Brown-Forman Corporation, Q2 2011, Earnings Call 2010-12-09

Presentation

Operator

Good morning. My name is Kila, and I will be your conference operator today. At this time, I would like to welcome everyone to the Brown-Forman Second Quarter Fiscal 2011 Conference call. — ***Operator Instructions*** — I will now turn the call over to Ben Marmor.

Ben Marmor

Good morning, and thank you for joining us for Brown-Forman's Fiscal 2011 Second Quarter Earnings call. This is Ben Marmor, the Director of Investor Relations at Brown-Forman. Joining me today are Paul Varga, our President and Chief Executive Officer; Don Berg, Executive Vice President and Chief Financial Officer; and Jane Morreau, Senior Vice President, Finance. Paul will begin our call this morning with a few remarks about our quarter and Don will provide additional commentary about our guidance and recent business performance.

As always, 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 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 fiscal 2011 second quarter. The release can be found on our website under the section titled Investor Relations. We have listed in the press release a number of risk factors that you should consider in conjunction with our forward-looking statements. Other significant risk factors are described in our Form 10-K, Form 8-K, and Form 10-Q reports filed with the Securities and Exchange Commission.

During this call, we also will discuss certain non-GAAP financial measures. These measures and the reasons management believes they provide useful information to investors regarding the company's financial conditions and result of operations are contained in the press release. And with that, I will turn the call over to Paul.

Paul Varga

Thank you, Ben, and good morning, everyone. I'll just say a few comments before turning it over to Don. Overall, we're pleased with the quarter we reported this morning and the first half of our fiscal year on a handful of fronts. I'll cite three. The first is our just overall performance. We feel that we had good gross profit growth on the heels of our international growth in the first half. And as you may have seen, as a result of that and our current views on foreign exchange, we've raised our guidance for the full year.

On a second front, we're really pleased in the first half to have been able to make strategic investments behind the business and I'll cite two areas. One, where in this first half investments we made behind our developing route-to-market around the world and most notably in markets such as Germany, Russia, Brazil and Canada. And then secondly, strategic investments we've made behind the brands, primarily in the areas of packaging and line extensions. We feel that these investments position the company for growth going forward.

And then finally, I would just want to mention that we're pleased with the continued strength of our balance sheet and our overall financial flexibility. This would be evidenced by the recent increase in our regular dividend and then last week's announcement related to a special dividend. So in general, we have really good feelings about the first half of the year. And with that, to talk about it a little more specifically, I'll turn it over to Don.

Donald Berg

Okay thanks, Paul. Good morning, everyone. I also plan to keep my comments brief this morning since later today, we'll spend some time discussing our global strategy at our Analyst Conference. As you all know, this morning, we issued our fiscal 2011 second quarter earnings release, and we raised our guidance for the year. Our performance during the second quarter and for the year-to-date is essentially a continuation of a story that we have experienced over the prior six months.

Given that performance are several important takeaways. The first takeaway is that we believe we're on track to deliver solid results for the year. We've raised our EPS guidance and have narrowed the range to $3.18 to $3.42. This movement, as Paul says, primarily driven by foreign exchange along with our gross profit expectations that are associated with our international growth and production efficiencies.

For our underlying operating income, we are maintaining our guidance for mid single-digit growth. Another takeaway is that during our second quarter, our gross profit growth remains solid at 3% on an underlying basis, an improvement over our fiscal year 2010 gross profit growth of 1%. The current 12-month run rate for gross profit has also improved to 3%.

Once again, the development of our business internationally continued to drive our growth with underlying international sales of 6%. Underlying sales in the U.S. remained soft but improved from our first quarter. While we're working to improve our U.S. trends, we are pleased with our success internationally in both developed and emerging markets.

A third key takeaway is our operating expenses were in line with our expectations. On an underlying basis, advertising expenses were up about 1%, underlying SG&A was up 6% during the quarter, reflecting the planned strategic investments we mentioned in the first quarter, primarily related to route-to-market changes, as well as the incremental pension expense that we noted in June, and that we'll continue to see throughout the rest of the fiscal year.

My final key takeaway is that the economic environment, although improving somewhat, remains fairly volatile. So with those highlights for the quarter, this morning, I'd like to focus some time on our international growth story.

During the second quarter, we continued our broad-based gains internationally in both developed and emerging markets, starting first with our progress with Jack Daniel's Tennessee Whiskey. In developed markets, both France and Germany grew Black Label depletions in the low double digits during the quarter. These two countries each improved on their 12-month growth trends and combined are closing in on the million case mark. While both Spain and Italy continued to be a bit volatile, both countries grew Black Label volume nicely in the quarter, building on their positive performances from the prior quarter. On a 12-month basis, both countries grew in the mid single digits.

Australia also grew Jack Daniel's Tennessee Whiskey in the low double digits as it has discontinued to be one of the few consistent growth markets throughout the entire global recession. The U.K.'s depletions declined in the quarter, but mostly reflecting a change in retail buy-in patterns from October to November. On a 12-month basis, volumes in the U.K. were flat.

Growth also continued in our emerging markets. Like many of our competitors, we have seen some nice growth in Latin America and Asia, although for us, it is on a relatively small base. Altogether, our Jack Daniel's BRIC business is a little over 250,000 cases. We experienced expected disruption in Russia with our change over to a new distribution arrangement. And excluding Russia, year-to-date, BRIC has grown at about 10%.

Mexico has been a Jack Daniel's success story for a number of years, especially since acquiring our own distribution platform through the Casa Herradura acquisition. Here, Black Label has continued to grow at solid double digits. At these growth rates, this market is beginning to close in on the 100,000 case milestone. Similarly, another important story for Brown-Forman, the release of the emerging markets throughout Eastern and Central Europe and the Middle East. Poland last year surpassed 100,000 cases of Jack Daniel's, and we have seen vibrant growth for a number of quarters.

Last quarter, growth accelerated over 35%, bringing that market's 12-month growth rate to over 25%. Our Central Europe region, which includes countries such as Austria, Netherlands, Hungary and the Balkans is another nice growth story for Jack. Altogether, over the last 12 months, we depleted over 325,000 cases in this region and the quarter's growth here also accelerated into double digits, bringing this area's 12-month growth to close to 10%. Our Eastern Europe, Middle East and Northern Africa area has also seen nice double-digit growth during this quarter. This area, which includes markets such as Turkey, Bulgaria, the Ukraine and Israel sells well over 400,000 cases per year and now has a 12-month growth of over 30%.

Before moving off of Jack Daniel's, let me mention that the Jack family of brands grew net sales by 5% for the second quarter. Both Gentleman Jack and Single Barrel had nice depletion growth rates during the quarter and over the 12-month period, both grew in the double digits.

Jack Daniel's RTDs grew depletions 18% fiscal year-to-date, adding almost 600,000 cases in this recent six-month period. In Mexico, which just launched the RTD a little over a year ago, we are already selling almost 300,000 cases on a 12-month basis.

Switching gears to Finlandia. Eastern and Central Europe are also important markets for this well-established vodka. Here, Poland, Finlandia's largest market returned to depletion growth this quarter. Other Eastern and Central Europe markets that showed volume growth include the Czech Republic, Slovakia, Hungary, the West Balkans, Bulgaria, Romania and the Ukraine. Altogether, these markets represent over 300,000 cases per year for Finlandia.

For Southern Comfort, all of Europe's depletions grew just over 1% for the quarter, bringing its year-to-date trend to flat. As we mentioned, these international performances were partially offset by a soft performance in the U.S. Both Jack Daniel's and Southern Comfort showed some modest improvement during the quarter but they are both still underperforming our expectations in a very competitive environment, not only in terms of programming efforts, but particularly with recent innovations and new product introductions.

We are looking at our entire portfolio and across the entire marketing spectrum as we react and respond. For example, our recent launch of Southern Comfort Lime is targeted to the recent success of flavored whiskeys, as well as the shot drinking occasion. We've also recently introduced new packaging for Southern Comfort. On other fronts, other examples of innovation that we've brought to the market recently include new packaging for Herradura as well as a whole new entry in the vodka category with Chambord Vodka.

Two other mentions before moving on, el Jimador during the quarter continued to grow depletions nicely in the mid single digits, led by double-digit growth in the United States. Herradura also grew in double digits for the quarter with double-digit growth both in the U.S., as well as in Mexico. And finally, I would point out that for our fiscal year-to-date, depletions for our super premium brands have been growing at about 10%.

Before closing, I'd liked to touch on a number of announcements recently related to our various distributions of cash to shareholders. First, our share repurchase authorization expired December 1. During that program, we purchased nearly two million shares for $170 million for an average price of just under $60 per share. In addition, we also recently announced a $1 per share special cash dividend on top of a 6.7% increase on our quarterly dividend. With our strong cash flows and strong balance sheet and current debt level, we are able to return cash to shareholders while continuing to have ample funds available should an attractive acquisition opportunity arise that we believe could create additional value.

In closing, based on our underlying sales and gross profit trends, and our expectations of total spending over the balance of the year, we continue to forecast mid single digit growth in the underlying operating income. Due to foreign exchange movements along with gross profit expectations associated with international growth and production efficiencies, we're increasing our expectations for fiscal 2011 and narrowing our guidance to $3.18 to $3.42 for the year.

On both a reported and an underlying operating income basis, that means we expect significant growth for the rest of this fiscal year. This is based primarily due to the comparables from a year ago in terms of SG&A expenses. As you think about the rest of the year, please remember that last year, we incurred a $0.07 per share, non-cash charge for a trademark impairment in the third quarter, and we also incurred various costs related to some compensation programs in the third and fourth quarters that we currently do not expect to recur this year. So with that, let me say thank you for listening, and we'll now open the call for questions.

Question and Answer

Operator

— Operator Instructions — The first question comes from the line of Dara Mohsenian of

Morgan Stanley.

Dara Mohsenian

Paul, I guess, I'm struggling to see why you guys are pleased with the top line performance in the quarter just because on a two-year average basis, so if you include the comparison from last year, your underlying sales growth was up 0.5%, which is a deceleration from the trends we've been seeing recently. And obviously, numbers kind of bounce around on a quarterly basis. But I guess the concern from my standpoint would be that it's inconsistent with the broader recovery that we're hearing about from others in the Alcohol segment recently. So is that a fair point? Can you give us an update on how you're performing from a market share standpoint within the industry, and particularly in the U.S. geography?

Paul Varga

I guess I'm not looking at the rolling numbers that you're referencing. But the one that stands out to me, is I think our fiscal year '10 underlying sales growth was about 1%. And so for the first half of this year, we're reporting 2%. So yes, it's not at some of the levels that we would have seen say in sort of pre-calendar year '08. But in terms of the progress from virtually little growth to edging along toward 2%, we find that to be helpful. And in addition to that I think as we put some spotlight on the fact that the gross profit growth of the company is I think four consecutive quarters running at 3%. So we're seeing some progress and improvement in that while also being able to make investments. So that was the basic gist in my opening. As it relates to market share, I think, I would just cite for our leading brand, Jack Daniel's, I suspect that the 5% family sales growth rate for the first half, I mean, we don't get it on a timely manner the ability to compare that sort of trademark performance to say underlying whiskey globally. But my guess is, thinking about it historically, that globally, the Jack Daniel's trademark is definitely gaining share worldwide. So that makes us pleased, I think. We cited this over the last couple of quarters the area where we really have focused a lot of attention right now is on Southern

Comfort, which has been losing some share. And to a lesser extent, I think there's some extenuating circumstances around Finlandia more so, but same thing, I mean they are good-sized brands for us, and so those would be – while Jack Daniel's is leading those two would be pulling it down. So I think Don intended to outline that as the main task ahead of us where we're going to get our growth. Along with a bunch of these other ones that he cited that off of smaller bases do add up. So looking across the whole landscape, I suspect particularly the United States where we have been losing share and were really – I think Don's comments were right on the money about sort of focus we got to place on Southern Comfort particularly but also on Jack Daniel's in order to make sure we're getting ever more competitive in the market place. So but overall, yes, if I look at the top line results across the globe, I feel pretty good about this first half.

Dara Mohsenian

And would you expect to see a continued recovery sequentially then when we look out to the back half of the year, given some of the progress you think you've made recently in the first half?

Paul Varga

Yes, I think so. A lot of it, you have to go market-by-market, Dara. And if I was looking at some of the U.S. distilled spirit trends just broadly in terms of volume metrics, three-month versus 12-month and if I was looking at some of the pricing and mix trends in that market, we see slight, not up to our expectations yet, improvement from first quarter to second quarter on Jack Daniel's and Southern Comfort both. And the industry overall is starting to show a little bit of more recovery with each passing quarter. So, yes, to the extent that continues, and we're also able to put some of the activities in place across the mix that Don referenced and be able to accelerate our share growth there, yes, I mean I would hope for a better recovery in the second half. And then, more likely as you really look ahead, a lot of our thinking about this is putting them on platforms to grow out into

FY ‘12 and ‘13 as well. But yes, we would keep our fingers crossed that sort of modest recoveries we’re seeing and some of the top line numbers would continue.

Dara Mohsenian

Has your long-term expectation around revenue growth changed at all given the circumstances from the last couple of years? At what point do you think you see kind of a normalized recovery back up to that mid-single digit type of range that you guys were posting before the downturn?

Paul Varga

I hope you’re coming this afternoon to hear us talk about some of the 10-year. A lot of that is going to depend. I’d love to hear your perspective on global economies and globally GDP growth and revenue growth. One of the thing’s that’s so interesting about our picture, I think our financials stack up pretty well against many of the industry, many of the leaders in the industry over sustained periods of time. People always will have soft comps or tough comps, that kind of thing from quarter-to-quarter. But if you look at it, and what I think is different about us is where we get our growth. I mean the composition across our geographic and brand portfolio, where we get it is sometimes a little different, the example being all the nice results done, and we continue to talk about, say in Europe, where others perhaps aren’t seeing as nice a growth rates in Europe. And they’re reliant more on other geographic regions of the world. But when it all adds up, I still continue to think that mid single digit in this environment, underlying operating growth while trying to make investments for future growth, particularly as the recovery comes is a nice growth profile for the company.

Dara Mohsenian

And from a top line standpoint, is it mid single digit top line expectations longer term or is more low to mid single digit?

Paul Varga

To the extent that it gets up into, I would guess that we would have to look at each plan. But if we were able to get the net sales growth, tracking consistently in the mid single digits, I'd expect that to have some leverage over a longer period of time to produce slightly higher operating income growth. If you were to – that's been our history to get a little more out of it through leverages as we get larger as a company and have a little bit more efficiency across various aspects of the P&L. But that remains to be seen. I mean we'll have to see what sort of economic recovery comes and then how the marketplace reacts to some of the innovation and changes in mix that we're putting forward.

Operator

Our next question comes the line of Kaumil Gajrawala of UBS.

Kaumil Gajrawala

First question on advertising, advertising as a percentage of sales used to run around that 13% range and it seems as we come into the weakness in the economy that's dropped to about 10%. Can you talk about what your outlook is for advertising spend through the back half of the year, and should we expect that number to grow back up to a 13% as time goes on?

Donald Berg

Yes, it's Don. Let me just back up for a second because we've talked about this quite a bit. When we look at how we go about investing behind our brands and building our brands, there's a couple of things that we have top of mind. One of the things is, and I kind of mentioned it a little bit in my remarks, we're looking at all the different aspects of the marketing mix that's available to us and oftentimes some of the things that we do don't end up in A&P. Paul had referenced, as well as I, some of the new packaging stuff that we've done that all ends up showing up as part of our cost of goods. To the extent that we're doing gift packs in the marketplace, that ends up showing up in cost of goods, depending upon where and how to the extent that we're doing targeted discounting, that ends up in the discounting line. And so as we look at our brand building, we look across all those different dimensions and how we're investing. And when you look at that, there has been better growth along our investment profile behind the brands. We've also talked quite a bit about continuing to keep a certain level of flexibility. So as the consumers change in terms of what they're responding to and reacting to, we can move kind of up and down these different marketing mix factors. And so I think a lot of the answer to your question is going to be where that consumers respond, how they respond and what they're responding to as to what you're going to see in that one specific A&P line item. The other comment that I'll just make is that we're being pretty thoughtful about where we're making our A&P investments and where we're seeing markets getting on a faster growth track and where consumers are responding better. We're putting additional funds there. And where we don't find consumers responding as much that's where we kind of pulling back until the environment changes and we find consumers to be more responsive. And so it's not an easy answer to all of that. It really is going to depend upon how the economy continues to evolve and develop over the course of the next few months and the next few years.

Paul Varga

I might just add one point. When we started to see changes, and really in the consumer environment, a softening of the economy, I think one thing, a lot of times what – this is one of the ways we view it. A lot of the investment that is captured oftentimes in the A&P line has a horizon that might span, certainly many of the investments we found ourselves making may have three- and five-year out type perspectives. And we found the need in a lower sales environment generally across the globe to skew some of the investment – not that this is a negative. It's really just to skew many of the investments to get a more immediate sales reaction to that changing consumer previous position. And so what we started to find is for example, packaging changes could elicit a much more rapid response in terms of consumer uptake we found versus some of the more slow and steady build that oftentimes say comes from media. Also, I think you're starting to see that I think ongoing there could be efficiencies as the changing world of media unfolds in front of us. For example, the social media, just the efficiency with which you can in many instances, get to your consumer for and what we hope is a more direct response related to a message you might be sending at a particular point in time. So I think a lot of things that converged over the last couple of years to make us think and rethink about the mix of investments, and as that environment changes, we'll continue to think about it. But I will say this, I mean it would be my goal over a very long period of time to make sure we have the most efficient investment posture we can for delivering the type of results we want. Don't want to just arbitrarily go out and measure the business on how much money I spend.

Kaumil Gajrawala

Is it fair to say with what you're talking about the reclassifications that more of that than we've seen over the past is falling into promotion, and therefore, netting out of the revenue line as opposed to being the advertising line?

Donald Berg

Some of it; a little of it, yes. I actually think the most important, I mean, the best examples we'll talk about is that our company are – for example, when el Jimador moved from a mixto product to 100% agave, that cost or that investment got captured in the cost of sales. And it was probably, in my view, I mean everybody could debate this, one of the predominant factors for its uptick in sales. This goes back years now, three or four years. But the change in packaging on Gentleman Jack, which would not have shown up in any sort of A&P line almost immediately changed the trajectory of that brand. So it's just almost trying to target the investments to get the results you want on the timeline you want is the way I'd say it. And so I know we're going to talk a little bit more about this, some this afternoon if you're in attendance. But it is one that I can see where you would have the question, but I hope you'll hear some of these examples and it will make it a little more clear to you.

Kaumil Gajrawala

If you could just provide any forward commentary on input costs, hedges in place, that sort of thing.

Paul Varga

What cost??

Kaumil Gajrawala

On your input cost outlook. And if you have any hedges that are in place?

Jane Morreau

I'll take that. This is Jane. In terms of our input cost for the remainder of the year, actually we will continue to see some efficiencies. We expect – we had some hedges in place on our corn prices. Yes, wheat prices have gone up a bit, which affects our brand Finlandia. But we actually expect to see some efficiencies for the rest of the year, due in part to our increased production and bottling that we're seeing going on, which is a good thing. In terms of hedges that we've got in place, the way I would think about them, assuming you're referring primarily to our foreign exchange, we like to think of it more as what would happen over the balance of a year should the rate, the whole basket of rates go up or down 10%. And so we've got a good portion of our hedges built in for the rest of the year, but we still have some volatility. And should the rates go up 10% for the rest of the year, we have about a $0.04 spot rate effect versus the outlook that we've given to you.

Operator

Our next question comes from the line of Vivien Azer of Citigroup.

Vivien Azer

I was hoping you could start off by talking a little bit about what trends you're seeing in on-premise?

Donald Berg

Specifically in the U.S.?

Vivien Azer

In the U.S. yes, please.

Donald Berg

We've certainly seen a lot of stabilization there. And have actually in more recent months started to see some growth coming out of the on-premise arena. The other market, just to talk a little bit outside the U.S. that's really important to us in the on-premise is the U.K. And we're also starting to see stabilization in growth there as well. In both of those important markets we're seeing some positive signs. We've seen some positive signs in the past that haven't stayed with us. Hopefully this one will. But it's looking a little positive right now.

Vivien Azer

And then in terms of the off-premise, you guys talked about the competitive activity that you're seeing. Is it kind of across the board? Are you seeing it both in terms of price and in terms of promo and the packaging investment like you guys are making but from your competitors? Or is there kind of a strategic in the priority that you're seeing from your competitive set? Like is everybody investing in price or one of those levers?

Donald Berg

We're kind of seeing all of that plus a lot in innovation. On the pricing front, it looks like it is starting to stabilize a bit. But just like you see in any holiday season, I mean, there are certain areas and regions and categories that you will see pricing being a lot more competitive than others. And so for us, I mean, just like last year, we talked a lot about, coming into holiday period about being very targeted in the discounting based upon the competitive environment that we're in. I think, if I remember right, we came out of that where Nielsen showed we had some the best price mix in the industry at that point in time. We're looking to kind of bring the same of approach to bear this year as well. But having said that, it does look like it's a little bit better pricing environment than what we had been seeing. A lot of what we're seeing is on the innovation front that we've been talking about there's a lot of new brands and new line extensions that are being introduced that are taking a lot of time and attention. And are in some cases, getting some high levels of consumer interest out there.

Paul Varga

I think a lot of companies, and you could put us in that camp, realized that one of the lower growth environment versus a few years ago, one of the most efficient things you can do is to do a really good line extension because it produces income and could say something very positive about the trademark. So if you can get that one-two punch working but a lot of folks know that, so the competition for space, whether it's on the shelf or on the floors around the globe, very notably in the United States, you're just seeing higher levels of competitiveness. But I don't expect – I think because of some of the shifts we've seen in consumer behavior, I think companies are correctly responding to try to meet some of those needs. So I think that may be along with – when you get into sort of the holiday season, you're always seeing varying levels of price competitiveness. But I would agree with Don. I think there's more sanity in what we're seeing in the more recent numbers than what we might have seen in prior years.

Operator

Our next question comes from the line of Lauren Torres, HSBC.

Lauren Torres

Question on the route-to-market changes. I guess you're cycling or kind of passing through some of the more or the higher expenses tied to those changes. Just any update with respect to where you are with respect to those changes? And then, I guess looking forward the benefits flowing through and how we should think about the upside from those investments looking into your numbers for next calendar year?

Paul Varga

I'll take it on one part and maybe Jane, who may know more of the details around some of the expensing and the seasonality of it. Actually one thing that makes us feel good about this first half is you always hold your breath when you're making changes in these marketplaces as to how smooth they might go. I actually think on balance, I mean, so many of these across such a short amount of time and that's concentrated really here in the first half, we're pleased with the way our people and any new partners were able to make some of these transitions. That allows you to gasp a little bit, I mean to let your breath out and say okay now we can get focused on the building of the business. So that is actually a source of confidence for us in at least on those markets where you can now get down to nitty-gritty of building the business in the marketplace. And having those, I would – the reason we would make those changes is to try to help the business. So quantifying that for you so that it would be helpful in your expectation to sales, I don't have any data to share with you on that. But I do think we're really pleased with not only the decisions in the first place, but also the way that they've been implemented. And a lot of the cost, I think I'm going to turn this to Jane, a lot of the costs we had scheduled for the first half, there will be some, I'm sure, ongoing costs baked in over the second half in the primary part of the transition costs already accounted for.

Jane Morreau

Paul, you're exactly right. The start-up expenses what we refer to is getting people hired, on-boarded, getting systems in place, all that stuff is pretty well behind us. But what you will see is we put in infrastructure. We hired a sales force down in Brazil to do exactly what Paul was saying is to focus on our portfolio and grow the portfolio for the future. So again, if you're going to be starting to focus on one line item in the P&L, such as SG&A expense, that will be up for the balance of the year of course because we didn't have that sales force a year ago.

Paul Varga

And back to earlier questions, we consider that as an as important investment behind improving the sales growth rate of our company as advertising or packaging or some of these other things. So in fact, I think it was Dara, who asked about sales growth rate and those markets over time, I expect to see the sales growth rate go up across our portfolio in the markets where we make those investments.

Lauren Torres

And I guess adding on to that with respect to the benefit of an increased sales force just other benefits as we think about next year, from an efficiency standpoint?

Paul Varga

In what way?

Lauren Torres

I mean, obviously, improving the efficiencies of these systems in your international markets should maybe flow through on a better expense line of cost savings things like that? Is there any way to quantify the benefit of this to earnings for next year?

Paul Varga

We just don't have the one-time costs, but the actual ongoing costs will stay with you, they're just in your new base. But of course the one-time costs that you have this year for the set up will go away. That's the only thing that I can think of.

Jane Morreau

Exactly. But again, as we had to get folks in place, and we're doing it for the future. We're doing it to build our portfolio. So we hopefully as time goes on, our desire and what we've seen in the past is you start leveraging. You will get leveraged over time as our growth in these markets grow. We don't necessarily have to add the people at the rate we just did for instance.

Paul Varga

And a lot of times, you all would think, okay, I'll think about the Jack Daniel's sales growth rate. We actually think it's not only that. It's also other brands in the portfolio because when you have more dedication to your Brown-Forman portfolio people, they have the time and commitment and the facility to focus on brands beyond just Jack Daniel's in markets where you do that. So when I say we would cross our fingers for improved sales growth rates in those markets, that's not just on Jack Daniel's it's on a multitude of brands.

Lauren Torres

And if I could also, just a clarification on your comment about the FX impact to this year's earnings. I think last quarter you mentioned the potential negative $0.05 impact and Jane you just mentioned plus or minus $0.04, is that how we should think about what the impact would be on that earnings range you updated us on?

Jane Morreau

Lauren, let me see if I can clarify this. We still are projecting a slight unfavorable impact to our earnings for the year. What I was referring to is within the range that we gave you or within our guidance, we of course have thought about it as what the spot rate is or recent rates are over the last couple of weeks. And should those rates go up or down by 10%, it could impact our earnings by plus or minus about $0.04.

Operator

Our next question comes from the line of Judy Hong of Goldman Sachs.

Judy Hong

Just going back to Jack's soft performance in the U.S., you obviously talked about hoping to accelerate the brand's growth going forward. But can you just help us understand what actually you think has been the drivers of that under performance? Is it more competitive pricing? Is it just your some of the brand investment's initiatives haven't really driven the share improvement that you expected that you wanted to see? I'm just trying to understand what's been the driver and how that sort of changes going forward.

Paul Varga

I think there's always a multitude of factors you can point to. But the things I think we've observed in really more the last six to 12 months I'll say that wouldn't been have existed I'll say, whether it was pricing environments or the economy and all the things that would have existed before has been an uptick and what I'll call competitive activity in some instances related to introduction to new line extensions. A lot of our key whiskey competitors have in the last several months introduced across the board and across almost virtually a lot of leading trademarks have been introducing into the marketplace line extensions. That would have to be one contributing factor. So when the consumer sees that, they have a natural curiosity or interest, and they may go try it and that trial occasion may be an occasion that Jack Daniel's didn't get. And of course we don't like that; we want those occasions. And so I think that maybe a little bit of what we've started to see. I mentioned that one aspect of the overall U.S. business in the last quarter was that we've seen that just overall whiskey sales have been kind of soft too. And we had a lot of sort of theories and postulations about that. But the reality is we started to see a little improvement in that in our second quarter, more or less the third quarter for the calendar year. So I thought that was encouraging. We saw a little bit of uptick in Jack Daniel's. But again, not up to our expectation or to the greater growth that we're seeing in the category or the overall distilled spirits industry. So as a result of that, we're very much focused on the marketing mix, where we spend our money, what we are doing with the Jack Daniel's brand in the marketplace, how are some of our line extension activity. Last time when we report on Jack Daniel's, we're talking only about Black Label and we are not adding in positive impacts sometimes of Gentleman Jack or Jack Daniel's Single Barrel, more premium line extensions and how they've been progressing in the United States. So if you added those to the big picture, it would paint a slightly different picture than what we see with Black Label. So if we look at it both ways, so we have a really good understanding of it. But I think the combination, you hinted at pricing. I think I can't really say that a lot of competitors are out there are really dropping their prices and that's really hurting Jack Daniel's in any way that's different than the types of ebb and flow and pricing that go on all the time. I actually think it probably relates more to just the uptick in competitive activity around innovation and line extension.

Judy Hong

So if you look at these innovations that's been introduced in the last 12 months or so from your competitors or even the ones that you've introduced, you have any evidence that those are actually helping kind of the core trademark brand equity? And so as people try these line extensions it's sort of helping the overall trademark and that maybe you may have been lacking a little bit just in terms of the number of innovations in that area? Is that what you're seeing? Or as you kind of look forward, do you think that the pace of some of these line extensions will also slow down because the companies will kind of go back to focusing on some of the core trademark?

Paul Varga

I can't predict the future. But I would say a good trademark, a very strong trademark that has a nice line extension in this environment. In my experience on this, if that's well implemented and well positioned and well throughout, that it is nothing but attitude. And that's been our experience with Jack Daniel's. I can't really comment for some of our competitors. They may be seeing something different. But I think it's fair that we've seen this with – Don remarked with this on Southern Comfort. Southern Comfort is responding to efforts in innovation and line extensions that are in the marketplace. And some of those innovations were a few months or in a couple of instances a year or so ahead of us. So catching up to it is part of it. But the early results we're seeing, I mean, it's very, very early on something like the Southern Comfort Lime introduction have been positive. And we feel good about the way it's being received in the marketplace. And I personally think that as long as it's received well by the consumer, it makes them feel good about the Southern Comfort brand, you tend to research these things a little bit upfront. But you really don't know until you get out into the marketplace. I think they're very positive additions, has been my experience and we just got to make sure we're doing the right things with the portfolio. And not just throwing stuff out in the marketplace. But I think that is one of the critical elements of the mix looking ahead. How do we do that well along with everything from tapping into social media, making sure we got our price volume mixes right, sending the right messages to the consumer at the right time and such, a whole handful of things.

Judy Hong

And then you talk about being encouraged by the international growth profit performance. Obviously, the sales growth there is pretty strong. But other than kind of the net sales growth, are there any drivers of gross profit improvement there whether you just have more scale so you can leverage your cost structure better? Is it price mix? Just in terms of the color as it relates to gross profit improvement internationally.

Paul Varga

I don't think it's really any different than the overall company, the international story that we cited. We're getting some production efficiencies as we said. I'll expand, I think people sometimes forget our company grew up in the United States. A lot of the people that follow us are in the United States. So there's naturally a high interest in the United States. But I think sometimes that comes at the cost of people understanding the very long-term success story of Jack Daniel's around the world and actually the thing that gives us so much encouragement is how low in many instances our share remains around the world. So we think we continue to have a widespread runway for growing the Jack Daniel's brand and trademark overall along with as we make some of these route-to-market changes and other ideas that come into play every so often, even greater opportunity for the rest of our portfolio. So I don't think there's any different story than the corporate story in the international markets other than the appeal of the brand and the overall stage of development that may exist in international markets relative to the U.S.

Operator

Our next question comes from the line of Tim Ramey of D.A. Davidson.

Timothy Ramey

Perhaps a lot of what you just said about Jack Daniel's would apply to the question I was going to ask, which is what about Finlandia? That brand enjoyed tremendous growth for a number of years and maybe accomplished a lot of those line extensions. And as I recall it was somewhat driven by the kind of the co-distribution with Jack in Eastern European markets. What are your plans and strategies there to kind of reintegrate that great brand?

Jane Morreau

Tim, as we think about Finlandia actually it did return to growth this quarter. We had some really tough comps, a point of reference versus a year ago and Eastern Europe, where the whole economy was pretty tough. But we see the opportunity for Finlandia around the world and particularly in Eastern European markets, we've seen a number of opportunities to grow and we're seeing nice double-digit growth there. We'll continue to expand there. Russia with our route-to-market that we just established with Coca-Cola Hellenic, we see tons of opportunity in that market. It's a big vodka as you know. And see the opportunity to really leverage that brand and to grow it even further. Similar to some of the things that we've talked about, we've got looking at the whole mix of how we spend behind Finlandia, being its package, being its flavor profiles, being sizes, bottles, line extensions, things like that, we're continuously looking at things along those areas. And we believe there's opportunities to leverage the Finlandia brand up and down the scale there as well.

Paul Varga

Tim, I think just to be clear, that really is one of the most interesting learnings for us over the last few years. The sale of Finlandia and Jack Daniel's side-by-side, I think you referenced, maybe like for example, the Polish development. Actually we felt Finlandia led that, I mean that was the basis, Finlandia being so strong in the Polish market, with Jack being able to come in alongside Finlandia. And while we were doing that, a lot of the innovation that was occurring out in Poland and other parts of Eastern Europe really related to the mainland but also development of flavors for that marketplace. And we think there's still a lot of innovation available to Finlandia still in flavors. Jane mentioned packaging. We've regularly looked at the ongoing upgrading of the Finlandia package. We think it's a really efficient way in that category to send really positive messages. Some of its performance in this first half is because it skews to Eastern Europe is tied up a little bit in that Russia transition. So I think that points for better results for Finlandia down the road for us as we get up and running with that transition. And then we're also going to be paying close attention to the recovery in Eastern Europe and the pace of that because that will have a stronger influence on the Finlandia performance than virtually any other brands depending upon how Eastern Europe goes. So those are some of the things that we're looking at and things that I actually think again later today, we're going to be talking about some of our 10-year expectations and ambitions. And we have really high ambitions for Finlandia and vodka in general over the next decade.

Operator

Our next question comes from the line of Kevin Dreyer of Gabelli & Company.

Kevin Dreyer

Just a quick question on your super-premium brands. Obviously, had a little bit of a tough time in the midst of the recession. Seem to be coming back nicely from a depletion standpoint although depletions are outstripping sales by a pretty wide margin. Can you give any color, kind of brand-by-brand as well as are you needing to promote – particularly I've noticed there have been a lot of promotion seem to be going on in the super-premium bourbon category?

Donald Berg

When you look over the course of the last 18 months to two years, by and large, our super-premium portfolio has continued to do well throughout that timeframe. We've got – actually right at about the time that – one of the brands that we include in that is Sonoma-Cutrer and right around the time that the recession hit, we had taken a line extension to Sonoma-Cutrer to the off-premise that really served us quite well. And it has been growing very nicely throughout this timeframe. Woodford has continued to grow for the most part in double digits throughout this whole time. Sometimes we throw in Gentleman Jack and Single Barrel as we talked about super premiums. Other times, we'll put that in the family of brands. Both of those brands have continued to grow throughout this period. At times, there were at higher growth rate than others. But they continue to grow pretty much throughout. The one brand that has struggled a bit during this time has been Tuaca. And when you look at where it competes in, in terms of liquors and the shot, drinking occasion, what have you, that's been one of the more competitive arenas. It's kind of held its own, but it hasn't seen some of the higher growth rates that we've seen in the rest of our super-premium portfolio. Herradura has been a little bit up-and-down. But it has been performing nicely over the near term as we've gotten the new package out and some of the other brand building things that we've implemented on Herradura since acquiring it a couple of years ago. When you look at what's happening more recently, I mentioned a little bit earlier that we're starting to see a little bit more strength in the on-premise and when you kind of go through the NABCA data and you see what's happening in the on-premise. Interestingly, a lot of these up premium brands are showing nice growth rates there. And typically, that's where they do the best. And so hopefully as we look forward in the future, we'll be able to even accelerate on these growth rates, if we can continue to see some of these trends in the on-premise continue to improve.

Paul Varga

Kevin, if you were referring to the depletion results in Schedule B versus the net sales as your data point for higher growth rates and depletions versus sales, I think that – I wouldn't want you to misinterpret that, that had anything to do with price reductions. And that probably dealt more with the mix of those super premium brands in terms of the growth rate. And I would just add to Don's point that it's really sort of a recurring theme here which is this last three quarter –this much more anecdotal in addition to qualitative, in addition to the first half results and the second quarter results that Herradura and the response to Herradura's new packaging, I mean, has really been exceptional. And we really actually feel like we're still at very early stages of making the full transition from either the old package or interim package to getting it out there on the shelf and on the bars in a way where it we can be one of the chief spokespersons for the brand, that package. So on some levels I feel like that one may actually, over the long third of time, really be one of those shining examples of how packaging plays a huge role in the ability to accelerate the sales growth rate. Similarly, we continue to be very impressed with the performance of Woodford Reserve. It's just a steady, very strong super premium performer and as it gains distribution, it continues to picks up consumer appeal so both of those would be examples that have held up very, very well here. Woodford, more over many, many quarters here; Herradura, more recently.

Operator

The next question comes from the line of Thomas Russo of Gardner Russo & Gardner.

Thomas Russo

Turkey, Middle East, I think you said, I think Don said volumes of 400,000, up 30%. So can you give us a little bit of background as to why, how sustainable and what the outlook might look for in like in that region? That's my first question and holiday cheer. It's a good one.

Paul Varga

The reason we continue to bring those points up, is because so many industries and companies have a similar story about a really explosive growth in a limited amount of geography and the composition of our business and the reason we talk about the Middle East or Africa or all these various locale around the world, where we're having success particularly with Jack Daniel's and to some extent with Finlandia is that we really have what we believe is a very broad, widespread growth story and remaining growth opportunity. So as it relates to the specific details in that region I'll turn it over to Don.

Donald Berg

It's a great example of how you can have a number of these countries that are not necessarily on your radar screen that you can get up to 50 to 100,000 cases and grow nicely and you add up a few markets that are 50 to 100,000 cases and all of a sudden you've got a nice little business there. And when you look at that area of the world, and there's some different answers to the question depending upon the specific country that you're talking. But Bulgaria and Romania both have been doing quite well and prior to the downturn, they had some very nice growth rates and then they stalled a bit as you saw the typical trading down that went on during that period and people just having to kind of re-adjust their consumer behaviors as a result of the economic downturn. What we're starting to see is a return to some of the growth rates that we saw there before and we've got great partners and we're doing some great brand building efforts that are just paying off and they tend to be markets that are intrigued by whiskey. They're traditionally vodka markets. They are looking for other alternatives, and whiskey is an area that they have tended to turn to. Turkey is a little bit of a different story. Turkey has been a bit up and down over the years. We basically put in our own infrastructure in our route to consumer move over a year ago. And I think we're starting to see some of those efforts begin to pay off in terms of having our own people on the ground and doing some really good programming. There's been historically some regulatory issues that are kind of now behind us and so the markets opened back up again. So it's a bit of a mixed bag, Tom. But when you look at that region overall, it's an area that has grown nicely historically. It seems to be picking that growth back up again, and could have a very bright future for it.

Paul Varga

Tom, I wish I understood it better but every time I talk to somebody about Jack Daniel's presence in Turkey, there's it's a real connection at some level between the Jack Daniel's brand and the Turkish consumer in a way. I don't know if it's an Americana and the Western appeal, all of that, and there's always been fluctuations in the trading patterns there. But at the consumer level, we think Jack Daniel's connects extremely well to the Turkish consumer.

Thomas Russo

Second question, can you just touch on the health of the pre-mix market overall? We see some Jack Daniel's growth. There's also this terrific opportunity in Mexico with pre-mix. Just a quick view across the globe on how strong that is and where do you look it to go to?

Paul Varga

I think we were between 15% and 20% growth the first half in the – that was at the Jack Daniel's RTDs or was that overall? I think it was the Jack Daniel's one. Yes, the Jack Daniel's. Tom, I mean, I actually feel like we see that – as well as an RTD business, we really see it as an extension of the Jack Daniel's brand into a variety of occasions. And the consistency with which it's being received in markets, particularly where that type of business actually exists has really encouraged us. And it's really surprising that this Mexico responds so quickly, particularly on the heels of that nice New Mix business we've got done in Mexico has been really encouraging. But beyond that, it's places like Italy and Germany and the U.K. and many other markets. And I can't tell you how impressed I am with the long-term progress and the way we've adjusted down in the Australian market, which is our largest one. And sort of set the tone for the way that Brown-Forman and Jack Daniel's can do the ready-to-drink market effectively for our company. I mean we don't have to go in and dominate it or anything like that. It's just really enter into consumer occasions of convenience, mix ability and in a way, I say this often and I know people don't necessarily always buy this. But I actually think it creates a wonderful marketing message as well in the marketplace through branded drinking occasions, that say that Jack Daniels and American whiskey are very mixable. So those are the areas that we continue to see a lot of potential for growth there. Don or Jane, you want to talk about some of the New Mix possibilities or trends?

Donald Berg

We've also seen, and it's early days yet, we've got some new introductions, relatively new introductions, Southern Comfort pre-mix in the U.K. that's doing fairly well. We're just in the process of bringing New Mix into the United States. And while it's very early there, there does seem to be quite a bit of interest in New Mix here in the U.S. In Mexico, where we've got quite a large share of that market, there's been some trade channel issues there. And so that's why you've seen some of the slowdown of New Mix in Mexico. But basically, when you look at the consumer takeaway, what we're seeing is still some very, very healthy trends there.

Thomas Russo

Paul, you mentioned I think in the Southern Comfort discussion that there was also – you referred to the growth in flavored whiskeys. I wonder if you could just spend a quick second on that and what you're seeing in that category.

Paul Varga

A handful of the traditional whiskey trademarks that you know well have put into the marketplace over the last years, mostly in two areas, honey flavored and some cherry flavored. So things that almost I think people would have thought of as unheard of years ago, the traditional approach to whiskey, but very much to capture new occasions, some of it oriented around both on-premise and home straight consumption occasions. For example, when you're a brand like Southern Comfort and Jack Daniel's would have a share of your business, where that's where you generate it. I think you're prone to some competitive inroads there. And whether it's trial or sustained, is still unknown to us. But I just think it's important for not only us to know it but us to be able to adjust our mix and our approach to the marketing and selling of the brand in a way that can not only appropriately defend the consumer franchise and occasions we got but also maybe push ahead and actually gain share in that area. So that's really what it is. And I think the best example I can cite right now is the Southern Comfort response. Some of these brands have been out there now, Tom, 18 months, a couple of years. And so they've got a little bit of a head start. But we've seen quite a few recent introductions. And as long as we think – we'll still be very thoughtful about it but do it right, that we think there's real opportunity for our trademarks to play in that arena as well.

Operator

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

Dara Mohsenian

I might have missed this, but can you give us an updated impact of FX on your full year EPS?

Jane Morreau

I said a moment ago, we actually are expecting this year's forecast that are in the range that we gave you to have a slight unfavorable impact versus last year. So it's a slight unfavorability still.

Operator

The final question comes from the line of Edward Mundy of Nomura.

Edward Mundy

Just on pricing in the U.S. again, looking at the recent Nielsen and Napka data it would appear that the number one player in the U.S. is adopting a slightly firmer attitude towards pricing. Are you seeing this in the market, yet? And if so, do you think that this trend might impact industry pricing as a whole going forward?

Paul Varga

We cannot look at any one corporate competitor as much as much as we would individual brand-by-brand. But I think I would reiterate what Don had earlier referenced that if you look at 12-month volume versus value and then look at three-month volume and value, I think you're beginning to see a better, in our view, spread between them, a more favorable spread where it looks like value is ahead of the volume whereas on the 12-month basis, there would either been narrower or even a little bit behind. So it would validate, if the leader you referred to was an example for the whole marketplace, we would agree that it looks like there's some improvement in the combination of pricing and mix.

Operator

I'm going to turn the call back over to the presenters.

Ben Marmor

Thank you, Kila. We look forward to seeing many of you at our conference later today. And for those who are not in attendance, the meeting will be webcast; just follow the link through our corporate website. Thank you, everyone for joining us this morning. Take care.

Paul Varga

Thanks so much.

Operator

Thank you. This concludes today's conference. You may now disconnect.