the full dollar impact. And as we said before, it's more important to us to support the business model, support innovation, support superiority, execute pricing in the right way and recover gross margin and cost impact over time versus rushing to do this faster. So, you should expect sequential progress. I won't give you a specific timeline. We will continue to use all three: productivity, innovation and pricing.

Operator

Your next question will come from the line of Dara Mohsenian with Morgan Stanley.

Q - Dara Mohsenian {BIO 3017577 <GO>}

Hi. Good morning. I was hoping to get a bit more detail on China, how much of the decline in the quarter do you think was specifically related to lockdowns and maybe the comp versus last year? And can you give us a bit more granularity on some of the performance by product category there? And any thoughts on China going forward with the continued lockdowns in April and how the business is positioned going forward? Thanks.

A - Andre Schulten {BIO 22079652 <GO>}

Yes. Thanks, Dara. Good morning. Look, China -- the lockdowns had two impacts in China for us. One, on the supply side, we have two plants in the Shanghai area and the contract manufacturer, those obviously were shut down for now an extended period of time. So, we had to activate our business continuity plans to offset as much of that production impact as we could. And we're certainly seeing a significant impact in terms of consumer demand. About 25%, I think, was the Wall Street estimates of consumers are somehow impacted by lockdown. That is impacting our consumers' ability to reach stores, grocery stores, department stores.

Even online shopping is significantly constrained due to the inability to deliver. So, we certainly see a significant impact from lockdowns. Latest read of market size, our categories over the past three months through March was flat in terms of value in China. With the continued lockdown and the difficulties in the market, we would expect April to be flat to negative.

In terms of category detail, beauty is significantly exposed to China. As you know, bigger part of beauty is -- of the beauty business is in China. SK-II continues to be under pressure due to the market effect and channel effect in China. So, that dynamic has not changed. The longer term story on China, based on historical results, which have been extremely strong over the past three, four years, as you know, we've grown high singles, low doubles in China.

We believe the market continues to be very attractive market for us. We expect categories to return to mid-single, high-singles growth. We have a very strong organization, very strong supply chain, very strong R&D organization in China. So, we remain confident and we will continue to invest to capture the growth in the future.

Operator

All right. Next question will come from the line of Rob Ottenstein with Evercore.

Q - Robert Ottenstein {BIO 1498660 <GO>}

Great. Thank you very much. Just a point of clarification to start off. Can you tell us kind of what your pricing run rate was at the end of the quarter, given that the pricing was going in throughout the quarter and the year? I think you were 5% on average, but just like to get a sense of what the run rate was.

And then I'd like to dig in a little bit more on the state of the consumer. You mentioned that elasticities were 20% to 30% better than what history has shown. But the current conditions, we've never had these kind of current conditions before, at least in anybody's recent memory. So, I was wondering what your consumer panels are telling you about why the elasticities are better. Is it because of increased savings? Is it the low rates of unemployment? How much is maybe contributed to your superiority? Just trying to get a little bit better sense of your read on the consumer from your own internal research. Thank you.

A - Andre Schulten {BIO 22079652 <GO>}

Okay. Thanks, Robert. So, in terms of pricing run rate for the quarter, on average we have a 5-point contribution to top-line. As we said, pricing will continue to increase as more of the price increases flow through. So, I would say exiting the quarter, I would see about a 6% run rate to top-line from pricing contribution. So, you will see more of the pricing that has been announced that will flow through in April, for the flow through in quarter four.

Pricing elasticities remain favorable and within the portfolio that we offer to consumers, we broadly see a trade-up into higher priced propositions that offer better value and better product performance. So -- and that explains the mix effect that you see in gross margin, where we see higher unit sales items being chosen with higher penny profit, but slightly lower gross margin. So, consumers are trading into single unit dose detergents instead of liquid detergent. Consumers are trading into Swaddlers instead of Baby Dry in diapers. So, we see consumers trading up even within our portfolio into higher performing product propositions.

The relevance of product performance in our categories, we believe is the reason, why consumers are not trading down. We've had an extensive period of trial during the early COVID phases, where consumers have traded into P&G. They experienced the superior performance of our propositions. They've seen the relative value that we provide, even though the cash outlay might be higher, they see the higher efficacy of the product and the benefit that they gained from it. And we've seen repeat rates reaffirming that.

We believe that a good portion of the resiliency of our demand is driven by the superiority of the product and packaging, clear communication of the benefits basis, clear communication of the value, good retail execution and carefully crafted price increases that allow consumers to choose the cash outlay. They feel ready to afford and to choose the brand and brand proposition that they are looking for. So, I leave it at that.

A - Jon R. Moeller {BIO 16200095 <GO>}

Hey, Robert, this is Jon. Just a couple other pieces of perspective on this and of course, it's a rapidly evolving situation and this could change tomorrow. But if you look for data points to support Andre's comments on consumer resiliency, you obviously see them within the internals of our income statement as you mentioned. Also, if you look at private label shares as a proxy for trade-down, they remain below year ago in the U.S., for the past 3, 6 and 12 months. They remain below year ago in Europe for the past 3, 6 and 12 months.

And if you look at market shares across channels, Andre mentioned earlier that we've worked to improve our distribution in channels, where consumers with more of a budget challenge are inclined to shop. Our share growth in those channels entirely consistent with his points, are some of our highest share growth across retail banners. So, in the dollar channel, for example, significant share growth.

Again, we'll have to monitor this very closely. Things can change tomorrow, but as we sit here today, it looks like the moves we've made to focus the portfolio in daily use categories, where performance drive brand choice and deliver on the performance aspect across the vectors of superiority and be very granular in our pricing executions is holding up.

Operator

All right. Next question will come from the line of Kevin Grundy with Jefferies.

Q - Kevin Grundy {BIO 16423871 <GO>}

Great. Thanks. Good morning, everyone. My question relates to category growth rates, understanding the volatility of the environment and I guess I'm coming at this from the angle, I'm trying to unpack the strength of the 10% organic sales growth in the quarter and just the areas of favorability versus your plan. We've covered a lot of this demand elasticity clearly better, trade up remains favorable despite the environment, you continue to gain market share, which is great up 50 basis points globally, though. I'm less certain that degree of market share gain would be very different than your plan. And then we haven't touched on this in the call.

I'm not sure maybe there is some degree of inventory rebalancing with the trade because demand has outstripped supply in recent quarters. So, where I'm going with this and understand the volatility of the environment, has there been any material change in your view for the categories. As you look across your geographies, and you look across the category that you participate in, and we're thinking about our forecast going forward. Any material change to category growth rates based on what your current currently seeing? Your comments there would be helpful. Thank you.

A - Andre Schulten {BIO 22079652 <GO>}

Good morning, Kevin, thank you. So, category growth rates are holding up well. Fiscal year-to-date, global category growth and the categories we compete in is 5%. We expect that to continue at around 5%. Category growth in focus markets is 5%. Category growth in enterprise markets is 7%. So, it's a strong five on a global level. It's fairly consistent enterprise market has been growing past 3, 6 and 12 at 7%. Focus markets have gone between 4% and 5% over the past 3, 6 and 12 months.

So, if anything in the most recent reading, we've seen strengthening of category growth. We're also pleased with the fact that we see P&G leading and disproportionately contributing to category growth in most of the markets we're competing in, via innovation and via leading innovation, and thereby driving category growth and participating in that category growth via share growth.

So, overall, we feel good about the level of category growth we're seeing, slight acceleration across the periods, P&G contributing via our strategy of driving market growth via superiority investment and innovation. And that certainly is benefiting our growth and is in line with our growth model we want to drive, because it's the only way to sustainably grow at these levels by driving market growth and then participating in that growth via share growth.

A - Jon R. Moeller {BIO 16200095 <GO>}

Yes. Market growth is something that doesn't happen to us. We need to positively impact at ourselves, which are exactly what Andre just said. And that's what we're trying to do through our strategy. I will also say Kevin that if you look at the last quarter, there are several negatives within the quarter from a top-line standpoint, several challenges that we've been working against, we've talked about China, our second largest market down mid singles. We've talked about the unfortunate situation in Russia and the Ukraine.

One thing we haven't talked about, except indirectly, is that we're still racing to catch up with demand in our largest market, the U.S. but we're not fully supplying the markets demand. And all of those, hopefully over time, or some of them at least offer even additional upside as they reverse themselves.

Operator

Your next question comes from the line of Olivia Tong with Raymond James.

Q - Olivia Tong {BIO 22252574 <GO>}

Great. Thank you. Just a little bit of a follow-up there. Could you just talk a little bit about where the supply constraints are most acute? And where you're starting to see potentially some more capacity coming back across a category, particularly amongst private label players? You mentioned pricing in Feminine Care, Home Care, Oral Care. Can you talk about a little bit about your decision, as you consider future rounds of price increases and what categories you could potentially -- how you think about what category you could potentially move on further? Thank you.

A - Andre Schulten {BIO 22079652 <GO>}

All right Good morning, Olivia. Supply constraints may be to just start at the global level, supply constraints are only present in every potential bucket that you can think through being able to source raw and tech materials is still difficult in sufficient quantities. Getting raw and tech materials to the places we need to get them to continues to be costly and highly volatile, labor availability is certainly a stretch not for P&G directly, but more for our supplier base.

And then getting finished product out to our retailers by being able to actually ship with truck availability in the U.S. for example, it's difficult. So, it's across all aspects of the supply chain. We are making progress. Our on-shelf availability continues to be stable at around 93%, 94%. Even as we grow at these levels that we are happy to report, we're growing at in Q3 and fiscal year-to-date.

We have more and more categories coming off managed supply in the U.S. over the next two months. So, we are carefully working with our retail partners to ensure that we do this in the right way to ensure the best service and best on-shelf availability with our retail partners and we're making progress heavy the most investment in terms of capacity will be in our North America and European markets to ensure that we have sufficient capacity to keep up with increased demand we see. Those investments will take hold over the next two years, but we expect to be in a better situation over the next quarter three to six months specifically in the U.S. moving out of managed supply.

There is no, to your second part of the question on pricing, there is no formula based approach to pricing in any of these categories. So, we're carefully watching, number one consumer behavior and the strength of our superiority relative to the market. We are looking at the cost pressures and cost headwinds that we are seeing and you will have noticed that in our paper categories and Fem Care, in Baby Care, in Family Care and in our Fabric and Home care categories that's where we see the biggest impact from commodity cost increases transportation, transportation warehouse, but also foreign exchange impacts.

So, the impacts are bigger, there is superiority and then it becomes a matter of do we have the right innovation available, or do we feel that it is right at this point in time to recover via pricing versus leveraging productivity and the balance between those three elements, as we've talked before. So, I wouldn't say there's any formulaic approach, but certainly Fabric and Home Care and the paper categories are most exposed to the cost pressures. So, the combination of all three elements needs to play out more aggressively in those categories and maybe in some others.

Jon, anything you want to add?

A - Jon R. Moeller {BIO 16200095 <GO>}

No, I think, you've covered it and Olivia, first of all, it's great to hear your voice again. And obviously, we can't provide any more granularity than Andre already has in terms of where price -- future price increases would occur. That's not something that's legally permissible.

Operator

Your next question will come from the line of Wendy Nicholson with Citi.

Q - Wendy Nicholson {BIO 2081269 <GO>}

I guess not to beat a dead horse, but just to follow up on that point. As you think about the priority for the P&L, in those categories, I mean, I look at paper, I look at laundry or fabric. Those are categories, where there is just to start with, maybe more competition, maybe less brand loyalty, maybe a little bit more private label, just to start with, even though private label may not be gaining share yet. And so I'm wondering, if your priority is to offset commodity headwinds as much as you possibly can to preserve gross margin, or is it to preserve market share at this point?

And then relatedly, you haven't really talked that much about currency and what you're doing in some of the bigger emerging markets, not even just emerging markets, but Japan for example, where currency is a significant headwind. Are you adopting a different stand, with regard to taking prices to offset currency headwinds? And are you seeing any differences in elasticity maybe in some of those emerging markets? Thanks so much.

A - Andre Schulten {BIO 22079652 <GO>}

In terms of priority, our priority remains a reasonable recovery time on the dollar impact of commodities, foreign exchange and T&W headwinds across all categories. We will do this in a way that provides value to the consumer, provides a superior proposition to the consumer by combining it with innovation. There is no timeline for us that forces us to recover gross margin over a certain period of time. We want to return to margin expansion and we will. Our balanced growth model requires us to drive top-line, bottom line, but also reasonable margin expansion.

So, there is continued commitment to return to that point, but we will do it in a way that provides the right value to the consumer in every brand, in every market, at any given point in time, so we can serve consumers in the best way possible and maintain business momentum.

To your second question on foreign exchange rate pricing, across markets foreign exchange rate pricing is a reality we are dealing with every day; we've been dealing with for years. Nothing different to report in terms of elasticities. It's being executed in some markets more pronounced, you've seen us taking significant price increases, for example, in Turkey. Significant price increases in Argentina. So, those are being executed. The organizations know very well how to do those and they are baked in our forecast and guidance.

A - Jon R. Moeller {BIO 16200095 <GO>}

Just one other point, Wendy. You asked -- the question that you asked is the question that we get asked by the organization every day, which is, which of these matters most? Essentially top-line and continued share progression or bottom line and earnings recovery. And the answer always is both. It's Andres balance point. We need to do both or we get out of balance, and the wheels come off. So, we need to continue and we will continue to invest in top-line momentum, as we recover the commodity costs or a combination of pricing, productivity et cetera. So, that's, it's both.

Operator

All right. Your next question comes from the line of Nik Modi with RBC Capital Markets.

Q - Nik Modi {BIO 7351672 <GO>}

Yes. Thank you. Good morning, everyone. I wanted to ask a different slant to the premiumization and trade-down question, not necessarily on trade down, but just slowing momentum of premiumization because during the pandemic, you had a lot of low-income consumers with all that extra stimulus money engaging more in premium priced chairs. So, I was just curious on your observations on that and kind of how do you think that's going to manifest in terms of that particular income strata and how they're behaving with food and gas inflation the way it is? Thank you.

A - Andre Schulten {BIO 22079652 <GO>}

Yes. Morning, Nik. Look, we're not seeing it. We've see consumers trade into P&G brand and trade up within the P&G brand portfolio throughout the pandemic. Every quarter of the fiscal year we've seen consumers continue to trade up within the P&G brand portfolio into higher premium propositions across most categories. That's the mix effect we've seen on the gross margin and the positive mix effect on sales. So, we continue to see consumers stay within the P&G portfolio and many consumers actually trading up within the P&G portfolio, as they see the benefit of those higher premium propositions.

As we've said before, we don't take that for granted, we don't assume that what we're seeing to date is necessarily an indication of what will happen in the future. We are very well aware that consumers might end up looking at budget constraints. Where we see, for example, private label losses reducing, we continue to see P&G growth. So, even private labor coming back so far is not impacting P&G's ability to grow within those markets or within those market category combinations.

Our best defense to serve the consumer in a more budget constrained environment other point we've talked through from the portfolio focus that we're operating to superiority to value claims, cash outlay choices, price ladder choices, distribution across all channels. So, I come back to those elements that we control that will serve us well, I believe, even for consumers that are more budget constrained and looking for choices.

A - Jon R. Moeller {BIO 16200095 <GO>}

There are a lot of mileage benefits, and some of the higher price products that we need to proactively communicate, as Andre mentioned earlier. The assumption that just because something is higher priced, it costs me more per job is not a valid assumption, and we have to help people understand that.

Operator

All right. Your next question will come from the line of Chris Carey with Wells Fargo Securities.

Q - Chris Carey {BIO 21810941 <GO>}

Hi. Good morning.

A - Andre Schulten {BIO 22079652 <GO>}

Good morning, Chris.

Q - Chris Carey {BIO 21810941 <GO>}

I wanted to ask the question about the Personal Health Care business, organic growth over 30%, certainly impressive. I appreciate there's a dynamic here, where there's some recovery from like basically a non-existent cold flu, but also conscious that this is one of those categories, where you're particularly focused and there's been some innovation.

I wonder if you can just comment on how much of the strength in the business which is recovery versus things you're doing a bit more offensively that have a bit more legs long term. And just connected to that, fiscal Q4 implied organic sales guidance is for strength, but deceleration on a two-year stack. And I wonder if you're baking in any normalization there, or if there is other puts and takes that we should keep in mind? Thanks.

A - Andre Schulten {BIO 22079652 <GO>}

All right. Thanks. Chris. PHC had a fabulous quarter, as we point out. Part of that certainly is the stronger cold, cough, flu season. It's 57% stronger in our estimation than last year's season, which was abnormally low, driven by the mask mandates and everything else going on, a slightly stronger season than average by about 4%. But importantly, North America Vicks, for example, was able to outpace that season growth, plus 123% growth versus the season, which drove about 1.9 share points over the period. So, within respiratory season recovery certainly a big point about Vicks growing ahead of the season recovery and building share.

The growth is also broader than just respiratory. Digestive organic sales are up mid-teens and sleep is up nearly 30%. So, the breadth of the portfolio is performing even beyond just the season recovery. So, we continue to be very pleased with the results of the PHC portfolio and certainly see significant future runway there.

On quarter four sales guidance, the only thing I would say is, as we mentioned before we do not assume the favorable price elasticities to hold. In our forecasting, we assume price elasticities to return to normal levels that we've seen historically. That's the only thing I let you know, the rest I think is fairly clear.

Operator

The next question will come from the line of Kaumil Gajrawala with Credit Suisse.

Q - Kaumil Gajrawala {BIO 20703548 <GO>}

Hi. I'd like to maybe just follow-up on a comment from earlier on sequential gross margin improvement. Was that a just a general comment on something that you expect over time? Or, were you kind of indicating that gross margins we see today are trough margins in 4Q and as we get into the beginning of the next fiscal year is when we'll start to see it?

A - Andre Schulten {BIO 22079652 <GO>}

General comment over time, Kaumil; we're not forecasting gross margin or gross margin guidance here. Too many moving pieces. But over time, we remain committed to building gross margin as part of the balanced growth model.

Q - Kaumil Gajrawala {BIO 20703548 <GO>}

Got it. Thank you.

Operator

The next question comes from Mark Astrachan with Stifel.

Q - Mark Astrachan {BIO 15313233 <GO>}

Yes. Thanks, and morning everybody. I wanted to ask specifically a bit more about Beauty. So, volumes negative. I guess, I'm curious how much of it is category shift? It seems a bit away from Skin Care given pandemic effect there into some more discretionary categories. How much is, it market share challenges for SK-II around Asia and China specifically? And how do you think about how much of what I just said could be transitory versus needing more change from your standpoint to improve trends? Thank you.

A - Andre Schulten {BIO 22079652 <GO>}

Yes. Thanks Mark. We're very confident in the Beauty portfolio. If you look at the performance of this portfolio over the past five years, it's been just outstanding, right? The core portfolio has grown sales more than $3 billion over the past five years, profits more than $1 billion, significant shareholder value creation and 26 quarters of uninterrupted growth. So, the core portfolio has been performing extremely well.

And as you say, there are a number of headwinds that we see as temporary. China and the dynamics in China certainly being one of those significant dynamics, which is impacting the broader Hair Care and Skin Care portfolio, but also the broader impact on SK-II, as it comes to the travel retail shutdown during the COVID period and the impact of China on the SK-II consumption with department stores being closed down and even some of the online business being hampered.

So, there are a number of temporary effects that we see. You have seen us announced a few portfolio additions, acquisitions over the past months that are focused on the premium and super-premium segments in the category. We believe that's a growth opportunity beyond the core portfolio in specialty channels. So, we've proven that strategy with previous acquisitions like First Aid Beauty. And so we want to build out the portfolio in the premium and super-premium segment in addition to restrengthening the core.

So, there's certainly work to do to address the opportunities in China on the core business, rebuild strength and momentum on SK-II, and further help our business to serve premium and super-premium consumers and specialty channels in the U.S. and outside the US. But we're very confident in the core focused portfolio and some targeted additions via acquisition that we tucked in, which set us well for future growth in the Beauty category.

Operator

Next question comes from line of Peter Grom with UBS.

Q - Peter Grom {BIO 22424199 <GO>}

Hey, good morning, everyone. So, in the release there were a few comments around lapping pandemic related consumption. And I think you called out appliances and cleaning specifically. I just would be curious, when you look at performance in those categories, how does the recent performance compared versus your expectations? I guess what I'm trying to understand is, are you seeing a normalization that is in line with your expectations in some of those categories that saw significant growth over the past couple of years, or has demand held up better or been worse than you would have anticipated?

A - Andre Schulten {BIO 22079652 <GO>}

Yes. I can start Peter, and then maybe Jon wants to add a few points here. But overall consumption is holding up. As I mentioned, market growth, 5% of focus markets, 7% in enterprise markets. That's certainly an indication that overall consumption in all categories is holding up well. There are some natural -- not natural, but logical switches.

So, when we think about, for example, our Grooming business, the Appliances business has experienced significant growth during the pandemic, as more and more jobs that were done in salons and barbershops moved in-house. So, folks -- people bought these appliances, experienced the fact that they can do the job themselves, and they continue to do so. But once that need is satisfied, appliances sees a decline versus that peak in terms of incremental job growth and incremental overall growth.

At the same time, there's a natural hedge within the Grooming portfolio. So, blades and razors were under pressure, as more people work from home and stayed at home, with reopening, that part of the category resumed growth. So, there's a hedge component within Grooming, for example.

Within anything that is health and hygiene related, I think consumers continue to put more emphasis on jobs to be done. They spend more time at home. So, we continue to see our categories to benefit from both effects. Paper towel consumption continues to be increased by more than 10%. We'll see where bath tissue ends up once supply is unconstrained, but more time at home certainly would speak to more in-home consumption versus away-from-home consumption.

The only part, where we saw a little bit of a decline was anything that has to do with household -- surface disinfection, surface cleaning. That's a relatively smaller part of our portfolio. But as consumers get more used to the right balance there, we saw a little bit of a decline. But overall, all categories still benefiting from more time at home and higher focus on health and hygiene and certainly Beauty and Personal Care related categories benefiting from reopening.

Operator

Your next question comes from line of Andrea Teixeira with JPMorgan.

Q - Andrea Teixeira {BIO 1941397 <GO>}

Thank you. I was hoping if you can please comment on the Baby, Fem Care and Family Care. Seems that you continue to regain share in the U.S. and also potentially in China despite the challenges there. And similar to this question, you had an impressive growth in the cold and flu brand franchises. But you start to lap those comps there. So, do you think the growth is still sustainable with the innovation you've made in other franchises in health care? Thank you.

A - Andre Schulten {BIO 22079652 <GO>}

Yes. Thanks, Andrea. So, Baby Care share is improving significantly in Europe and in North America, driven by major innovation that was launched in the market, both in Europe and in North America. We will continue to build on that share momentum. We will continue to drive superiority via incremental innovation, investment in brand communication, go-to-market execution.

We've also been able to enter some new parts and grow some new segments within the Baby Care category. When you think about Ninjamas launches, for example, in North America, that's a category that has been relatively quiet. It serves children between 5 and 12, with all the night bed-wetting issues. And reentering that category with a creative and relevant proposition allowed us to grow the category mid-teens. And at the same time, build an 8% to 9% share position within the category.

We continue to build share in pants. Pants is a trade-up category in Europe and an opportunity in North America. That allows us to grow our position as well. So, broad innovation in terms of true product innovation, but also new jobs to be done and communication.

Fem Care, we are seeing big success in both adult incontinence, but also in the most premium propositions in Fem Care. The biggest growth, for example, in Fem Care pads in North America is driven by Infinity, our most premium proposition, which is a unique proposition from P&G form-based pad, delivering superior comfort and absorbency. Again, same formula. Significantly innovating in relevant ways for the consumer, investment in communication, retail execution, allows us to drive overall market growth and share growth.

On cold and flu, I don't have much more to add, Andrea, versus what we said before. We are growing ahead of the segment in terms of respiratory, with strong innovation in Vicks. And we are growing the balance of the portfolio in terms of absolute sales growth and share growth, be it sleep or digestive. So overall, we feel there's significant runway left on our PHC portfolio, and it's playing out in the market.

Operator

And your final question will come from the line of Jonathan Feeney with Consumer Edge.

Q - Jonathan Feeney {BIO 2268157 <GO>}

Thanks very much. I give you a lot of credit. I mean, there hasn't been a lot of discussion about retailer pushback to pricing. And maybe that's just because the results are good overall. But just looking at the U.S. market, why is it that your relationships with retailers seem so good that elasticities are better? It's really a consumer level discussion. And do you expect that to continue?

Can you give me any color around, why that particular -- is it maybe just simply that they're short product, and there's more demand versus supply, so you're kind of in the driver's seat? What allowed this pretty good -- a series of very good relationships to emerge? And how sustainable do you think that proves if we need another round of significant pricing second half of the year? Thanks.

A - Andre Schulten {BIO 22079652 <GO>}

I'll start, and I'm sure Jon has a few points to add here. But generally, discussions with retailers work better if your business comes from a position of strength. Consumers are looking for your propositions. Velocity at shelf is strong. You have innovation programs that are credible and tangible and meaningful for consumers. You have in-store programs that are meaningful for retailers and consumers. You have an ability to communicate and support the advertising, both in digital as well as in mass advertising. And all of those things hold true, as we entered this commodity inflation cycle.

P&G came from a relatively strong position in terms of superiority. We continue to invest in innovation. Products on shelf, we're doing well. And that sets up a good discussion with retailers about future growth potential, the need for pricing, which is very clear, given the inflation cycle and the reality that it's broad-based within multiple industries. No guarantee that, that will continue. It will always be, as we said before, a very careful balance for us between productivity, innovation and pricing.

A - Jon R. Moeller {BIO 16200095 <GO>}

Yes. Our retail partners are also competitors in most cases, with their own label offerings. And because the increases and costs are so significant, they need to be able, in most cases, obviously, entirely at their discretion. But they need to be generally able to raise pricing on their own brands. And when that's true, that becomes less of an issue, not a non-issue, but less of an issue for us. And I think the biggest change that's occurred over the last several years in our dialogue has been a more deliberate and over-focus on our part on market growth and on being -- and a commitment to be a disproportionate contributor to market growth.

At the end of the day, a retail partner doesn't care what our share is. What they care about is, what their sales are and are they growing or not. And we need to be a source of that growth. And when we do that dependably and reliably, as Andre said, it changes the nature of the conversation, and that becomes the focus of the conversation, as opposed to other things.

We have an opportunity in better serving our retail partners with supply, as we've talked about several times, and we're working to address that. That's important in terms of continuing to serve them effectively. But that contribution to market growth sustainably and dependently changes world.

A - Andre Schulten {BIO 22079652 <GO>}

All right. I think that concludes the call. Thank you for spending time with us today. John Chevalier and I will be available all day, if you have any other questions. So, please feel free to call. You know where to find us. Have a wonderful rest of the day.

Operator

And ladies and gentlemen, that concludes today's conference. Thank you for your participation. You may now disconnect. Have a great day.