Q2 2026
2025-12-04

Presentation

Operator

Good day, and thank you for standing by. Welcome to the Brown-Forman Corporation Second Quarter and First Half of Fiscal 2026 Earnings Conference Call. — ***Operator Instructions*** — Please be advised that today's conference is being recorded. I would now like to hand the conference over to your first speaker today, Sue Perram, Vice President, Director, Investor Relations. You may begin.

Susanne Perram

Thank you, and good morning, everyone. I would like to thank each of you for joining us today for Brown-Forman's Second Quarter and First Half of Fiscal Year 2026 Earnings Call. Joining me today are Lawson Whiting, President and Chief Executive Officer; and Leanne Cunningham, Executive Vice President and Chief Financial Officer. This morning's conference call contains forward-looking statements based on our current expectations.

Numerous risks and uncertainties may cause actual results to differ materially from those anticipated or projected in these statements. Many of the factors that will determine future results are beyond the company's ability to control or predict. You should not place undue reliance on any forward-looking statements, and except as required by law, the company undertakes no obligation to update any of these statements, whether due to new information, future events or otherwise.

This morning, we issued a press release containing our results for the second quarter and first half of fiscal year 2026, in addition to posting presentation materials that Lawson and Leanne will walk you through momentarily. Both the release and the presentation can be found on our website under the section titled Investors, Events and Presentations. In the press release, we have listed a number of the risk factors you should consider in conjunction with our forward-looking statements. Other significant risk factors are described in our 2025 Form 10-K and from time to time, in our Form 10-Q reports filed with the Securities and Exchange Commission.

During this call, we will be discussing certain non-GAAP financial measures. These measures, a reconciliation to the most directly comparable GAAP financial measures and the reasons management believes they provide useful information to investors regarding the company's financial condition and results of operations are contained in the press release and investor presentation.

With that, I'd like to turn the call over to Lawson.

Lawson Whiting

Thank you, Sue, and good morning, everyone. I'm pleased to share our second quarter and first half of fiscal 2026 results with you today. I'll start by sharing a few comments on the operating environment and then provide the key drivers and highlights of our top line results, including our geographic performance, strategic innovation and the two unique headwinds Brown-Forman is currently facing. Then I'll turn it over to Leanne, who will share additional insights on other financial highlights, including gross margin and operating expenses and our full year fiscal 2026 outlook, which we are now reaffirming.

While the operating environment remains challenging and uncertain, it has been relatively consistent with our expectations and the themes from the second quarter remain largely consistent with those from the first quarter of this fiscal year. We believe cyclical pressures related to ongoing macroeconomic and geopolitical uncertainties continued to negatively impact consumer confidence and reduced discretionary spending in the U.S. and many developed international markets. On the other hand, we continue to see resilient consumers in a number of our emerging international markets where trends are generally much stronger.

We expect cyclical headwinds to ease over time while also acknowledging that we're operating in a very dynamic industry and some current headwinds may persist over time. With that in mind, our focus remains sharply on managing the factors that we can influence. Now moving to our first half fiscal 2026 top line performance. Our first half fiscal 2026 reported net sales declined 4% with organic net sales flat after adjusting for the A&D impact related to Korbel and Sonoma-Cutrer, which are no longer in our current portfolio.

From a geographic perspective, our organic net sales results were led by the collective strength of the emerging international markets, which provided double-digit growth of 12% and the Travel Retail channel, which increased 6%. While this growth was partially offset by a 6% decline in the developed international markets collectively and flat performance in the United States, it's important to note that both performance in developed international markets and the U.S. sequentially improved from our first quarter results. Diving deeper into the emerging international markets, Mexico and Brazil continued to deliver strong double-digit growth.

While the economic environment in Mexico remains subdued with consumers seeking value and trading down, these conditions have benefited our RTD portfolio, which helped fuel 18% organic net sales growth in the first half of fiscal 2026. New Mix, the world's first tequila-based RTD delivered very strong double-digit growth as the brand continued to lead the category and gain share in Mexico. Our distribution of brands within the William Grant & Sons portfolio also provided incremental organic net sales.

We continue to believe this complementary portfolio provides us additional strength to achieve greater development and growth of our portfolio of brands in Mexico, particularly in the on-trade and in the super premium segment. In Brazil, our strategic approach to building the Jack Daniel's family of brands continues to produce strong results with organic net sales growing more than 20% in the first half of fiscal '26. Jack Daniel's Tennessee Apple and Jack Daniel's Tennessee Whiskey led the growth and gained share as we continue to expand our geographic reach, increased distribution and leverage our revenue growth management capabilities.

In addition, as we mentioned last quarter, we believe premiumization is an opportunity in Brazil, and we continue to focus on increasing distribution for our super premium whiskey portfolio.

The Global Travel Retail channel delivered organic net sales growth of 6% in the first half of fiscal 2026, with growth in most of the major regions as passenger numbers continue to increase, surpassing pre-pandemic levels. The travel retail channel is not only a growth contributor, but also a critical brand building platform. As we shared during our recent Investor Day, the global Jack Daniel's campaign, That's What Makes Jack, JACK has launched in select international airports to position us to reach consumers on this global stage.

Turning to our developed markets. Consumer sentiment and confidence both remain pressured in most European economies, creating a difficult operating environment. While the outlook remains challenging, we are maintaining or gaining share of the whiskey category in 6 of our 8 top European markets. In the U.K., economic conditions are negatively impacting consumer spending and total distilled spirits trends in both the on- and off-premise. Organic net sales declined 13% as we lapped tougher comparisons in the year ago period related to wholesaler and key retailer buying patterns. While off-premise takeaway trends for total distilled spirits as well as the whiskey category are in low single-digit decline, the trends have improved slightly and Jack Daniel's Tennessee Whiskey continues to gain market share. Organic net sales declined 8% in Germany, where similar to the U.K., consumers have been impacted by challenging economic conditions.

This has led to higher rates of saving, softening of total distilled spirits trends and an increase in competitive promotional activity. Despite the operating environment, our super premium brands, Diplomático Rum, Gentleman Jack and Woodford Reserve delivered double-digit growth in the first half of fiscal 2026. The last market I'll focus on today is the United States. Total distilled spirits trends have decelerated but continue to decline at a low single-digit rate as consumers are pressured to make their dollars stretch further.

Even in this environment, we continue to close the gap with TDS and organic net sales were flat in the first half of fiscal 2026. These results continue to be ahead of our depletion-based results as well as takeaway trends driven by the powerful combination of our U.S. distributor changes and the launch of Jack Daniel's Tennessee Blackberry. With distributor transitions now complete, we have turned our focus from transition to execution, especially during the important holiday season.

Two key objectives for the transitions were increased distributor investment funds and improved margin structure, and I'm pleased to see these two areas contributing positively to organic net sales results. Increased dedication and focus from our distributor partners was another goal of our route to consumer transformation in the U.S. and has driven increased distribution for Jack Daniel's Tennessee Whiskey as well as Jack Daniel's Tennessee Honey, Fire and Apple.

The launch of Jack Daniel's Tennessee Blackberry continued to exceed expectations as we progress through the first half of fiscal 2026. As we shared during our Investor Day in October, Blackberry is getting wonderful feedback and buzz from distributors, retailers, consumers, both new and existing and the media. This continued excitement drove shipments to exceed depletions, though the difference between the two decreased as we move through the first half of the fiscal year. We remain encouraged by the strong start in the U.S. and are using the excitement to sustain momentum and drive consumer takeaway.

As I mentioned before, Blackberry is a globally relevant flavor trend across food and beverage categories, and Jack Daniel's has a proven track record of leveraging our global footprint and capabilities to extend the impact of new flavor launches. We also began a phased launch of Jack Daniel's Blackberry outside of the U.S. in select international markets, including the U.K., Germany and France as well as the global travel retail channel.

Similar to the U.S., the initial response from retailers and consumers has been incredibly strong. In the U.K., at Tesco, Jack Daniel's Blackberry was the best new product development launch in the spirits category with more than half of the consumers that purchased the product being new to the spirits category.

The brand also generated a double-digit repeat purchase rate. In Germany, Amazon sold out the Jack Daniel's Blackberry in the preorder shop. And in France, the brand is listed in the major retailers with positive media impressions, visibility in the main aisle and promising initial sell-through in both the off- and on-premise channels. Again, we're pleased with the early stages of the Blackberry launch, and we'll continue executing our strategic phased launch to support scalable and sustainable geographic expansion for the next few years.

Finally, I'll briefly share an update on two headwinds that are somewhat unique to Brown-Forman. Many of you will recall from our previous communications that used barrel sales and the trade dispute between the U.S. and Canada are substantial headwinds for us this fiscal year, and they significantly impacted our first half organic net sales results. Organic net sales for used barrels decreased by more than 60% as the current industry operating environment, particularly for the Scotch and Irish whiskey suppliers continues to pressure demand and pricing.

Canada's organic net sales also declined over 60% as beverage alcohol products produced in the United States continue to be off the shelves in the majority of Canadian provinces. Our much smaller non-U.S. brands, such as Diplomàtico and the Glendronach continued to deliver organic net sales growth, but they were not able to offset the decline of our brands that are produced in the U.S. Overall, the first half of fiscal 2026 has unfolded largely as we anticipated, and we believe we remain positioned to achieve our full year guidance, driven by a series of key actions we've been taking.

These include navigating the current environment with a balanced focus on the short and long term, strengthening our portfolio of brands through strategic innovation as well as a focus on our premium plus brands and RTDs to address consumer trends, making key route-to-consumer transitions, including the U.S., Japan and Italy and streamlining our workforce structure to increase our agility, leverage synergies and enhance our ways of working, which we believe will enable us to fuel the growth of our brands, our business and our people at a more rapid pace.

I remain fully confident in the potential of Brown-Forman, our brands and our people, and I'd like to extend my thanks and appreciation to our dedicated team of employees for their resilience and commitment. Before I conclude my comments, I also want to provide an update on our CFO recruitment process. In August, we announced Leanne had made the decision to retire at the end of the current fiscal year on April 30. Our recruitment process for her successor is well underway. And as you would expect, we are being very thoughtful in our approach to ensure we select a successor who will best position Brown-Forman for the long term.

With that in mind, we anticipate that the process may extend into early next calendar year. In the meantime, I appreciate Leanne's continued leadership, and I'm personally grateful for the opportunity to continue working closely together until her replacement is on board in the next few months.

With that, I'll turn the call over to Leanne.

Leanne Cunningham

Thank you, Lawson, and good morning, everyone. As Lawson mentioned, I will provide additional insights on other financial highlights, including gross margin and operating expenses and conclude our prepared remarks with comments on our full year fiscal 2026 outlook.

First to our gross margin. In the first half of fiscal 2026, our reported gross profit decreased 4%, resulting in a reported gross margin of 59.5%. Our gross profit margin expanded 30 basis points due to a 190 basis points A&D benefit largely related to the conclusion of our relationship with Korbel and the absence of the prior year transition services agreement for Sonoma-Cutrer. This benefit was partially offset by 110 basis points of higher costs, largely due to lower production levels. inflation on our input costs and timing of cost fluctuations and 50 basis points of unfavorable price/mix due to the strong growth of New Mix and lower used barrel sales.

Continuing with our other financial highlights, I'll turn to our operating expenses. In the first half, organic advertising expense decreased 1%, which is largely aligned with our depletion-based top line results. We continue to believe our level of investment behind our brands is healthy with a focus on Jack Daniel's Tennessee Whiskey to support the, That's What Makes Jack, JACK global campaign as well as the launch of Jack Daniel's Tennessee Blackberry. As we shared during our Investor Day, the Jack Daniel's global campaign represents our largest in brand history with the majority of fiscal 2026 expenses to occur during the key selling months of October, November and December.

Our organic SG&A investment decreased 4% following our strategic workforce restructuring initiative. In total, reported operating income decreased 9% and organic operating income decreased 4% in the first half of fiscal 2026. In addition to the $22 million non-operating post-retirement expense related to our workforce initiatives, these results led to a 13% diluted earnings per share decrease to $0.83 per share. Before moving to our outlook, I'd like to take the opportunity to provide you with a few comments related to our capital allocation philosophy. We approach our capital deployment decisions with the core objective of sustainable long-term value creation.

Our capital allocation philosophy balances ongoing investment in the business, including organic investments and acquisitions alongside shareholder returns such as regular dividends, share repurchases and special dividends. First, in the first half of fiscal 2026, capital expenditures decreased by $16 million compared to the year ago period. While we continue to fully invest behind our business, we have completed a number of projects and expansions, which reduced our working capital requirements and improved cash generated. We grew cash flows from operations by $163 million to $292 million, primarily reflecting disciplined working capital management.

Free cash flow, defined as net cash provided by operating activities less purchase of PP&E as presented in the statement of cash flows increased by $179 million to $236 million, reflecting strong operating cash flow generation and lower capital expenditure needs. Secondly, on November 19, 2025, our Board of Directors approved a 2% increase in the quarterly cash dividend, marking 42 consecutive years of dividend increases and 82 consecutive years of paying a regular cash dividend. This is a powerful testament to the strength of our balance sheet, the confidence we have in our ability to generate strong cash flow and to our commitment to returning cash to shareholders.

Finally, as you may recall, on October 2, 2025, the Brown-Forman Board of Directors authorized the repurchase of up to $400 million of our outstanding shares of Class A and

Class B common stock. As of October 31, 2025, we have repurchased $99 million of our outstanding shares of Class A and Class B common stock. Our enduring commitment to our valued shareholders, coupled with a long-term perspective and the focus on building valuable brands is the foundation of our capital allocation philosophy and guides our decisions.

Now turning to our full year fiscal 2026 outlook, which, as Lawson shared, we are reaffirming. We continue to navigate a spirits sector facing headwinds and still expect that the behavior of the consumer and the level of trade inventories will not change meaningfully during the 2026 fiscal year. Our guidance also continues to assume that there will be no change to the current tariff impact, direct and indirect on our products. We strongly believe that we will navigate these short-term challenges through the strength of our portfolio, including strategic innovation, the benefits of our route-to-consumer transitions and our evolved workforce structure.

Our expectations from a geographic perspective remain the same as well. We still forecast continued growth in our emerging markets and the global travel retail channel and expect the depletion-based trends in the U.S. and developed international markets to remain similar to fiscal 2025 with the exception of Canada. The continued unavailability of American Spirits products in Canada resulted in a significant impact to our top line performance. While we are hopeful for the return of American products to Canadian store shelves, we continue to assume this headwind will persist for our full fiscal year and is reflected in our full year guidance.

In addition to Canada, the other cyclical headwind, largely specific to Brown-Forman is the year-over-year change in our used barrel sales. Used barrel sales have returned to levels that reflect the challenging and uncertain operating environment for the spirits industry. We continue to expect used barrel sales to be lower by more than half of fiscal

2025 level.

While we continue to execute our long-term pricing strategy and expect to benefit from our revenue growth management activities and strategic innovation, particularly Jack Daniel's Tennessee Blackberry, we anticipate product mix headwinds due to the faster growth of our RTD portfolio and agency brands in Japan and Mexico. We still anticipate that shipments will roughly be in line with depletions in fiscal 2026.

We anticipate that ordering patterns in the second half of the year will reflect more typical seasonality as our U.S. distributor network moves beyond the phasing impact of the initial transitions and the launch of Jack Daniel's Tennessee Blackberry concludes. For fiscal 2026, based on the currently known factors, we continue to expect a low single-digit decline in organic net sales, and reported gross margin expansion as we believe the benefit from A&D will more than offset the headwinds from negative price/mix and higher costs.

While input costs will continue to benefit from lower agave cost, we project higher costs compared to the prior year, largely driven by the impact of inflation and lower production volumes. In addition, as we shared previously, following the divestiture of Sonoma-Cutrer, we entered into a transition services agreement, which had a negative impact on our overall reported gross margin. The TSA has ended, resulting in a positive impact on a year-over-year basis, and the absence of Korbel is expected to benefit reported gross margin.

Our outlook for organic operating expenses reflects continued management of controllable expenses. Our A&P spend will continue to reflect investment behind our brands that is aligned with our depletion-based top line outlook. We also continue to expect a reduction in SG&A following our strategic workforce restructuring initiative. Based on the above, we are forecasting organic operating income to decline in the low single-digit range. We also continue to expect our effective tax rate to be in the range of approximately 21% to 23%.

We are updating our estimated capital expenditures outlook from a range of $125 million to $135 million to a range of $110 million to $120 million for the full year. While this range is lower than previous years, we have completed a number of projects and expansions and remain committed to our long-held capital allocation philosophy to first invest fully behind our business. And we also continue to focus on reducing our finished goods inventory, which should further reduce our working capital needs and significantly improve cash generated.

Again, our performance in the first half of fiscal 2026 is largely in line with our expectations and provides us the confidence to reaffirm our full year 2026 outlook. As we enter the second half of fiscal 2026, we will continue to focus on growing our portfolio of brands, capitalizing on our strategic route to consumer changes and leveraging our evolved workforce structure. We are committed to thoughtfully and strategically managing through the current volatility and uncertainty while positioning the company to deliver long-term growth.

This concludes our prepared remarks. Please open the line for questions.

Question and Answer

Operator

— ***Operator Instructions*** — And our first question will be coming from Lauren Lieberman of Barclays.

Lauren Lieberman

Just wanted to talk a little bit again about the new distribution partners. It seems like you're starting to see impact, but really gearing up now into the holiday season. So maybe

I would just love a little perspective on how you might compare the plans that are in place for this year's holiday season versus last. And then also the level of caution that you're seeing from these brand-new distributor partners who are going to be excited, but you've also got the known headwinds and questions around the consumer and the category environment.

Lawson Whiting

All right. Let me take a try at this. So a little bit of context, particularly for those that haven't followed us closely this year around what we've done in the U.S. in terms of RTC changes. So California was the first. That was back on May 1. And I think generally, we would say, while the transition took longer than we expected, it is now moving and improving quickly. It's been a strong recovery in Q2. And for the most part, have the teams hired and are – I call the transition complete. The other 13 markets went live on August 1.

So we always have to keep reminding ourselves that was only 3 months ago – 3 months now. It was really all off of Q2, but we had a lot of new partners, obviously – not obviously, but the largest transition markets for Texas and New York. In those places, the teams are in place. Everything is moving pretty much as planned, I think. So – the one learning, I think we had, the primary area where we had more disruption with the emerging brands where it just took a little bit longer. We – as always happens, when you change a distributor, you get – you tend to lose some menus, some drinklist, things like that. So that takes a little bit of time.

We've been addressing that quite a bit. So overall, I'd say we're happy with our new and our existing partners and how everybody is performing. We've closed the gap to TDS quite a bit in the first half of this year. So – and actually, if you exclude RTDs, we're actually above TDS. So there are some green shoots and some good news there. Now to your question, Lauren, about the consumer itself and how we – sort of how we're seeing things, I guess, these days, it hasn't changed significantly. We were talking yesterday as a team that this seemed like a boring quarter.

But in a lot of ways, it was because they're – one, we've had a lot of volatility in the last couple of years, and that seems to be slowing down a bit. But the consumer behavior in the emerging markets continues to be very strong. Global Travel Retail was very strong. We continue to see softness in the U.S. and some of our larger markets in Europe. But in aggregate, I do think – look, you've seen all the other categories within the CPG world of food and personal care and QSRs and retail and a bunch of others, all of whom have gotten more conservative in the last, say, 6 months or so, and we see some of that, too. I think it's important to look at the takeaway trends at TDS for the U.S. they're still declining. They haven't moved a lot, but they have weakened a bit.

So in terms of total distilled spirits takeaway, that is a little bit concerning. But as I said, we're closing the gap on that. Some of that is, we're improving better and some of it is the market is going down a little bit. So I think another important point within TDS, innovation remains the big driver. And that's not only for us with Jack Daniel's Tennessee Blackberry, which has been very important, and I'm sure we're going to talk more about that this morning. But innovation in general is a big factor in the U.S. market these days.

The RTD category is really the only category gaining share. And while not – we'd like to say, while not a trend, we are seeing some weakening for the first time in terms of trade down. And that's really the first time. So I don't want to make too big of a deal about it. But certainly, when you look at $100 and above or $50 to $100, those price points have weakened considerably from where they were, say, 6 months or a year ago.

So – and the only – I don't – not that I don't want to get into structural versus cyclical, you didn't ask that, but I do find it interesting trade down is clearly a cyclical factor, not a structural factor, at least in my head. So if you're weighing out the factors that are out there between structural and cyclical, this is one more that says the consumer is pinched. They are trading down just a little bit, but we do think that's a temporary thing and will turn.

Leanne Cunningham

And then what I'll build on to that is we've been saying for several quarters, we've been trying to strategically navigate the volatile environment at pace, and then we're beginning to see the benefits of those strategic initiatives, like we said in our prepared remarks. Lawson said that innovation is driving growth, and we have our strategic innovation of Blackberry.

From a strategic RTC perspective, we've made the changes to our U.S. distributor network as well as own distribution in Japan and Italy, which are contributing. And then from an SG&A perspective, our evolved workforce. I mean, we're really getting to the point where we are seeing benefits from the initiatives that we have been putting in place to drive the results we reported today.

Operator

And our next question will be coming from Peter Grom of UBS.

Peter Grom

I thought I wanted to follow up on the last point just on what you're seeing in terms of the consumer and the category, but maybe more real time just around the upcoming holiday season, what you've kind of seen through November and a few days here in December. Because you mentioned the categories continue to decelerate in loss, and you kind of touched on the fact that other CPG companies are talking about a weaker performance over the last 6 months.

But I think a lot of those CPG peers even this week are speaking to an operating environment that actually has gotten a bit more worse, I would say, or more challenged over the last 6 weeks or so. So is that similar to what you're seeing? Are you seeing the category get a lot worse quarter-to-date and kind of what you're expecting from a holiday period? And then I guess just underpinning that, right? You noted on the difference between what we're seeing in terms of category trends and your organic results here in the U.S. So should that gap narrow looking forward such that what we see in the data is more aligned with kind of your underlying growth?

Lawson Whiting

Yes. So look, as I said a second ago, the total distilled spirits has weakened in the last 6 months or so, not dramatically, but it has. I don't know about the last month, I don't really track trends quite that short term. But I think the promotional environment, I mean, look, we know the consumer is going to be looking for sort of value and remaining very brand loyal, I think. But the environment remains rational. When you look through the different – like the Nielsen takeaway numbers and the pricing figures within there, we use this term, we used it a few times in the last year of a rational behavior by the other big suppliers.

Tequila has felt some pressure, but honestly, not as much maybe as some would have predicted given the massive drop in the agave costs. American whiskey pricing is holding up fairly well – let's see what is it, down about 0.5 point. So that's pretty close. We're actually a little bit less than that. So holding together. And it seems like just the pricing environment remains rational.

And I think our expectations for this holiday season are – we're trying to be optimistic, but at the same time, we are looking and seeing some of the macro trends that are tough. So I think we're looking forward to a good – I feel like the teams have got us set up, and we've got our new distributors that are very aware of the importance of getting this season right. And from what we are hearing, we're ready to go. So let's see how it all turns out.

Leanne Cunningham

And then to your second question on the U.S., where we are showing a plus 3% for the U.S. on our depletion-based top line results compared to kind of takeaway trends of a minus 3%. What really is driving that gap for us is part of it is the launch of Jack Daniel's Tennessee Blackberry. And as we shared in our last call, it's moving through the process of original shipments impacting our organic results to depletions and then to takeaway.

Q2 for us was the first full quarter of having full shipments and beginning to move into depletion-based results. And we're seeing it bleed into consumer takeaway. As we get into the next couple of quarters, we should see all of those data points balance out. And then the other piece for the U.S. is that benefit that we are referring to from our U.S. distributor relationship terms and the strategic initiative that we put in place for that.

Lawson Whiting

Yes, that's important, actually. We make sure everybody heard that. That improved terms are something that are, I mean, permanent. We're going to have them all year. And so that is giving us some breathing room. It's adding to our top line growth. And I think it is a very successful outcome of what we did. The other point to really highlight, I think, is the lower used barrel sales.

I think maybe a few people underestimated how big of a problem, quite honestly, that is. The sales are down 61% in the first half of the year. It's a pretty big business and a pretty big hit. Our results obviously would have been that much better had that not come through. But that's not – I know that's not – really not a consumer thing. It's more of a global slowdown in beverage alcohol, which is now slowing down barrel sales.

Leanne Cunningham

Yes. And just to build on that just a bit, when we said it in our prepared remarks that when you look at the American produced spirits products being off the shelf in largely all the provinces in Canada and the cyclicality in this environment of used barrel sales, collectively, those two were more than 2 points of impact – negative impact to our top line.

Operator

And our next question will be coming from Nadine Sarwat of Bernstein.

Nadine Sarwat

Two questions from me. Leanne, I'd like to come back to the U.S. You spoke about take-away. So by my calculation, your U.S. net sales growth at an underlying level was a plus 3%. You said takeaway was minus 3%. Can you talk to in more detail breaking down how that 6 percentage point gap will play out over the next 2 quarters?

And then my second question is, you Lawson touched on pricing. In this lower volumes for longer environment, how should we think about how you're approaching strategy when it comes to pricing and what you're seeing from your peers when it comes to calendar 2026, as I know this is top of mind for many people.

Leanne Cunningham

Okay. Nadine, I'll start with your first question, which, again, kind of going back to the U.S. top line depletion pace results at a plus 3%, takeaway at a minus 3%. It's really how we are seeing the flow-through of innovation with the impact of Jack Daniel's Tennessee Blackberry launch, which I just spoke to and also the benefit from the U.S. distributor relationship terms that we're seeing flow through. As we go through the rest of the fiscal year, we expect those to narrow. And then I'll turn it over to Lawson for…

Lawson Whiting

Just sort of the pricing environment, look, I really – we have not changed our sort of philosophy, if you will, on pricing and flow and flow are constantly words that I use with our teams. And so and they're doing that. And the U.S. is tough right now, but like Brown-Forman's pricing across the entire portfolio is down 0.3%. So close to flat in terms of an overall price. And the TDS is a little bit worse than that, but not a lot.

So I'll go back to the line I used a minute ago on sort of a rational performance. It does seem like the big players are holding together. So I feel pretty good about it. Look, we'll continue to monitor the competitor promotional activity and respond when we have to. But we also are very conscious about protecting our pricing and our margins and ultimately, our brand equity. So as I say, I think we feel pretty good about the pricing environment. It certainly could have been a whole lot worse.

Operator

Our next question will be coming from Robert Ottenstein of Evercore ISI.

Robert Ottenstein

Just a couple of follow-ups, please. Lawson, I think you mentioned kind of the $100-plus area is where you're seeing most of the trade down. Does that mean that in the $20 to $30 area, you're really not seeing any trade down at this point? So that's just question number one. Question number two is, I just love to kind of give your thoughts on why you think the current level of advertising marketing investment is the right area and how you come up with that answer and whether you think, I guess, presumably that increased investment wouldn't stimulate demand.

And that's not just for you, but for the industry as a whole, right? Do you think the whole industry is doing the right advertising, marketing out there to create desire and help? Or are we at just a point with the consumer that the returns on those investments don't make sense, both for you and the industry?

Lawson Whiting

Yes. Okay. Let me hit the pricing one first. And I'm just looking at what is Nielsen 3-month value numbers by price points. And yes, the $100 plus is down 18%. But that's a small total volume. Obviously, that's a very small area. But interestingly, from what is this – from $10 to $30, which would comprise a huge percentage of the total – in fact, I can do that number in my head.

It's about 60% or 70% of the total market is in that price range, and they're all down at 4%. So that's where we say trade down. $100 is down that much and the sort of the $30 and below is all down around 4%. The higher price points, ones in between there are more like 6%, 7% down. So it's a pretty clear line of where the pricing environment goes and where the consumer seems to be evolving down. So – what was the other question…

Leanne Cunningham

And then on A&P, yes, we've had our philosophy that A&P spend is going to align with our depletion-based top line growth. But we are continuing to focus on investing behind our brands, and we're focusing on maintaining and growing our share of voice and supporting the long-term brand equity. It is important to remember, we're navigating a challenging environment, and we're carefully managing all of our operating expenses.

But it's important to recall that over the last 5 years, we have added nearly $100 million to brand expense. We continue to work to find initiatives to free up more dollars to continue to reinvest in our brands and our workforce restructuring initiative was one of those where when we get to the place where we can have the right level of benefit, then we will continue to increase.

But again, you go back to our portfolio, it's very tight. A large portion of our portfolio falls under kind of that House of Jack. And so we feel like we get a lot of synergies with the structure of our portfolio of brands.

Lawson Whiting

Yes. And sort of the end of your question around as an industry, I mean, I don't necessarily know. It is a difficult time, and we are testing different ways of advertising and trying to see what reactions we get. But look, the environment is as subdued as it is.

When you've got TDS down around 4-ish it's tough to say we're going to advertise our way out of this. We need – there are other important tailwinds, I think, that will help. So we'll continue to – look, we've had the same guidance for years on – advertising is going to grow about with our depletion-based sales, and I think we're pretty much sticking to that over a full year.

Operator

And our next question will be coming from Drew Levine and he is with JPMorgan.

Drew Levine

Lawson, hoping you could talk to how you're viewing performance of the rest of the Jack Daniel's family of brands following the launch of Blackberry. What the interplay is between the brands, how you're viewing cannibalization, if it's coming in line or better than expected? And then also how that's trending international. You mentioned strong response in U.K., Germany and France. How incremental has Blackberry been in those markets? And then if you could talk to additional market launches in 2026.

Lawson Whiting

Yes. So look, it's only been 3 months. So it is difficult to draw on is it impacting Blackberry or is it impacting the rest of your flavors. So historically, there haven't been that much – the cannibalization has been minimal. We do recognize every time you do a new one that you're going to turn up that a little bit. But in the first 90 days, I can't – we don't really know yet. So now the whole – the plan for Blackberry over the next couple of years, we obviously have launched in the United States.

We've launched in a handful of markets in Europe, but we are not global by any means yet. And so our goal or benefit for this is to make it a multiyear benefit to the company, not just a couple of quarters or even 1 year. And that's one of the major, major benefits that Jack has over so many of its competitors in the flavor conversation, it's because it is so global. We also haven't done all sizes. I mean there's lots of things that we're doing to try to stretch the launch out to be a benefit for some period of time. So – and we know that, especially when you do a launch like this, it benefits the whole portfolio or the whole Jack Daniel's family of brands because we get a lot of incremental displays.

So that was the comment about Tesco and some of the others in France and Germany, where they all want to get on board of this big launch and then that kind of sucks in the rest of the portfolio around it. And so right now, we are pleased. We really are. We've gotten good consumer feedback. We've got great trade feedback. And feel like we've got a very successful innovation.

Leanne Cunningham

And then one last detail to your question about the markets. Again, we, as you know, launched in the U.S. in August. This fall, we were launching in the U.K., France, Germany, Poland, Czechia, Turkey and GTR, just so you have that information.

Lawson Whiting

But we didn't go to a place like Brazil or…

Leanne Cunningham

Absolutely…

Lawson Whiting

A lot of others…

Leanne Cunningham

It’s more developed in Europe at this point.

Lawson Whiting

There are huge flavor markets for us.

Operator

And our next question will be coming from Chris Pitcher of Rothschild Company and Redburn.

Chris Pitcher

A follow-up on the reduced CapEx outlook. It still looks like it’s a sort of a growth number ahead of depreciation. But in terms of barrels being purchased and warehouse space being expanded, can we read into that, that you’re probably getting to a stage now where you’re going to maintain or perhaps even reduce the value of your barreled whiskeys? Obviously, we’ll get a bit more color with the 10-Q.

Leanne Cunningham

Yes. I mean from a capacity perspective, from a CapEx perspective, we currently have the distilling, warehousing and bottling capacities that we need to support the future demand that we look out to. And that was one of the reasons why we were able to reduce our capital expenditure outlook. And then from an inventory perspective, as we have been sharing with you for several quarters, all through F ’25 and even into F ’26 with the volatility that was caused through the pandemic and supply chain challenges that we had, we’re in a position where we are producing at lower levels.

We have been very clear about that and the impact that’s having on cost as we are trying to reduce our finished goods inventory levels that we have around the world. We have made really good progress on that as it’s – but we still have to work through some of the strategic tariff mitigation inventories we had out there. And we also took in finished goods inventory to support the new agency brand business that we have. And then from a barrel whiskey perspective, if you look kind of consecutively over the last few quarters, it continues to moderate.

And again, that is just us adjusting to the long-term demand that we see against the supply that we have. And so with some of the performance levels that we have, we have the ability to balance those as we go forward.

Lawson Whiting

Yes. Let me just add to that a little bit. You'll notice we did create a Schedule E in our earnings release to get everybody's eyes a little more focused on free cash flow because we do see some opportunities going forward with lower levels of CapEx going forward. And as we wind down or work through the inventory that we have, it's a material change and some good news in terms of benefits to the balance sheet and just the free cash flow. So yes, we feel pretty good about the outlook there.

Operator

Our next question will be coming from Andrea Pistacchi of Bank of America.

Andrea Pistacchi

My question is on cost savings actually. So your SG&A in Q2, if I calculate more or less correctly, I think declined around 1%, 2%. And the run rate in recent quarters had been more than that, more like 6%, 7%. So could you comment, please, on the momentum of your cost-saving initiatives, particularly as we go into the second half when you'll be lapping some of the more substantial initiatives that you've taken in the last 12 months?

And– I mean this is relevant given the environment which remains – visibility remains low. So timing of improvement of top line is still a bit uncertain. So just wanted to hear about your ability to potentially accelerate savings in this environment and whether maybe there were any one-off factors in the SG&A in H1, Q2?

Leanne Cunningham

Okay. For SG&A, it really is about the year ago period as we were beginning to envision what our new evolved streamlined, simplified workforce structure would be ahead of that announcement, there were a large number of open roles in the year ago period as well as an adjustment to our full year compensation expectations. So that's why you're seeing that kind of negative one, first half in this first half of this year.

We'll continue to see some benefits as we go forward in the year to go, but you are correct that it will begin to moderate as we lap that mid-January announcement and really that fourth quarter of last year benefit that we'll be lapping from an SG&A perspective. We continue, as we had previously said in our prepared remarks, we are doing in this environment, everything to carefully and tightly manage and control all of our operating expenses and controllable costs where that is available.

Operator

And our next question will be coming from Steve Powers of Deutsche Bank.

Stephen Robert Powers

Lawson, in the first half, the shipments across your total business came in slightly ahead of depletions as you've highlighted. I guess, is it fair to assume that, that reverses and that shipments and depletions end up the year essentially in line? Or because of those distributor term favorability items and progressive launches of Blackberry, et cetera, is it otherwise fair to assume that you end up maybe a little bit ahead on shipments versus depletions? Curious on that.

And if you could, within that, I don't know how far you can go on this, but any quantification of the size of those distributor term benefits or any details on exactly what you may have been able to kind of carve out in terms of what makes up those benefits would be helpful.

Leanne Cunningham

Okay. Well, I will start with your comment on shipments versus depletions. And again, like we said, we expected stronger shipments in our first half because we had to load in the new distributors in the U.S., and we were launching Jack Daniel's Tennessee Blackberry. We said in our last call that we expected that to moderate as we got to the first half and that our first half top line organic sales would be in line with our guidance. Now here we are today, a little bit better than that, and that is after the more than 2 points impact from Canada and used barrels.

But that's really about Jack Daniel's Tennessee Blackberry exceeding our expectations. We do expect that for the full year, the gap between shipments and depletions will narrow. And if you look at the gap between where we were at Q1 and where we are at the first half, it has already narrowed significantly.

We expect for it to narrow more. But except to the extent of the continued launch in this year of Jack Daniel's Tennessee Blackberry. So those shipments might be slightly ahead of depletions. One thing that I will say that we have to keep in mind as we go into the year ago period from an organic top line perspective is that New Mix, which has been one of our strongest drivers of growth in the second half, we will begin to comp and compare against those very strong double-digit growth percentages that we saw in the year ago period.

So we'll just have to keep that in mind as we look in the year-to-go period. And then your other was the benefit from distributor terms. We haven't been specific to that other than to say our expectations are, we'll have greater focus, more dedication, distributor investment on the behalf of our brands and kind of better terms. And we are seeing the benefit of those flow-throughs, but we haven't been more specific than that.

Operator

Our next question will be coming from Filippo Falorni of Citi.

Filippo Falorni

I have two questions. The first one on emerging markets, clearly still solid double-digit year-to-date. But if I compare to the year-to-date in Q1 of 25%, it implies a big deceleration in Q2. So maybe can you walk us through what drove those – that deceleration? And to your point, Leanne, as we think about the second half of the year, cycling tougher New Mix comps, what are your expectations on emerging markets for the second half?

And then my second question is on gross margins. Can you help us understand the puts and takes in the second half? Obviously, you're still going to have the Korbel benefit flowing through from an acquisition divestiture line. The TSA should be largely done – and then maybe on the commodity cost environment, should we see some benefits from agave in the back half? And is the expectation still for gross margin expansion for the year?

Leanne Cunningham

Okay. Great. Well, I'll start with – it's always dangerous from – on an emerging markets perspective, it's always dangerous to kind of look at 1 quarter. We never had the expectation that emerging markets were going to stay at a plus 25%. We're very pleased at the end of the first half, we are at a plus 12%. There was just some timing in there. There's so many great things to talk about, and we tried to share them in our prepared remarks, which Mexico is doing great with New Mix being boosted by strong takeaway and gaining share, and we've got the emerging brands.

Brazil continues to be a very strong market for us as we are geographically expanding and we have the growth of Tennessee Whiskey and Jack Daniel's Apple and our super premium. We expect those things to continue. They may moderate more as we go through the year. And specifically with – I guess I just mentioned, with New Mix being one of our largest contributors to growth. As we get to that second half, it will begin to comp those very strong prior year growth rates in the second half.

So we're really pleased with our emerging market growth to date, and it will continue to be a growth driver for us for the full year. Then to your gross margin question, as we look at the full year, we do expect to continue to benefit, like we said, from A&D, which is the absence of Korbel and the prior year Sonoma-Cutrer TSA being completed. From our price mix perspective, we continue to benefit from our long-term pricing strategy that Lawson just spoke of, and we'll continue to have positive portfolio mix from Jack Daniel's Tennessee Blackberry and then those higher net pricing across the U.S. from our distributor relationship terms we talked about.

But due to agency brands, RTDs and lower gross margin or lower used barrel sales, we do expect that to be a headwind for us. And we do expect as well continued pressure from input costs, whether we will have some benefit from lower agave cost, but that will be more than offset by higher input inflation costs on our inputs and lower production volumes as we continue to reduce our finished goods inventory that we've talked about to reduce the working capital intensity on our balance sheet. But net-net, for the full year, we do expect A&D will more than offset the headwinds of the negative price mix.

And then to your very last piece, which is on our commodities. From a commodities pricing perspective, it's kind of returned to more historical – in line with more historical inflation rates, even wage and general inflation are now closer. With agave, there is a benefit to our cost, but it remains high because with the slowing of our demand, it is taking us longer to work through the high-cost bulk tequila that we have, the aging inventory and the finished goods.

Wood, we've talked about, it is fully outsourced now, and we will see benefits to that in the future, but that will take a period of time as it moves through our aging process. Grains are continuing to be a little bit favorable, and we are seeing a kind of steady pricing to a slight decline. And then our glass is forecasted to be a little bit higher, but that's largely related to the cost of natural gas.

Operator

And our next question will be coming from Kevin Grundy of BNP Paribas.

Kevin Grundy

Nice to see at the Investor Day recently. Two-part question for me, if you indulge here. Just first on the near term. So the organic sales, both on the top line, the organic sales guidance implies down low to mid-single digits in the back half of the year. Just wanted to kind of get your sense of where you think you fall out within the range given all the moving parts that we talked about, some narrowing of the gap with ships and depletes with distributor changes, et cetera.

So that would be number one. And then number two, and Lawson, this may bump up against the structural versus cyclical sort of debate, but it's kind of the elephant in the room and worth getting your updated thoughts. What's the level of confidence on the building blocks that Brown-Forman can get back to growth?

Very specifically, what macro and micro factors are you looking at? I know you're engaging with your consumers constantly. What are they telling you? What are you getting in consumer surveys, et cetera, is an entirely cyclical dynamic and there's not something more structural going on – because as you're very well aware, I mean, there's no shortage of sort of data points out there, whether this is cannabis, health and wellness, consumers moving away, et cetera.

So anything you can do there to kind of reaffirm, I guess, confidence that the spirits industry is not sort of going to perpetually be in sector decline?

Lawson Whiting

You want to start with the structural cyclical, my favorite one. Look, I mean, to be honest, we spent a lot of time last quarter talking about this, and there's not that much new information out there. In terms of what hit the media, I think, at least in the last even few weeks around GLP-1s becoming a bigger factor of the potential for an oral – for a pill as opposed to taking a shot, is that going to increase the number of people on it. I mean that's a future thing.

That's not a today thing. So that there's a headwind there. The cyclical one I talked about earlier around the trade down and some of those, I think, is a real factor going on right there. But the rest of it is kind of about the same. It's somewhere in the middle. To say we're seeing a lot of green shoots right now. I mean, you can't say that about the U.S. spirits market in aggregate. I think we've said this morning that our own performance is getting better. So congratulations to the teams for that. But I honestly don't think the environment has changed that much over the last quarter in terms of a structural cyclical argument.

Leanne Cunningham

And then I would say to your last question, Kevin, on the top line, I would say with the volatility that continues to be in the marketplace and the operating environment, we're not in a place where we are narrowing our top line range.

It does assume here, we said it flat at the end of the first half. We do expect it to continue to moderate and to come in line with our guidance, and that is about some of the things we've talked about today which is we've loaded in a lot of our initial inventory for the Jack Daniel's Tennessee Blackberry launch and our new distributors in the U.S. that should now begin to normalize in our second half and look like something that is more traditional for the back half of the year, and we'll begin to comp New Mix from last year.

So we do – we're not at a point yet with the volatility we have and where we sit, but we are very pleased that our half year results have come in kind of in line with our expectations.

Operator

And in the interest of time, we're concluding this Q&A session. I would now like to turn the call back to Sue Perram for closing remarks.

Susanne Perram

Thank you. And thank you to Lawson and Leanne and to everyone for joining us today for Brown-Forman's Second Quarter and First Half of Fiscal Year 2026 Earnings Call. If you have any additional questions, please contact us. With the holiday season upon us, we hope that everyone celebrates the season responsibly and that your spirits are bright. From all of us at Brown-Forman, we wish you the happiest of holidays. With that, that concludes our call.

Operator

And this concludes today's program. Thank you for participating. You may now disconnect.