Q2 2017 Earnings Call

Company Participants

- Jon R. Moeller, Chief Financial Officer

Other Participants

- Ali Dibadj, Analyst
- Bill Schmitz, Analyst
- Bonnie L. Herzog, Analyst
- Caroline Levy, Analyst
- Dara W. Mohsenian, Analyst
- Jason English, Analyst
- Jon R. Andersen, Analyst
- Jonathan Feeney, Analyst
- Joseph Nicholas Altobello, Analyst
- Kevin Grundy, Analyst
- Lauren Rae Lieberman, Analyst
- Mark Astrachan, Analyst
- Nik Modi, Analyst
- Olivia Tong, Analyst
- Stephen R. Powers, Analyst
- Wendy C. Nicholson, Analyst
- William B. Chappell, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good morning, and welcome to Procter & Gamble's Quarter End Conference Call. P&G would like to remind you that today's 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.

Also, 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 the underlying growth trends of the business and has posted on its Investor Relations website, www.pginvestor.com, a full reconciliation of non-GAAP and other financial measures.

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

Jon R. Moeller {BIO 16200095 <GO>}

Good morning. Our second quarter results keep us on track with our objectives for fiscal year 2017. Organic sales for the quarter grew 2%. This includes about a one-point drag from the rationalization of the ongoing portfolio and reduced finished product sales to our Venezuelan subsidiaries. It also includes negative impacts from Indian demonetization and difficult to operate environments in markets such as Nigeria, Egypt, Turkey, and Argentina. Top-line growth was broad-based. Organic sales improved in five of six regions, 11 of the 15 largest markets, all five reporting segments and in 9 of 10 product categories.

In the U.S., our largest market, organic sales grew 2%. Over the last three semesters, U.S. organic sales have progressed from up about 0.5-point versus a year ago to up about 1.5 points to up more than 2 points. In China, our second largest market, organic sales growth has also progressed over the last three semesters and down 8% to down 2% to up 2.5% including 3% growth in the most recent quarter.

We're making similar progress in each of our largest categories. Over the last three semesters, Fabric Care organic sales growth has progressed from up just less than 1% to 1.5% to 3% growth; Hair Care, from down 1% to flat to up more than 2%; Baby Care from down more than 2 points to flat to up about 0.5-point; and Grooming, from up 1.5-point to up over 2 points in the two most recent semesters.

Sales growth in the quarter was volume driven, organic volume was up 2%. Pricing and mix were each essentially neutral to organic sales growth. All-in sales for the company were flat versus the prior year, including a 2-point headwind from foreign exchange.

Moving to the bottom line, core earnings per share were $1.08, up 4% versus the prior year. Foreign exchange was a 5-point headwind on second quarter earnings growth, about $0.05 per share worse than we expected heading into the quarter. On a constant currency basis, core earnings per share were up 9%. On a year-to-date basis, constant currency core earnings per share growth is up double-digits, extending the four-year streak of high-single or double-digit constant currency core earnings per share growth.

Core gross margin increased 70 basis points. On a constant currency basis, core gross margin was up 120 basis points, including 210 basis points of productivity improvement and a modest benefit from volume growth. Commodities, mix and pricing were each at 30% hurt to gross margin in the quarter.

Core operating margin was in line with the prior year quarter. On a constant currency basis, core operating margin was up 60 basis points. Productivity improvements contributed 230 basis points of operating margin benefit.

Core effective tax rate was 23.5%, essentially equal to the base period rate. All-in GAAP earnings per share were $2.88 for the quarter, up 157% versus the prior year. This includes gain of $1.95 per share from the Beauty transaction with Coty that closed at the beginning of the quarter.

We generated $2.4 billion of adjusted free cash flow. We returned $12.7 billion to shareholders, $1.8 billion in dividends, $1.5 billion in share repurchase and $9.4 billion in share exchanges with the Beauty transaction.

Despite some significant and unforeseen challenges, we stand at the halfway mark of our fiscal year essentially on track with where we hoped we'd be. We're raising our guidance for fiscal year organic sales growth from around 2% to a range of plus 2% to 3%, with the fourth quarter expected to be stronger than the third quarter.

We now expect fiscal 2017 all-in sales growth to be in line with the prior year. This includes a 2-point to 3-point headwind for the combined impacts of foreign exchange and divestitures. We're maintaining, for now, our guidance for bottom line core earnings per share growth of mid-single-digits. We continue to deal with an unprecedented amount of geopolitical disruption and uncertainty, which is affecting market growth, currency and commodities.

We're not immune from these macro dynamics. We're aggressively driving cost savings to mitigate these impacts, but we're protecting investments in the business to accelerate organic sales growth in a sustainable, long-term, market constructive and value accretive way, even if it means results end up below the current core earnings per share guidance range.

We continue within our core earnings per share estimates to reflect a reduction in fourth quarter non-operating income, due to lower gains from minor brand divestitures. We now expect the core effective tax rate for the fiscal year to be slightly below last year's level. All-in GAAP earnings per share are forecasted to increase by 48% to 50%, including the one-time gain from the Beauty transaction.

At current rates and prices, CapEx is more than $0.5 billion headwind of fiscal 2017 earnings. Commodities are a $200 million headwind. Combined, there are about a $0.26 per share drag on fiscal 2017 core EPS. We're working to offset this, but are not yet completely there. Further significant currency weakness, commodity cost increases or additional geopolitical disruption are not anticipated within this guidance range.

We expect adjusted free cash flow productivity of 90% or better. As you know, fiscal 2017 is a year of significant value return to shareowners. We expect to pay dividends of over $7 billion. We reduced outstanding shares by $9.4 billion in the transaction of Coty and we expect to purchase over $5 billion of our stock, in total, about $22 billion in dividend payments, share exchanges and share repurchase this year.

As David said again at our Analyst Day, our objective is sustainably balanced growth and value creation. We discussed our focus areas in depth in our Analyst Day Presentation, which is available on our Investor Relations website, so I won't elaborate on these again today.

Instead, I thought the balance of our time this morning to be most productively spent providing perspective on the most frequent conversation topics and questions we've been engaging with you on at and since the Analyst Day meeting, top-line progress and prospects, retail trade transformation, naturals products and sustainability, cost structure progress and prospects, portfolio, foreign exchange impacts and our management approach to them, capital structure and debt, and the bundle of trade, tariffs and tax reform. I'll take each of these one by one. And then, I'll turn it over to you for additional questions.

First, how do we view our top-line progress and longer term prospects? We stand modestly ahead of plan. We grew organic sales about 0.5-point faster in each of the first two quarters than we were forecasting going in. We're making sequential progress in most of our top categories and markets, and we're doing this despite some significant unexpected challenges.

India demonetization, the elimination of INR 500 and INR 1,000 bank notes that accounted for over 80% of that country's currency in a cash-dominated economy was an unexpected headwind. It swung high single-digits growth last quarter to a decline of high singles this quarter.

Economic crises in Egypt and Nigeria are dramatically impacting category size. Market contractions in Russia, Argentina, and Turkey pose real challenges and we have had to manage the market impacts of politically related currency devaluation in places like the UK and Mexico.

Our organic top-line for the first half of the year has been affected by the portfolio work we're doing in the 10 ongoing categories and by loss sales to our Venezuelan subsidiaries. With all these challenges, we grew organic sales between 2% and 3% for the first half, putting us, as I said, modestly ahead of plan. This is very encouraging as are many elements looking forward.

We're now a more focused 10-category company where purchase intent and choice are driven by a specific job to be done and our products effectiveness in doing it. These are predominantly daily use categories that matter to our retail partners. We said the new portfolio would grow up to a point faster and over the first two quarters of this fiscal year, we're seeing that play out.

We're increasing our investments in market stimulating product innovation. We're continuing to improve and expand unit dose detergents. This premium price form is already past $2 billion in retail sales. We're currently building on this line-up, launching Tide PODS plus Downy in North America. Our scent bead offerings, including Downy Unstopables, Lenor, Gain Fireworks and Bounce, are growing fast and are growing the fabric enhancer category. In the U.S. Downy beads are growing in the mid-20s, and the category is up 7 points.

In Germany, where we launched Lenor beads last summer, the fabric enhancer category is up 6% and our share is now over 50%. Our scent beads are available in 33 countries so far, including our recent launch in the Arabian Peninsula.

Always Discreet has increased market growth rates for female adult incontinence products by roughly 50% in the eight countries that we've launched so far. Last fall, we launched our new Pampers Easy Ups training pants in the U.S. Since the launch, segment growth is 16% and Pampers' share has increased by over 4 points.

We're strengthening investments in brand awareness and trial at the point of market entry and point of market change. 70% of new moms in the U.S. will receive samples of our best Pampers products through our prenatal and hospital programs. Gillette will sample over 2 million FlexBall ProShield razors with the young man on their 18th birthdays. We'll distribute over 30 million laundry detergent samples of new washing machines this fiscal year. We're connecting Always with girls when they most need reassurance and self confidence, as they enter puberty and become new Feminine Care consumers.

We're making organizational changes to improve our execution, speed and responsiveness to local market dynamics. We're increasing our investment of sales resources to improve coverage of fast-growing channels including eCommerce and specialties stores. We're adding salespeople with deep category experiences in categories like Personal Health Care. And we're changing our talent development and career planning approach to build and reward applied category mastery.

In our larger markets, we're establishing direct end-to-end lines from each product category straight through to our retail customer teams. In smaller countries that we manage as market clusters, we're implementing changes to give on the ground business leaders more flexibility to react quickly to competitive threats or customer opportunities.

We see a significant cost and cash productivity runway ahead of us enabling us to keep funding smart market accretive growth opportunities. While we're not without our top-line challenges, we're currently tracking ahead of plan and are raising our outlook for the year.

The next topic you've been asking about is retail trade transformation and the impacts and opportunities for P&G. Our largest opportunity across channels of trade lies in creating and building indispensable brands and products of superior value and in providing go to market experiences that are relevant and valuable to shoppers wherever they choose to shop. If we do this well, we should have opportunity across channels and classes of trade.

We don't currently envision an or retail world, online or offline, mobile or desktop, subscription or à la carte. The mix along each of these continuums will vary by category, by country, by consumer and by occasion. We need to be relevant across this mix. One measure of relevance is market share. Our results vary by category and country, but on an aggregate basis, our online shares are currently equal to offline.

P&G eCommerce sales are now $3 billion. I was with David and the team last week in China while we have more work to do, our eCommerce business there will reach 20% of sales and will exceed $1 billion this year, with an aggregate eCommerce share larger than the next three largest competitors in our categories combined. In Korea, eCommerce is now 40% of our business.

We're building a full toolkit of capabilities we can put to work where relevant. For diapers, subscription can provide convenience and increased loyalty. For SK-II super premium skin care, direct-to-consumer counseling, either in-store or online, can help inform the benefits of regimen usage.

We're prototyping supply chain capabilities to produce and deliver eaches at equal cost per unit to current batch production. We're positioning ourselves for relevance across channels and shopping preferences. We remain fully committed to our omni-channel retail partners and shoppers where most of the business remains and where we also see significant growth opportunities.

Stores continue to hold strong relevance for many shoppers. For many shoppers, stores are more convenient; stopping at one location for multiple items, no packages left at the door; no passwords to manage. They can be more efficient for many shoppers; groceries, gas, banking and pharmacy, all in one stop. Stores can be cheaper, with no membership fees or delivery charges. And for some consumers, stores offer a social experience away from home or a break from out behind their desks.

The important points are that we continue to create and build indispensable brands and products whose relevance extends across channels and are building the skills, capabilities and partnerships to win wherever consumers choose to shop.

The next question, is there an opportunity for P&G to better serve the naturals consumer and the increasingly environmentally concerned shopper?

There absolutely is. We introduced the first bio-based detergent with the cleaning power of Tide with Tide purclean this past year. purclean provides the cleaning power of Tide with 65% bio-based ingredients and it's produced with 100% renewable wind power electricity in a facility operating with zero manufacturing waste to landfill. While it's still early days, purclean holds a 7% share of the pure and naturals segment and is driving over 150% of the naturals segment growth.

We're just launching Herbal Essences with Bio:Renew, a revolutionary blend of antioxidants, aloe and sea kelp that delivers an amazing product experience. The launch includes nine new collections including styling products free of parabens, dyes and gluten, and an alcohol-free hairspray.

We're launching new Febreze Air Effects that introduces a proprietary odor fighting technology delivered in a plastic can versus the previous aluminum packaging. The plastic can reduces the carbon footprint by 11% and results in a more efficient manufacturing process using 15% less energy and reducing waste by 10%.

On Charmin, we've added Forest Stewardship Council labels to let consumers know that 100% of our pulp is sourced from environmentally responsible forests.

P&G is a sustainability leader in the laundry and home care industry. We're the first multinational company to globally remove phosphates from all laundry and auto dishwashing detergents without a compromise in cleaning. We're the first multinational company with 98% of its liquid laundry detergent compacted globally, with a dosage recommendation of 75 mls or lower and we're on-track to reach 100% compaction in the near future.

We believe one of the largest impacts we can make is enabling and educating consumers to use energy-efficient laundry wash cycles. We've set a target to have 70% of all machine wash loads completed in energy-efficient cycles by 2020. We hope to get there with innovations like Tide HE Turbo Clean specifically designed for great performance in high-efficiency machines.

Moving behind the scenes, our supply network transformation enables improvements in environmental sustainability as we move manufacturing and distribution closer to consumption. Since 2010, we've reduced truck transportation kilometers by more than 25%. Over the same time period, our plant sites have reduced water use by 24% and increased our renewable energy use to 10% with a goal of 30% in the next four years.

As we reported in our first-ever Citizenship Report published in December, we've recently achieved our 2020 goal of reducing energy use at P&G facilities by 20%, four years ahead of schedule. And recently, we set a goal for zero manufacturing waste to landfill from all production sites by 2020. These natural ingredient-based products and our industry-leading efforts to improve the environmental sustainability of our operations enable us to increase the relevance of our brands and products with the naturals consumer and the increasingly environmentally conscious shopper.

Next, how are you feeling about your cost structure as it stands today and going forward? We feel very good about our current cost structure having made significant progress over the past several years and we have significant savings opportunities in front of us which should enable us to invest in smart market-constructive financially-accretive growth.

We've talked about the historical progress before. We set a goal to save $10 billion over five years and then accelerated and exceeded each of our productivity objectives over that period. We reduced manufacturing enrollment on a same-site basis by 27% and on an all-in basis including divestitures by 35%. We reduced overhead enrollment by nearly 25% excluding divestitures and by about 35% including divestitures.

Net of reinvestments into innovation, sales coverage, media and sampling, productivity savings have enabled us to deliver constant currency gross and operating profit margin improvement and high-single-digit to double-digit constant currency core earnings per share growth in each of the last four fiscal years. Over that same time period, constant currency earnings in our developing market grew six times faster than organic sales, significantly expanding local currency profit margins. On the balance sheet, we've improved inventory by around 10 days and payables by more than 30 days over the last five years.

Our aggregate 22% core operating profit margin is the third highest in our industry. Only two companies in our primary competitive peer group have higher margins, Reckitt and Colgate, largely due to the categories they compete in. Over the last three fiscal years, we've grown our top quintile operating margin by more than 2 points. What matters more than aggregate margin is the competitive comparison within each category. P&G's category gross margins are higher than competition by an average of about 5 points, up to as many as 14 points. The comparison favors P&G in over three-quarters of the cases. Over the last four years, we've grown our aggregate gross margin by 2 points.

We see similar advantages in core SG&A overhead. When we compare P&G's SG&A overhead costs to a competitive average weighted by P&G's business mix by sector, our costs are more than 100 basis points lower than the competitive weighted average. Over the last four years, we've reduced P&G's overhead costs as a percentage of sales by 50 basis points. Over the next five years, we expect further improvement.

Putting this together at the operating margin level, P&G's operating margins are higher than competition in more than 70% of the category level comparisons. We have double-digit advantages in several and a notable gap in just one. We have further advantages in below-the-line costs. We borrow at some of the most favorable rates in our industry and have a tax rate that is among the industry's lowest.

We're in an advantaged position, but there is significant opportunity remaining to increase structural cost advantages and further improve cash efficiency. We discussed many of these opportunities at our Analyst Day meeting including the transformation of our supply chain and the digitization and automation of more of our work processes both on and off the manufacturing floor. We'll continue to improve productivity up and down the income statement and across the balance sheet, creating fuel to reinvest in smart value-accretive growth.

The next question you've been asking is whether we're confident we'll maximize value with the recently restructured company? We believe we can create superior value with the new company that we've just created. We've been through significant portfolio evaluation and reconstruction over the last two years. We've carefully and thoroughly evaluated each of our businesses for strategic merit, fit with our core capabilities, financial attractiveness and historical track record of return.

As we completed this thorough analysis, we felt several of the categories and more than half the brands had the potential to create more value in the hands of other companies with stronger, more relevant capabilities in the categories in question: pet food with Mars, fragrances with Coty. We moved these categories out, removed all the stranded overhead and monetized a portion of the incremental value for our shareowners.

In the last few years, we've transitioned from a company that competes in 16 product categories to one that competes in 10, from about 170 brands to 65 brands. The businesses we exited represented about 14% of fiscal 2013 sales and only about 6% of our profit. Our new 10 category portfolio has historically grown 1 point faster and been 2 margin points more profitable than the old portfolio.

So our affirmative response to value creation with the current company is not a function of our unwillingness to change or consider alternatives. The conviction comes from having done exactly that. It's only been one quarter – three months, since we completed the majority of the portfolio moves but we're encouraged by the path ahead of us.

Another reason to value creation is maximized with the new company are the synergies that exist within the new company portfolio which are greater than the synergies that existed in the old portfolio. A number of the innovation platforms we're advancing have relevance in multiple of the 10 categories. The supply chain we're transforming is designed to synergize this portfolio with multi-category production and mixing centers.

Most of the businesses we divested, batteries, for example, or pet food, were self-contained from a manufacturing standpoint and had different patterns and endpoints of distribution. The mix of businesses we're moving forward with continues to facilitate highly synergized and cost-effective support functions and maintains scaled purchasing advantages. For some businesses we chose to divest, we had to add a significant number of resources to provide the same level of support, a significant cost to synergy associated with the separation.

The cost dis-synergies to complete separation would be massive. The operational dis-synergy is extraordinarily complex. The tax implications would likely be very significant, as would capital structure dis-synergy's resulting interest expense. To overcome these negatives and create more value with separate pieces, we would have to be comfortable believing in dramatically higher top-line growth rates, more than just 1 point or 2 points, over many years. At current rates of market growth, this would imply sustained growth above market rates.

Having said all of that, our view to value creation will continue to be an extremely dynamic one. We're not wed to the past simply because it is the past. We spent the last two years creating a new company, a new cost structure, a new portfolio. We're now creating the supply chain and the organizational structure and culture that allow us to drive sustained, balanced top and bottom-line growth and are encouraged by the prospects.

The next question, how do you think about FX and how do you respond to it? It might be helpful to very briefly recount how FX impacts reported earnings. There are, as you know, three impacts. First, exchange rates affect the local cost of imported finished products and raw materials. We attempt to recover these cost increases through pricing when local legal requirements and market realities allow it. Though there's a lag between, when a currency devalues, the costs are incurred and the pricing is taken and executed through our channels of distribution.

Second, we need to revalue transaction-related foreign currency working capital balances at the end of every quarter at current spot rates. This includes a revaluation of working capital balances related to transactions between P&G legal entities that operate in different currencies. Balance sheet revaluation impacts are most pronounced when currencies make significant inter-quarter moves such as the sharp devaluation of the Mexican Peso in November.

And last is income statement translation, as a result of foreign subsidiaries that did not use U.S. dollar as their functional currency are translated back to U.S. dollars at the new exchange rates.

Given the complexity of our global supply chain and the volatility of currency markets, the degree to which each of these impacts affects us in a given quarter can vary quite a bit. We've managed through more than $4 billion of cumulative FX impacts over the last four years, nearly half of fiscal year 2012 net earnings. Of this impact, about 30% was from transaction, 20% was from balance sheet revaluation and the remaining 50% was from translation.

At current rate, the FX is more than $0.5 billion headwind to the current fiscal year, an increase of more than $300 million since earnings last October. Our primary approach to mitigating the impact of FX movements is operational hedging. Where financially feasible, we try to denominate expenses in the same currencies in which we're selling products. One way to do this is with local manufacturing. As we localize manufacturing, more of our labor costs are denominated in local currency, more raw and packaging materials are sourced in local currencies.

There're limits, though, to localization benefits. It wouldn't make financial or operational sense to build blades and razors' plants in the 120 countries, for example. And many material inputs such as pulp, lauric oils and the crude oil derivatives are globally denominated in dollars. About two-thirds of our global commodity spend is dollar-denominated.

We're sometimes asked why we don't simply hedge away the remaining FX exposures? It's a good question and something we look at internally and with a different set of outside eyes every year as we prepare our financial plan. There're three reasons we typically don't end up choosing to hedge the majority of the exposure. Up to two-thirds of our foreign exchange losses and a significant amount of our forward exposure is in currencies that are either non-deliverable or are very difficult to hedge. The Argentinean Peso, Egyptian Pound, the Russian Ruble, the Nigerian Naira are some examples.

Second, hedging is neither free nor necessarily cheap. Currency volatility increases this cost. The last shortfall of hedging is the answer is that it solves nothing longer-term. It does nothing to help restore the fundamental margin structure of a business. It simply defers volatility. While it takes time and there's a lag between the hurt and the help (28:54), we typically look to pricing, sizing, mix enhancement, sourcing choices and cost reduction to manage FX impacts.

Russia provides a recent example. Two years ago when the ruble devalued, we were left with negative gross margins across our portfolio of products requiring us to take action.

We initiated pricing and monitored consumer and competitive reaction, making adjustments where needed. Over an 18-month period, we took five pricing actions resulting in a net 25% price increase across the portfolio. We made product sizing changes to ensure affordability with the pricing. Simultaneously, we aggressively reduced non-value added costs and worked to improve our product mix. Our operating approach is measured and practical. It is not defined by a fiscal year or a quarter. It often takes longer than that. We can't stand still, but we also can't get out of balance.

Next question, are we considering any changes to our capital structure? Should we be more leveraged? We remain committed to strong cash returns for shareowners as an important part of overall shareholder value creation. Over the last 10 fiscal years, P&G has returned over $123 billion to shareholders through dividends, share repurchase and share exchanges. We've returned 100% of net earnings over those 10 years.

We've paid a dividend for 126 consecutive years and we've increased the dividend from 60 consecutive years. Our dividend payout is over 70% of net earnings compared to a U.S. peer group average of about 54%. Our dividend yield is currently over 3%, a full point higher than the S&P 500 average. At the start of the last fiscal year, we forecast that we would return up to $70 billion in dividends, share exchange and share repurchase over four years through fiscal 2019. With $15 billion returned last fiscal and about $22 billion projected for this year, we're making good progress towards that goal.

We believe we're in a good spot with our AA- credit rating and should retain it, particularly as interest costs are poised to increase and as potential tax reform creates uncertainty about future deductibility of interest expense. We're financing around $30 billion in debt at an average interest rate below 1.6%. Commercial paper makes up about a third of our debt portfolio. We've been able to access the CP market in several European countries at negative interest rates. Overall, we're borrowing at 70 basis points, 80 basis points below 10-year treasury rates and below five-year rates. These are among the lowest rates in our industry.

A downgrade would provide additional leverage that could be used to purchase more shares or to issue a special dividend. This would obviously be a one-time benefit. It's not a recurring source of cash. Additional debt service, an increase in the cost of debt service and a less efficient mix of debt with lower CP capacity essentially offset over time the modest cash return benefit.

Finally, we've received a number of questions about potential impacts from U.S. policy changes related to trade barriers, tariffs and tax reform. While we certainly appreciate the appropriateness of these questions, we're guessing right along with you on what the impacts may or may not be on our business.

That said, there're a few facts that might be helpful. P&G produces 85% of the product that it sells in the U.S. domestically and we export about 10%. So a net import balance of only about 5% of U.S. sales. The majority of the small amount of imported product is produced in Canada. We estimate that over 90% of the materials we use to manufacture products in the U.S. are sourced domestically.

Material imports occur primarily in the case of insufficient U.S. supply. From our experience in many other markets, local supply constraints are usually taken into account as governments consider tariffs or other border adjustments. As always in tax and trade, the details matter very much, not just the headline rates and rules. As more details are known, we'll update you on how they'll affect our business.

Now wrapping up as I've said before, we leave the second quarter essentially on track to deliver our fiscal year objectives, despite unforeseen and significant setbacks. We're increasing top-line guidance. We're continuing our work to crawl out from under-additional FX hurts, and will remain on plan to return about $22 billion to shareowners through a combination of dividends, share repurchase and share exchange.

Hopefully, you've found this question-guided discussion a helpful one. I'll now be happy to take any additional questions.

Q&A

Operator

Your first question comes from the line of Wendy Nicholson with Citi.

Q - Wendy C. Nicholson {BIO 2081269 <GO>}

Hi. Good morning. My question has to do actually with the Hair Care business specifically, because I know last year at CAGNY that was an area where you cited particularly robust innovation pipeline and all that, but the U.S. market share data has not been good in recent months. So when you called out that as a category that's been particularly strong and has accelerated, can you explain where that's coming from? Is it that the U.S. isn't accurately reflecting what you're seeing, has there been any pipeline sale? Is it international markets? Is it non-track channels? And what's the sustainability, do you think, of the strength in Hair Care given how competitive that category is? Thanks.

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

Thank you, Wendy. The strength in the U.S. is primarily behind Head & Shoulders and Pantene, both of which are doing very well. We're not doing so well on the balance of the portfolio, the smaller brands, particularly Herbal Essence. We are just, as we speak, relaunching Herbal Essence. And I talked earlier in our prepared remarks about the naturals-based focus of that launch and we're very excited about that. So part of the dynamic here has been different growth rates across the brands, but we're, again, relaunching Herbal Essence as we speak.

Across markets, we've continued to do well in markets like China. Hair Care has done very well in Latin America. So there's also a geographic dynamic that's driving the overall aggregate result. You mentioned non-track channels. That's a significant impact and it's going to be increasingly frustrating for this community, I think. If you look at the U.S. on an aggregate P&G basis, I don't have the data with me for just Hair Care, but if you look at all of our categories, there's about a 0.4 difference, or that's 400 – or 0.4%, that explains the difference between reported growth rates in something like Nielsen and our growth rates that we're reporting through our earnings release. That increases dramatically when you grow to a market like China where that delta is up to 6 points. So that's also one of the drivers. And we're doing relatively well from a Hair Care standpoint online.

I think the program – know the program strengthens going forward. We're bringing new initiatives to market, not just on Herbal Essence but on Pantene and Head & Shoulders across geographies. So we feel reasonably good about the sustainability of the growth that we've been delivering more recently.

Operator

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

Q - Dara W. Mohsenian {BIO 3017577 <GO>}

Hey, good morning. So I wanted to focus on organic sales. First, the full-year organic sales growth guidance raise, is that more due to upside from the first half of the year that you already reported? Or are you also more optimistic about the second half that it should be better than what you originally expected? And does the first half outperformance give you greater confidence you'll end the year growing in line with the categories you previously articulated? And then to the last question, you mentioned a gap between untracked and tracked channels. In the U.S., it looked like it was a couple hundred basis points in the quarter. So I just want to get more specifics particularly on the U.S. across your business. Is that just that untracked channels have really accelerated or are there things like shipment timing in there and do you think it's true for the industry or is it more of a P&G phenomena?

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

The answer to your first three or four questions is yes. So, we did do better in the first half than we expected we would. So we're at about 2.5% through the first six months and we expect to improve that modestly as we go through the back of the year. So yes, it reflects progress to date. Yes, it reflects our confidence in the back half, and yes, we would expect we hope to get close to market growth rates as we exit the year. As I said in our prepared remarks, we expect the fourth quarter to be stronger than the third quarter though as always this won't be a straight line, but the answer broadly is yes.

In terms of, are there things besides the non-track channel dynamics driving differences between what you're seeing in our reported sales numbers and the market based numbers, there're always puts and calls in different markets. For example, in China, Chinese New Year fell very early this year. And so there were some part of the normal inventory low that occurs ahead of the Chinese New Year holiday but this year occurred in December, last year would've occurred in January, February. I can't remember exactly when the holiday was last year.

So there are those dynamics, but broadly I think you can look at the 2% on the quarter as a pretty good number representative of the general strength of the business. It might be just a tad high because of the dynamics like the Chinese New Year timing and timing on different year-to-year promotional items, but there's nothing very significant or concerning within that.

Operator

The next question comes from the line of Ali Dibadj with Bernstein.

Q - Ali Dibadj {BIO 15328592 <GO>}

Hey, guys. I have a question on SG&A and a question on just pricing. So first maybe with the second one. It was clearly flat to down everywhere and below FX, although you keep saying you want to offset FX. And I want to understand whether that's kind of the strategy or really just a determination of a weak consumer. And I asked that I guess in the context of, is the plan to grow really from market share versus category growth? We've all seen the Nielsen numbers, for example, slow down, but on a global basis. That's question one. The other one on margins, really, is I totally get the gross margin 210 basis points of productivity. I think that's great. I want to understand does that continue? So should we expect 200s of basis points of improvement on gross margin from productivity and for how long? So is that sustainable?

And then on SG&A specifically, only 20 basis points of productivity, I frankly have a tough time with some of the benchmarking numbers you're putting up there saying you're actually better than peers without including scale and everything else, but 20 basis points seems a little low and I want to get a sense of whether you expect that to ramp up and then the 80 basis points reinvestment, how much of that is sampling versus actual kind of advertising expense increase? Thanks.

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

All right. I candidly can't possibly answer all of those questions, but I will take a shot at the big ones within that. In terms of pricing, when we look at pricing inclusive of promotion as a component of our top-line growth, it was neutral on the quarter. It's been neutral to positive for the past 24 quarters consecutively. It has been positive for the last 12 years.

So as it relates to the promotion part of the question or potential part of the question, as I've said many times, we will be competitive on promotion but it is not something that we typically lead with. We'd rather spend a $1 on innovation or equity when we have that opportunity.

In terms of the flat pricing in the quarter and it's vis-à-vis FX increases, I mentioned when I was talking about FX that there's often a significant lag between when the FX hits us and when we're able to take smart pricing. And if you think about what's happened in the FX markets over the last, call it, six quarters, most of the increase that we're talking about, we talked about $500 million of FX impact versus year ago, I mentioned that $300 million of that has occurred since we reported earnings in October. So the pricing environment that exists in the market now is reflective of a more neutral FX environment and we'll have to see what happens going forward.

We are very cognizant that with a broad dollar move against most currencies that our pricing flexibility will be somewhat limited or will be less than it might otherwise have been. Nonetheless it will continue to be part of the strategy but there'll be a bigger component of cost reduction, mix management, sizing, et cetera.

As relates to margin, I think the gross – I honestly don't have in my head the exact gross margin numbers quarter-by-quarter. I just don't think about things that way, but the general order of magnitude you've seen is representative of the strength of the productivity program. That's going to differ quarter-by-quarter depending on commodity impacts, depending on how much volume we ship, but generally I expect to see healthy gross margin contribution as we go forward.

Recall we mentioned that our next $10 billion productivity program – the majority of that would be in cost of goods, which is part of the reason why you see a divergence between the gross margin benefit from productivity and the SG&A benefit. 20 points a quarter on SG&A, I'll take that any time. We obviously have more opportunity ahead of us, as I said, and we'll see how that progresses. At the same time, we've talked about reinvesting in things like sales coverage, which we are doing and that is also reflected in the overall numbers. I think I'll leave it there and feel free to get back to me later in the day, Ali, if I missed an important part.

Operator

Our next question comes from the line of Lauren Lieberman with Barclays.

Q - Lauren Rae Lieberman {BIO 4832525 <GO>}

Great. Thanks. I'm going to actually try to ask one question, not seven. So wondered if you could talk a little bit more about innovation? I thought one of the things I picked up at the Analyst Day around the Tide purclean that was really interesting was the notion of lean innovation and trying to move a lot faster on bringing things to market and particularly things that are going to be increasingly consumer relevant. So can you talk if there're other examples of where you are already putting that lean innovation mindset to work or if that's still very much on the come? And then any other kind of notable news flow that we should be looking for in the next couple of months? Thanks.

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

Thank you, Lauren. Lean innovation is in its early days in terms of both our learning and implementation. It offers significant opportunity for the reasons you described; quick learning, quick response, lower cost learning, more shots on goal. I was just in a meeting for a couple of hours yesterday afternoon with some of the leadership team on lean innovation, and some of the pilot programs where we're applying that to try to improve again both the cost profile, the speed to market and the number of ideas that we're screening. So we're very excited about the potential it holds, but it's early days.

Operator

Our next question comes from the line of Steve Powers with UBS.

Q - Stephen R. Powers {BIO 20734688 <GO>}

Great. Thanks. Hi, Jon. Just going back to sort of the demand-building efforts that you've been making. I was just hoping if you could frame and quantify the magnitude of the year-over-year increases in demand-building this quarter? And I'm thinking across trade spend, A&P sampling, the whole gamut, relative to the run rate looking backwards over the course of fiscal 2016 in Q1 versus where you think that trend is going forward. I'm trying to figure out if we're at a relatively steady year-over-year increase or if we're poised to accelerate further or decelerate, that kind of thing. Thank you.

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

Sure, Steve. We've tried and we've talked about this a couple of times to both ensure that our demand creation efforts are sufficient and that they are sustained.

One of the problems that we created in the past was a fair degree of volatility in support levels for the business, and it's why I made the remarks that I made, when I was talking about the bottom line guidance, in the context of FX that we're simply not going to make those choices. We are going to continue to support the business in a sustained fashion through the balance of this year, through the balance of next year.

Our support levels are pretty ratable quarter-by-quarter throughout this fiscal year. I don't have all the base period numbers exactly in my head, so I'm not sure what all the index comparisons would be, but I think what you've seen is symptomatic of what you will see going forward.

It's not just, though, the marketing and trade spending that we're viewing as investments in demand creation. It's also the investments in capability, which comes in several forms. We've talked coverage, which we're investing in. We've talked about category mastery, both building and hiring in from the outside, we've been doing that. We've talked about category dedication. We've talked about increasing the flexibility of our operations to respond to changes, whether they're changes in opportunities, whether they're competitive, trade initiated or otherwise.

And so, all of this, we're hopeful has an impact on demand creation. All of this, we're hopeful, is market accretive in its approach, and we still have a lot to prove. We still have a lot of work to do. But so far, it's progressing in the direction that we had hoped.

Operator

And your next question comes from the line of Nik Modi with RBC Capital Markets.

Q - Nik Modi {BIO 7351672 <GO>}

Thanks. Good morning, everyone. Jon, can you just give us an update on in-store execution? I know that's something that we talked about at the Analyst Day and kind of some of the initiatives you're putting in place to really make sure you get the right assortment merchandising, limit out of stocks, et cetera. And has there ever been a discussion internally at P&G regarding moving perhaps the P&L responsibility to the customer teams versus the category or the geographic level? Thanks.

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

Thank you, Nik. I mean clearly, in-store execution is another important element, going back to Steve's question in sufficient demand creation, a significant number of consumer choices on brand and product are made at that shelf. So having the products available, having them be presented in an understandable and compelling way, is all incredibly important.

A couple of things here. One, our whole supply chain transformation, you're familiar with I think the fact that we now are operating these mixing centers in the U.S. which are designed to get us closer to consumption and are designed to reduce out-of-stocks, we've significantly improved out-of-stock levels across our customer base through that, so we're very happy about that. And this is an initiative that's going to be rolling globally in markets as appropriate. So we expect to continue to improve that. It's very important.

We've also tried to get clearer and clearer alignment between our brand teams and our sales teams on what are the drivers of both market growth and brand growth in an in-store context, and then, frame the trade programs and our execution in-store against those drivers, key business drivers, and be very focused in really, really what are the two or three drivers that matter most.

And then, we're measuring performance against a combination of those drivers, which are different by category, was that delivered in-store and gross margin or gross contribution. So there is an element of profit responsibility and profit consideration that's occurring all the way down through to a sales professional in the store. And this is an area I frankly think we have a lot of upside in. There's some great work going on around the world, and it's a clear driver of our business.

Operator

The next question comes from the line of Olivia Tong with Bank of America Merrill Lynch.

Q - Olivia Tong {BIO 7481692 <GO>}

Great, thanks. I just wanted to see if you could talk a little bit about some of the things that you're seeing, some of the key things you're seeing that give you the confidence to raise your organic sales outlook, because we have to go back pretty far to see the last time you guys did that. And is it more a function of the categories getting better or that your execution is improving too? Because I look at like Oral Care, the category seems to be getting better, but then, some of the sore spots in your product grouping, there's still some challenges that we're seeing there like in diapers. Thanks.

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

Thank you. In general, on an aggregate basis, category growth continues to decline at a very modest level, but it's declining. Some of that is developing market dynamics associated with some of the big currency moves. The U.S. is essentially – is pretty stable, maybe a slight uptick here or there. So the majority of the progress that has been made is really execution. And very little of it, in fact, I would have to look at specifically the numbers, but I would expect that the category growth driver of our growth is a negative in the whole equation, a modest negative, but a negative.

Operator

Our next question comes from the line of Joe Altobello with Raymond James.

Q - Joseph Nicholas Altobello {BIO 5113646 <GO>}

Hey, guys. Good morning. I just wanted to stay on the concept of demand creation for a second and the increased investment that you guys are doing in things like sampling and sales coverage. I was just curious in terms of a more broader question, the trend that you're seeing in the overall cost to acquire a customer and to keep that customer versus where it was, say, five years ago. Thanks.

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

There are actually more options available to us to attract customers to our brand and more tools than there probably were five years ago. So done right, there's no reason that the cost of acquisition of a customer should be higher today than it was five years ago.

Having said that, there's a lot more complexity in the shopping environment, in the media environment. And done wrong, you can increase pretty significantly inefficiencies in the cost of customer acquisition. I really can't give you a more specific answer than that, Joe, but I don't see customer acquisition costs as being significantly increased or inflated as we go forward. I mean we can reach consumers and shoppers today in much richer, more direct ways than we ever could.

Operator

Our next question comes from the line of Kevin Grundy with Jefferies.

Q - Kevin Grundy {BIO 16423871 <GO>}

Thanks. Good morning. First one, Jon, a housekeeping question. I don't believe you gave this, and I apologize if you did. Can you provide global category growth and maybe separate that by EM and DM?

And then, the second piece, I wanted to come back to a comment you made, and we've touched on a lot of these topics, but just to sort of underscore the importance here, you talked about long-term investment, even if it means P&G's results end up below the current guidance of mid-single-digit core constant currency. And that sounded new to me, and you tend to be very choiceful about the language that you use. So is this just a matter of the stronger dollar and less ability to take pricing? Is this a matter of promotion ramping may be a bit more than anticipated? I just wanted to kind of come back to that and maybe underscore some of the key drivers behind that comment. Thanks.

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

Thank you, Kevin. We've talked about this both last year and this and we've done it – we've talked about it in the context of FX, which is what's relevant again this year. We need to support our businesses in a sustainable sufficient way, and we're going to do that. The challenge of doing that and delivering an EPS number in the current environment is almost entirely FX. It is not – I mean of course, there are examples by category where promotion levels have increased or by country where promotion levels have increased, but on a broad scale basis, as we look over the total business, that's not the driver of the challenge from a profitability standpoint. It is FX and commodities. And I talked about the $500 million, $0.5 billion of FX, $300 million of which has just come on since October and about $200 million worth of commodity costs.

We're committed to work as hard as we can to offset that, making smart choices on cost and ideally, continuing to push the top-line as well. What we're not going to do is reduce investment that's working to drive growth just to deliver a near-term quarterly number. So that's all we're saying and I think that is maybe inconsistent in totality with our past. I think it's very consistent with the last couple of years, how we've been approaching the business.

In terms of market growth, developed market growth is about 1% overall, developing is about 5%, not a significant change in either versus the prior quarter. That yields about 3% global growth through obviously significant differences by country, but that's the aggregate look at that.

Operator

Our next question comes from Bill Schmitz with Deutsche Bank.

Q - Bill Schmitz {BIO 5038103 <GO>}

Hey, Jon. Good morning. I think just I add more detail to the delta on the commodity and FX inflation, because I think it was $0.12 before and it's $0.26 now. So you kept guidance, obviously, I guess sales are modestly up. So can you just talk specifically how you are going to try to make up for that gap?

And then, can you just talk about two of the categories that stood out good and bad, so like, the Oral Care business, obviously, came in way better. Was that market share gains or was that acceleration in category growth? And then, just very briefly on diapers, you talked about higher promotional spending. What's the strategic rationale for that? Because I know you've talked pretty extensively about promotions being sort of like short-term fix and not a long-term brand equity driver. Thanks.

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

Thank you, Bill. The strategic rationale for the increase in promotion of the diaper category is competitive response. I'll just leave that there.

In terms of Oral Care, we're making very good progress on both our paste business, but also on our more high-end brush business, the automatic or power brushing and that's growing extremely well in markets like the U.S., but also in markets like China.

In terms of the breakdown of FX, I mean you talked about 12 points (sic) [$0.12] (59:29) going to 26 points (sic) [$0.26] (59:31). About three quarters of that occurred since October, and it's across currencies. And if I were to show you a graph today of currencies that are down and up, but I'm sure you have one sitting on your desk, as it is, they're all – there's been a significant move that's occurred.

And as I said earlier, it's different by category, by country, but we're going to try to recover that hit through a combination of price increases where they're relevant, sizing changes, mix, cost. And there really isn't one answer – I apologize – that gives you an aggregate feel for how that happens. It's markedly different by market, by currency.

And one of the big differences is a yen or euro functional currency competitor impacted by the devaluation in a specific market or not. Another variable is, what's happening to local inflation and how are our local competitors' cost structures being impacted by what's happened and do they have a reason to price or not. Another factor is where are we in terms of category leadership or followership, are we the number one brand or are we the number three brand, that has an impact.

So it's a very granular game and a very executional game, but one that we, frankly, despite issues within a given quarter, have done generally fairly well at, over the last four years, offsetting the $4 billion of FX. I mean nobody likes the $3.80 or whatever the EPS number is that people feel we're stuck on, but it could've been a whole lot worse. And we've done, I think, a very good job of managing that and have an eye towards managing even more effectively from a growth standpoint on the top-line as we go forward.

Operator

Our next question comes from the line of Bill Chappell with SunTrust.

Q - William B. Chappell {BIO 1737315 <GO>}

Good morning. Thanks. Hey, Jon, just taking a step back, maybe you could give us a little more in the genesis of this call. I mean it's a different format and kind of walking through the Q&A, it's earlier, I think this is the earliest you've ever reported or at least that I can remember in terms of since the quarter closed and ahead of some of your competitors. And you obviously had a message you wanted to get out there.

So are you frustrated with the stock price? Do you not feel like people understand what's going on with P&G after the Analyst Day? Are there just key issues that you wanted to get out? I mean just a little more color would be great, because it was kind of a surprise, obviously, to see you reporting this early and kind of going through this format.

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

Sure. Sure. Sure. This is a fairly clean quarter for us, and it's obviously not a year-end quarter. So we were able to get our accounts together in fairly short order. And having an earlier call, frankly, allowed me to take advantage of some scheduling opportunities next week, and it's as simple as that.

In terms of the format, I just didn't think you wanted to go through the Analyst Day march again, since that was available for you online and that's essentially the format we've used before is to walk through productivity, walk through portfolio, walk through top-line. I thought I would just diversify a bit and make sure all of the ground was hopefully helpfully covered for you, and that's all there was to that.

Operator

Our next question comes from the line of Caroline Levy with CLSA.

Q - Caroline Levy {BIO 1494597 <GO>}

Good morning, Jon. Thank you so much. As always, I'm very interested in what's going on in China, with particular interest in whether the heavy discounting in the diaper category has continued, and if you expect that to mitigate at any point or has the consumer become used to 20% lower pricing? The other area in China would be detergents where you've had some strong local competition, and Oral Care where you've had strong local competition. So if you could just bring us up to date on that, that would be helpful.

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

I want to step back on China first, and then, I'll get to your specific questions. I think it's very important that we understand that China continues to be a very attractive opportunity. This is a market that is among the highest growth rates across the world on a sustained basis, and that really hasn't changed.

It's a market that is, as we've talked before, premiumizing significantly. Consumers are trading up to better-performing products across categories. As we move out of the one-child policy, there's certainly only upside that exists there, since the economy transitions from more of a manufacturing based economy to a degree of a more consumption-based economy, that's significant upside. And we have a market position there and a capability set that allows us to take advantage and participate in all of those upsides.

So China continues to be – as you know, it's our second largest market both in terms of sales and profit, so it's also a big focus area for us. I mentioned on the call that David and I were there last week. No better way to start the new year than to go to China. And the business is responding fairly well overall. We went from minus 8% quarters not very long ago to the quarter we just completed was plus 3%, the first half was plus 2.5%. Obviously, we still have some work to do, because the markets are growing depending on the category mid-singles.

In terms of specific categories, Oral Care, we're doing fairly well in, and that's being driven primarily by Power Brush and by our Oral-B paste launch, a very premium dual phase product that's doing very well. It's in limited distribution, but that distribution is going to be expanding as that has proven out.

We do see continued promotion in the diaper category, but it's important to note that at the same time that that's happening, that's really a competitive driven dynamic. At the same time that's happening, consumers are continuing to trade up to premium tiers, and that is by far the fastest growing segment of the market.

So the notion that consumers in China have become, if you will, price sensitive, that's certainly not what we're seeing. This is a competitive dynamic that reflects in some ways the size of the opportunity, that reflects in some ways changes in, frankly, currency rates and regulation. But it's not something I would expect to categorize the category for extended periods of time, and it's certainly not a reflection of a desire for lower price on the part of the Chinese consumer. It's very focused on product quality and product performance.

Detergents, our Ariel liquids launch is about on target with where we expected it to be. We do have, as you mentioned, very good strong local competition, but we also have two very good and strong brands in Tide and Ariel, and continue to work to build that business.

Operator

Our next question comes from the line of Jonathan Feeney with Consumer Edge Research.

Q - Jonathan Feeney {BIO 2268157 <GO>}

Thanks very much, Jon. Just one question on Fabric Care. There's been a significant competitive entrant or re-entrant into North America in Fabric Care and I think a lot of people have been wondering what implications that might have. When you think about Fabric Care globally, pricing a little down, and then, significantly down relative to currency, just kind of trying to understand what's going on if – first of all, how North America – what North America pricing looks like, if you could comment on that, and if competitive entry there or anyplace else is, you just mentioned China, but is having an impact. Thank you.

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

The pricing environment in the U.S. market for detergents has become more competitive over the last quarter or two. As a result, you've seen market growth rates go from positive to slightly negative, and that's being driven as much by anticipation on the part of competitors as to what the new entrant is going to do than it is anything else. And we'll see how that plays out.

We're, in terms of how that strategy, how Henkel's strategy is going to play out, it's way too early for us to know that. Our best play continues to be to strengthen our brands, both from a product efficacy standpoint and a consumer delight standpoint which we continue to do.

Operator

And next, we'll go to Bonnie Herzog with Wells Fargo.

Q - Bonnie L. Herzog {BIO 1840179 <GO>}

Hi, Jon. Good morning.

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

Good morning.

Q - Bonnie L. Herzog {BIO 1840179 <GO>}

In light of this tough competitive environment in many of your key categories, how much further pricing promotions do you think is needed to drive share? And then, you've talked in the past about getting your price ladders right in your different categories, so I'd be curious to hear what percentage of your business now has the right price ladders in place versus what percentage still needs to be tweaked and then, maybe highlight which categories might need the most work. Thank you.

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

Sure, Bonnie. I'm limited in what I can say about future pricing directions legally, but I can talk about current status and general strategy, which I'm happy to do. The majority of our portfolio, whether that's defined by category or by market, is where we feel we need to be from a price ladder standpoint. There are clearly in some categories, a couple of categories, where we have opportunities and, again, I really don't want to name categories, but I bet you and I, if we wrote them on two separate pieces of paper, would find some of the same names.

Those are factored into our plans that we've articulated today. We will be competitive on price, but again, we're not going to lead with promotion as a way to grow market share. I don't believe it's a sustainable way to grow market share, because there's absolutely nothing proprietary about it. It can be repeated in a nanosecond and matched, which is very different than either cutting-edge innovation or idea inspired equity building. So there'll be a mix, but we will be competitive. We're generally where we need to be, but not in every category-country combination.

Operator

Our next question comes from the line of Jon Andersen with William Blair.

Q - Jon R. Andersen {BIO 15033263 <GO>}

Thanks. Hi, Jon. I had a question on the kind of the multi-channel discussion you outlined earlier. You mentioned that the company's aggregate online share is comparable or equal to its offline share. I'm wondering if there are any specific markets or categories, one or two, where that isn't the case, and you think there's more work to be done, but you could talk a little bit about those and what your intentions are there? Thanks.

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

Probably the primary example of where we have more work to do, that matters from a size standpoint, is China. In aggregate, our online shares in China are below our offline shares. We're making a lot of progress though. I mentioned $1 billion in sales in online this year, now 20% of our business. That business, the online business, is growing at a 30%, 40%, 50% clip depending on the month or the quarter. And we are building share.

Our online share is growing. It is not yet though to the same level as our offline shares and that's probably the biggest example of where that's the case. And in some other markets, we're overdeveloped, from an online standpoint. And again, it differs dramatically by category.

You can appreciate that categories like Power Brush, like our electric shaving business, some of the – certainly, the diaper business are very well developed online, and some of the others a little bit less so. But if we were to get – and I expect we will – get China to market share equivalence online versus offline, the aggregate statement I would be making then is that our online shares are higher than our offline shares.

Operator

Our next question comes from the line of Mark Astrachan with Stifel, Nicolaus.

Q - Mark Astrachan {BIO 15313233 <GO>}

Yeah, thanks. Morning, everyone. I wanted to follow up on the commentary in the omni-channel and wanting to be where consumers shop. So just curious, has there been a change in discussions around pricing and maybe broader product support for your brands given the increasing challenges faced by those traditional retailers and their seeming need for greater reinvestment to drive traffic, I mean, any sort of commentary on last couple of years, last six months, whatever it is that you've seen that you could talk about would be helpful.

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

Everyone, whether they're an online retailer or an offline retailer, is participating in the race to drive traffic to their specific channel or chain. The biggest help we can give any retailer, whether online or offline, are indispensable brands that consumers need and want. That is, by far, the biggest driver of traffic for them and creating offerings that are relevant for their shopper, which may be different across channels.

If we have products that are not irresistibly superior and don't delight consumers, the notion that we're going to drive store traffic on those items with a lower price is a hard one to get comfortable with. So we're really focused in our discussions with our retail partners on driving their market basket and market growth through better performing brands that ideally are indispensable to consumers.

We're also very focused with them on making our joint operations as cost efficient as possible, which gives them inherently more pricing flexibility or marketing flexibility than they would otherwise have. And that's a big part – certainly not all of the part – but a big part of our approach on supply chain transformation, it's been designed inherently with this customer-enabling focus in mind and reducing their costs as well as our costs, increasing shelf presence in terms of availability, which helps both us and them. So that is by far the majority of the conversation.

Operator

And sir, your final question comes from the line of Jason English with Goldman Sachs.

Q - Jason English {BIO 16418106 <GO>}

Hey. Good morning, folks. Thank you for squeezing me in here. Congratulations on another relatively solid quarter, especially, the progress in the U.S., its boost to aggregate top-line is apparent. I presume this is also an important driver of why mix from a gross margin headwind is abating. So my question's really around sustainability of the U.S. We've talked a few times throughout the quarter about the deviation in terms of reported results from what we can see in our data. But from what we see in the data, it is kind of concerning, overall sales eroding, but reported sales sort of accelerating. And despite a lot of your comments, Jon, on promotions and not wanting to lean too heavily, it looks like you're leaning really heavily on it in the data and sort of underlying, non-promoter base sales eroding even further.

So the data sort of raises questions of whether or not we have a bit of a transitory disconnect between the data and results, which we see from time-to-time, which usually revert, or whether this is now just really different, if we've had a step change in sort of on measured contribution that is going to keep this delta widening on the forward. Can you give us some more color on that and give us a little more reason to sort of not believe the data we're seeing in consumption?

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

I'd say a couple things, Jason. If I step way back and look at, for example, strength of program, front half, back half, I talked about that previously, I don't see a big change there. Innovation improves and increases in the back half in the U.S. We're increasingly getting the coverage patterns that we want to have in place with the talent and deep category mastery in place across the U.S.

So I don't see anything at an aggregate level that says that U.S. sales should decelerate. It wouldn't surprise me in a given quarter that instead of being plus 2, it's plus 1, but that's kind of the range at which I'm looking.

There are categories in the U.S. where promotion intensity has increased significantly. And what I'm not saying is that we're not participating in that. We need to be competitive. I've said that several times on this call and we will be competitive. What we won't typically do is lead promotion spending.

There are also times when certain competitors, for very good reasons, will take a list price decline. And our most efficient response may be at times for a period of time to increase promotion to get to the right price spread versus a competitor. So while that tactically looks like a differential increase in promotion, it's all about getting to a net price, again, us being responsive to what a competitor has offered.

So happy to talk about that more with you later today, Jason, if helpful.

John and I will be around the balance of the day. Thank you for your time, and hope to see most of you here in a couple of weeks at CAGNY.

Operator

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