Brown-Forman Corporation, Q2 2015, Earnings Call 2014-12-03

Presentation

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Brown-Forman Second Quarter Fiscal Year 2015 Earnings Conference Call. — ***Operator Instructions*** — I'll now turn the call over to Jay Koval, Director of Investor Relations. Please go ahead, sir.

Jason Koval

Thank you, Laurie, and good morning, everyone. I want to thank you for joining us today for Brown-Forman's Second Quarter 2015 Earnings Call. Joining me today are Paul Varga, our President and Chief Executive Officer; Jane Morreau, Executive Vice President and Chief Financial Officer; and Brian Fitzgerald, Chief Accounting 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 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 of fiscal 2015, and the release can be found on our website under the section titled Investor Relations. In the press release, we have listed a number of the 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 will be discussing 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 results of operations are contained in the press release.

And with that, I will turn the call over to Jane for her prepared remarks. Jane?

Jane Morreau

Thanks, Jay, and thanks for joining us for our second quarter earnings call. I'm planning on covering 2 topics today, which should leave plenty of time to address Q&A after our prepared remarks: first, I will review our first half results, including recent trends in the second quarter; and second, I'll discuss our updated outlook for fiscal 2015.

So let's get started by reviewing our recent results. As expected, second quarter underlying net sales of 7% represented a solid acceleration from our first quarter's 3% growth and resulted in first half underlying net sales growth of approximately 5.5%. You'll recall that the first quarter was negatively impacted by trade inventory adjustments in the United States, United Kingdom and Germany.

So let's look at the United States, where underlying net sales rebounded from flat sales growth in the first quarter to an increase of 10% in the second quarter, as U.S. retail trade inventory levels began to normalize. This resulted in our first half underlying net sales growth of 5% in the U.S. On prior calls, we have discussed our efforts to drive a more balanced mix of price and volume growth in the United States in fiscal 2015, and U.S. syndicated data from Nielsen and NABCA suggest we're accomplishing this goal. Jack Daniel's Tennessee Whiskey blended 3-month value trends are up over 6%, a 3.5 point acceleration from the 12-month trends we were experiencing at the start of the fiscal year.

Lower gas prices appear to be helping to drive better on-premise trends and a modest acceleration in TDS.

Moving now to our developed markets outside of the U.S. Underlying net sales increased 8% in the second quarter, a significant improvement from the first quarter's 1% decline and driving our year-to-date underlying net sales growth of 4%. A strong sequential acceleration in underlying net sales growth in the United Kingdom led to a high single-digit increase in the first half. Underlying net sales in Germany grew slightly in the second quarter, but our year-to-date results in that market are still down mid-single digits due to continued variability in trade buying patterns.

France and our — ***indiscernible*** — Swiss markets grew double digits. Canada continued to grow nicely, while results in Japan were flat and Australia declined slightly.

Underlying sales in emerging markets grew 8% year-to-date. Results were particularly strong in Turkey, Brazil, Ukraine, sub-Sahara Africa and Indonesia. It's worth noting that our recent initiatives in South Africa are driving strong gains in a very competitive marketplace. Russia's growth stalled in October due in part to a depreciating currency and waning consumer confidence, which have negatively impacted consumer demand in that market. Mexico's underlying net sales grew slightly in the first half following the first quarter's growth on easy comparisons. Poland's underlying net sales declined double digits as the market continued to struggle as – at the large excise tax increase taken at the start of calendar 2014. Excluding Poland and Mexico, our emerging markets grew underlying net sales 22% in the first half.

We estimate that after accounting for retail inventory adjustments in the U.S. and Germany, our overall first half underlying net sales grew over 6%, in line with the low end of our outlook we shared with you for fiscal 2015.

On a brand basis, our results accelerated sequentially due largely to the Jack Daniel's family of brands, which grew underlying net sales by 9% in the second quarter, up from the 5% in the first quarter. Woodford Reserve and Old Forester also enjoyed strong double-digit gains as favorable dynamics continued to support the growth of our authentic American whiskey brands. Finlandia Vodka's underlying net sales declined 6% year-to-date due to continued softness in Poland. Southern Comfort's underlying net sales declined 4%. And el Jimador and Herradura's underlying net sales both grew nicely in the first half, up 4% and 19%, respectively.

Moving now to the reconciliation of underlying to reported growth for our first 6 months. The big story is the rapid appreciation of the U.S. dollar, which is driving a large difference between our reported and underlying results throughout the P&L even after considering our hedges. The movement of our key currencies has been significant over the last few months with most of them depreciating versus the U.S. dollar. The euro, for example, is down roughly 7% since our call for the first quarter in late August.

Let's start by looking at sales, where our top line grew 5.5% on an underlying basis fueled by equal contributions of volume growth and price/mix. Foreign exchange negatively impacted our reported net sales by 3 percentage points in the second quarter and 1 percentage point year-to-date.

Underlying gross profit grew faster than net sales, up 7% as improving price/mix helped drive a 40 basis point improvement in gross margin.

Underlying A&P spend increased 5%, while underlying SG&A grew 10%. The increase in SG&A was driven primarily by our France route-to-market investments, some onetime items and the investments in our people, processes and systems to drive our company's continued globalization. We expected elevated SG&A growth to not subside – we expect elevated SG&A growth to not subside until we move into the fourth quarter and lap such items as the January 1 route-to-market investments we have been making in France.

So putting this all together, we delivered 6% underlying income growth in the first half of fiscal 2015. Foreign exchange headwinds hurt our reported operating income growth more than reported sales through the combined and roughly equal effects of a transactional impact on net exposure and revaluation of net current assets denominated in foreign currencies. As our non-U.S. business has expanded, so have our overseas net assets, particularly cash, and most notably in Europe. These revaluations are captured in the $17 million negative swing in the other income and expense line on the P&L.

For the first half of fiscal year, foreign exchange negatively affected operating income by $33 million, equivalent to a 7 percentage point hit to our operating income growth and a $0.10 drag on reported EPS, which came in at $1.67.

So now moving on to my second and final topic for this morning, an update on our outlook for fiscal 2015. We have a significant presence in the American whiskey category, which is enjoying favorable trends. Global demand for the category continues to grow, and we believe that we have the best American whiskey portfolio in the world measured by breadth, global appeal and leadership of the category's development.

We continue to invest in our brands, our people and our markets with an eye towards delivering market-leading returns for our shareholders. And with consumer takeaway trends in the U.S. acting as a tailwind, coupled with our disciplined approach to innovation, we believe we are well positioned to drive long-term growth through further development of our whiskey brands.

Today, we are reconfirming the ranges we shared with you for our full year outlook for underlying net sales growth of 6% to 8%. This rate of growth would represent significant outperformance of our competitive set, given their flat to modest declines over the last

12 months. The 6% to 8% range also assumes continued momentum in our U.S. business, stable economic conditions in Europe and no further disruption from markets such as Russia.

We also announced today the nationwide rollout of Jack Daniel's Tennessee Fire later this fiscal year after several months of strong and very positive response from consumers and the trade. We believe that this brand extension will help us seize one of the largest and fastest-growing opportunities in flavored whiskeys with a premium cinnamon-flavored whiskey under the Jack Daniel's trademark. But given the time needed to gain distribution and build momentum with consumers, we expect minimal impact on our underlying net sales and underlying operating income growth rates this fiscal year. And most of the positive impact from pipeline fill in the fourth quarter will be offset by investments to support the successful launch of the brand.

We also anticipate delivering 9% to 11% growth in underlying operating income. So while we will remain thoughtful in how we invest in A&P and SG&A, the pace and timing of our P&L investments will determine where within the range we land as we continue to find good opportunities to drive long-term growth through investments in our brands and our people.

Moving now to foreign exchange. Assuming current spot rates as well as our existing hedges, the foreign exchange headwinds that hurt our first half reported results are expected to continue to negatively impact our reported results in the back half of fiscal 2015. We anticipate foreign exchange will adversely impact our full year operating income by approximately $45 million to $50 million, removing 4 to 5 points from reported growth in fiscal 2015 and about $0.15 from EPS. This EPS headwind is $0.09 worse than our first quarter outlook of a $0.06 negative impact from foreign exchange. This is the principal driver for our revised EPS outlook for the year of $3.15 to $3.35.

As a sensitivity, assuming our foreign currency cash exposure collectively moves 10% in either direction, our EPS over the balance of the year would be impacted by approximately $0.07.

So to summarize, our underlying business fundamentals remain robust, and we are confident about our future growth prospects despite the challenging trading environment for the industry. We are investing heavily to meet future demand as seen through the large-scale distillery, warehouse and home place investments at Jack Daniel's Woodford Reserve and Old Forester. Meanwhile, we continue our track record of returning capital to shareholders through dividend growth as well as our share buybacks.

So before I turn the call over to Paul for his comments, we wanted to say how much we're looking forward to spending more time with you next Wednesday, December 10, in New York, where we plan to share our perspective on Brown-Forman's future growth prospects and positioning in the marketplace and our continued excitement for our American whiskey portfolio. Paul?

Paul Varga

Thanks, Jane. Good morning, everybody. I'll be brief here, but I just wanted to add a couple of additional comments.

Overall, I was pleased with the quarter, as we did see the acceleration in underlying net sales that we had anticipated when we spoke with you back in the summer. It was nice – particularly nice to see the U.S. Jack Daniel's Black Label acceleration. It has been some time since we've seen quarterly takeaway growth in the U.S. at this level. So this has been particularly encouraging for all of us.

You would have seen that the adverse impact of foreign exchange is an unwelcome reality for the company just now, but I am heartened by the fact that the first half underlying results generally met our expectations. And as Jane mentioned, they continue to compare quite favorably to what we observe from our global competitive set.

Now as we've commented many times in the past, our wonderful Jack Daniel's brand is the primary driver of this differential performance, and I'm going to cite just 3 of the ways in which we believe Jack does this.

First, as the undisputed leader of American whiskey, premium priced or otherwise, Jack Daniel's, along with some of our other well-performing premium bourbon brands, like Woodford Reserve and Old Forester, disproportionally skew the company to one of the hottest categories in our industry right now. And we continue to believe that American whiskey is still at a relatively early stage of global development.

Secondly, Jack Daniel's widespread global consumer appeal is the source of the company's exceptional geographic balance and diversification today. The benefits of this geographic breadth are not only that it provides Brown-Forman with a larger consumer marketplace and much longer runway for growth than a more limited geographic scope might, but it also enables us to weather those periodic regional or country setbacks that inevitably come along over time. Poland and Russia are 2 such examples in the results we've reported today. This vast geographic footprint also carries with it foreign exchange volatility that is also evident today. But we consider this a very acceptable risk for the benefits of geographic diversification.

And then third, the strength of the parent Jack Daniel's Black Label brand provides the foundation for thoughtful, meaningful line extensions such as Jack Daniel's Tennessee Honey, which has been a noteworthy contributor to the company's growth over the last few years. And with today's announcement that we'll be expanding Jack Daniel's Tennessee Fire nationally in the U.S., we are hopeful that it will follow the successful lead provided by Gentleman Jack, Tennessee Honey and the Jack Daniel's RTDs over the last

20 years or so.

So favorable category concentration, geographic breadth and diversification and impactful innovation, all driven by Jack Daniel's, are 3 of the primary factors that we believe account today for our company's favorable and differential performance. Accordingly, we will continue to invest in these areas and, of course, behind the Jack Daniel's trademark.

This concludes our prepared remarks for this morning, and we're now happy to take any questions that you have.

Question and Answer

Operator

— ***Operator Instructions*** — Your first question comes from the line of Vivien Azer of Cowen and Company.

Vivien Azer

So my first question has to do with the strong acceleration that you saw in the United States, in particular for Jack Daniel's. From time to time, we've discussed potential for a competitive disruption to the brown spirit renaissance from your vodka competitors. So can you talk a little bit about what you're seeing from the competitive stance, in particular from the white spirit players in the market?

Paul Varga

Sure. I mean, as I just commented, we were pleased to see this acceleration not only in the results that Jane discussed but also at some of the syndicated data that supports improved consumer takeaway. I mean, as I think about it, there are a couple of things that we might point to. Of course, the category continues to do very, very well, but the category has been doing well for some time. And the jump that we've seen in the Jack Daniel's Black Label trends recently, we think, may be attributable to a couple of factors.

One is this year, relative to past, we think we just have improved relative pricing. We had been quite aggressive in the U.S. and consistent over the last couple of years of taking prices. And I think in some places around the country, we got ahead of some of our competitive set and particularly at a time when the consumer might not have had as much disposable income. So you put together the fact that we have improved relative pricing, even though we haven't been like dramatically lowering prices, it's just that others have caught up to us as we've been less aggressive with pricing this year. And you put that together with maybe this benefit that the consumer is seeing from lower fuel prices, which might be giving them better discretionary income, and I think we might be at a sweet spot where it's easier for our consumer, who drinks this on occasion, to trade up more frequently, is maybe the bottom line. And then I would add to it, entering FY '15, we consciously mobilized our U.S. sales and marketing teams in the United States with a renewed focus on the Jack Daniel's Black Label brand. I mean, we – in some ways, we're – I would call it asserting our category leadership. I mean, just making sure we weren't taking for granted the fact that Brown-Forman was the leader of the American whiskey business in the United States at a time when it was booming and that, therefore, it made it, of course, more competitive. And I just think in some ways, through either investment, focus, just the heavy reminder of the importance of Jack Daniel's Black Label to Brown-Forman in its home country at a time that's very important for the category has really helped to focus attention promotionally and, from an investment standpoint, to also add to it. So I think the combination of that improved relative pricing, maybe improved posture from the consumer and then our promotional efforts around it may be the primary factors contributing to the uptick.

Vivien Azer

That's very helpful. Can you just remind us what your hedging strategy is, whether today's transactions, translation, a little bit of both? And then to follow up on that, the implications for lapping some of the expense hits that you're seeing right now as you go into '16.

Jane Morreau

Sure. So just to give you a little background on our hedging philosophy, I think that's what you're asking for, is first of all, we aren't in the market for speculating about FX. We have never done that. And we don't hedge in excess of our underlying net exposures either, and we don't fully hedge our transaction exposures. So in other words, we're not in to take a – get a 100% mitigated exposure all taken care of or we wouldn't go the other way and have none. So what instead we do, we do something that we call more like you're used to, dollar cost averaging, so that we're – over any period of time, a 12-month period of time, you would see about 50% of our transactional exposure, if you will, hedged. And so I thought – while I'm here, I thought I might just spend a little bit more talking about FX because I'm sure there's going to be more color to this. And think about what happened in our first half of the year, the $0.10. And I thought I'm going to spend a minute and break it down a bit more, because what I was just referring to largely centered around our transactional exposure. And our transactional exposure I'm referring to is really our business, our ongoing business or our sales of our product less the expenses to sell those products, so our people, our advertising and spending that we would do in foreign currency as well as any cost that might be incurred in a local market. And so when I look at that $0.10 that we had hurt our results in the first half, about half of it was due to that and that – and was – if you looked at the currency shifts, as I said early on, how much they moved in just a couple of months' period of time, it was pretty dramatic. The other half of it – but it worked as we planned in terms of how we hedge and what we would have been expecting in terms of our net exposure. The other half of it is what I was referring to that shows up on the other income and expense line item, and it is referred to as our net assets, largely cash in this case. And I think I referred to in the first quarter, we had – so out of that other $0.05 hit we had a like $0.02 hit in the first quarter that was onetime in nature that related to an intercompany transaction. The remaining

$0.03 was really driven by the revaluation of cash balances that we have, growing cash balances that would become bigger overseas. So when I look ahead and think about what to expect for the rest of the year, this piece that I'm talking about, the $0.05 piece I'm talking about, I would say that, that is done and behind us. It's the transactional piece that you still have exposure on, meaning at today's spot rates and you compare to what we're looking to do for the rest of the year compared to those spot rates, you've got downside. And that's where the $0.05 was coming from. So when you think about the FX and how much is ongoing versus how much is onetime in nature, I would split them in 2 pieces and then think of the rest of this year as $0.05. You're right in terms of the following year. Until we start lapping these rates, you'll still have some downside in F '16. So…

Vivien Azer

That's – exactly. That's very helpful. My last question has to do on Australia. I think recently, Diageo announced that they had reduced the ADD [ph] on some of their ready-to-drink products. I know that's a big ready-to-drink market for you guys as well. Have you guys made any adjustments to your ADD [ph]?

Jane Morreau

Yes. And so Vivien, that's something that we constantly look at. We're looking at our proof and consumers and what they're looking for and what they see in the products and what they're wanting in our products all the time. We actually are currently, and have been for a number of years – the SoCo RTDs, our Southern Comfort RTDs, in that market have been at that rate that Diageo was lowering their Smirnoff down to and Captain Morgan – they did some time ago – we're already there. And so – but we don't have any plans for our premium Jack Daniel's RTDs, to reduce them to those rates at this time. But it's an ongoing thing that we always look at and consider the consumers while we're at it. It's interesting to note, we do have an RTD, that we do have at a lower proof than even the Diageo one. And it's more for special events, like your camps and mining and different things like that where the alcohol products are allowed to be sold, but at a much lower rate. So – but no plans right now.

Paul Varga

And I'll tell you – I will add that, that move by Diageo is, I suspect, a direct reflection of them trying to remain competitive given what's been going on in that country with what I consider to be excessive excise taxation. And so one of the tools available to any of the brand owners is to reformulate in order to make the products to continue to be affordable and attractive to consumers. So you do end up having a trade-off between alcohol content and price. And so their move, in my view, is understandable.

Jane Morreau

Yes, absolutely.

Operator

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

Nik Modi

Yes. Just a couple of quick questions for me. On the pricing, you had a – it looked like a real nice result. Just I was wondering if you can break it down for us in terms of rate and mix. And just provide some context around that. And then the second and third questions, just quickly, are you guys doing Jack – Winter Jack this season? I usually buy for Thanksgiving. I didn't see it in the stores. So just curious if you guys are going to have that back out there as we think about comparisons versus 1 year ago. And then just the last question is, the guidance really looks like it's implying a nice acceleration in the back half of the year. And if Jack Fire is not really the – going to be a big driver of that, I'm just curious on what will be the driver.

Jane Morreau

Yes. By the way, where do you live? We're going to make sure that in your liquor stores, we've got Jack Daniel's Winter Jack.

Paul Varga

It will be available, yes, right.

Jane Morreau

It should be, yes.

Paul Varga

Maybe it was sold out.

Jane Morreau

Yes, there you go. But yes, we are planning on selling it. In terms of the – of pricing, recall at the beginning of the year when we communicated that, and I think we're very much on track to deliver this price/mix that we've been talking about. But we took very – Paul already alluded to it. After 2 years of really hefty, strong pricing in the U.S. in 4% to 5% range, 2 consecutive years of those rates, we chose in the U.S. to moderate, take time out, get some of the competitors to catch up from a relative perspective. And so it's very low, about a percent is all we were planning. But we were still planning pricing outside the U.S. And so we are still seeing pricing coming in from – coming from outside of the U.S. And we're expecting, I believe, when we talked about this early on, that we were expecting about 1/3 of our growth in net sales to come from pricing for the year. So I think we're still on target on that. And then your question in terms of the acceleration on the back half of the year, I think one of the things you have to think about is what happened in the first quarter. We – there was only a 3% growth rate in the first quarter. We had tough comps in the first quarter. We talked to what was going on. It was largely retail inventory, if you will, and we adjusted for that, and we come along – we knew we were going to get an acceleration in the second quarter. We grew 7% in the second quarter. I don't expect that 7% to slow down for the balance of the year. So – in fact, when we get to our fourth quarter, we had a pretty weak fourth quarter in a couple of markets. Particularly, we've been talking about for some time in Poland and Germany, and we're expecting a rebound in both of those places. They had some buy-ins in their third quarter of last year. And so that – we're not even including Fire in that. These are the things that we're talking about that will give us a lift in our sales growth, so.

Paul Varga

Along with the U.S. acceleration that we've been seeing. I mean, I think that…

Jane Morreau

And the U.S. — ***indiscernible*** —

Paul Varga

We're certainly dependent on that continued performance in the U.S. from Jack Daniel's Black Label as one of the contributing factors, whereas – again, it was another piece of the business that…

Jane Morreau

Was slower.

Paul Varga

Was slower in the first quarter than it will be through the remainder of the 9 months. So when you think about key markets in Europe and you think about the U.S. and then focus on the results for second quarter and think about that over the remainder of the second half, it can account for the kind of guidance we're giving you.

Jane Morreau

Yes, exactly. And back on your question on Fire, though. Again, just to reiterate what we said in terms of the timing of this, this is a late fiscal year introduction. The time that it's going to take to get into the system from a distribution, and really for the consumer to start pulling in and so forth like that, we really are – we've written down …

Paul Varga

Very modest.

Jane Morreau

Very, very minimal, if any, a very small amount in the forecast. And then we know there will be a pipeline. So our reported results will get some benefit from that at the top. By the time you get to the bottom, it's minimal, too, because we want to introduce this brand in the best way we can and, to be successful, invest – we're investing a lot to support the launch.

Operator

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

Judy Hong

I had a couple of questions, really more around your markets outside the U.S. So first, maybe just touch on the U.K. and Germany related to, number one, if all of the trade inventory volatility, if that's behind us now, so we see more normalized buying patterns going forward. And then if you strip out the inventory movement, what are you really seeing from an underlying perspective? And then the second question is really related to Russia. I know it's only 2% of your business, but clearly a pretty volatile situation. So how much of risk are you factoring in as you look out for the next 6 months, 12 months? And what are you – what have you noticed so far just in terms of your trends in that market?

Jane Morreau

Lots of questions. Great, Judy. Yes, in terms of the – what we're seeing in the markets outside the U.S., particularly you're focusing on the U.K. and Germany and those were the 2 markets we called out in our first quarter outside the U.S. that were having some disruptions in trade inventory adjustments. The U.K. is back in balance. So in our numbers, they had a great second quarter, and they're back in balance. They're growing half single digits year-to-date.

Paul Varga

Did very well in Jack Daniel's Tennessee Honey, too.

Jane Morreau

Absolutely. Thanks, Paul. And then Germany is still going through a period of, I would call it buying disruptions, if you will. It's an interesting market right now. The economy is pretty difficult. We have set for ourselves a – what we believe is the right strategy as it relates to the price positioning of our brands. The retail market there, as you can imagine, is very challenged with the economy and looking to take prices down. And so we continue to work through this situation with them, with our retail partners in that market. But we have not worked through all that yet. So as I've noted in our script today, we still have a little bit of hangover, if you will, from retail adjustments in the U.S. and in Germany. And so if we take in consideration – those are the 2 primary markets left that we have that occurring in. If you take the 5.5% underlying growth that we reported this morning and adjust for these 2 things, you're over 6% underlying growth.

Paul Varga

Okay.

Judy Hong

Got it, okay. And then...

Jane Morreau

You had 2 questions. Oh, yes, the Russian.

Judy Hong

Yes, and Russia, yes.

Paul Varga

I think on Russia, Jane alluded to it a bit in her comments. But I think the thing that we're focused on, I mean, it's a place where of course, as it relates to any relevance for our company as it relates to the trade disputes that are going on between Russia and the United States, I mean, we're just – we're continuing, as we said in the first quarter, to cooperate fully. There's no news for us to report on that today. The thing that we would have seen in Q2 relative to Q1 was – one, very much prevalent in a lot of people's results, was just weakening economic conditions within Russia associated with the consumer level; but then also, for brands who've been in the press like some of ours, some hesitancy at the trade level associated with buying and putting into inventory the brands while there's uncertainty around the government's actions. So I think the combination of those. Then you add to it the – when you look at our reported results, what's happened with the ruble, you get sort of 3 factors influencing what's been going on in the last 90 days in Russia for us. So as we have updates to report on, anything as it relates to the Russian regulatory agencies and how that affects our business, we'll certainly bring those forward to you all.

Judy Hong

Okay. And then just following up on the national expansion of Fire. Any color just in terms of, is there any changes to the approach you're taking here versus Honey, whether it's faster rollout of the national expansion? Given that you've already invested behind the Honey flavor line, is there less investment to be made here? Just any color just in terms of the difference between how you're approaching Fire expansion versus Honey.

Paul Varga

Sure. Let me give you a little background on this. Because it's a – and we're, of course, number one, by nature conservative on this front because we're dealing with the Jack Daniel's trademark. And I think we're just, as you would expect – and I hope you would expect that we really want to measure, not just short term, but continue to monitor long term the impact of the these line extensions off of Jack Daniel's. And I think one of the reasons we've largely, over a very long period of time, done it well, is because the conservative approach to it has served – I mean, it has really served us well. Now having said that, there's this what we think a great opportunity out there for Jack Daniel's Tennessee Fire associated with what's going on in the – particularly in the U.S. right now with the flavored whiskey segment. And so I'll just draw a couple of comparisons between Tennessee Fire and Tennessee Honey. One is that Tennessee Honey itself is a brand that today is in excess of 1 million cases, approximates $25 a bottle and is growing in excess of 30%. And so, number one, we just think we want to make sure we keep our eye on that because the statistics I just cited there, those 3 things, are very unusual, to have brands of that size, at that price point, at that growth rate. And so first and foremost, we wanted to make sure and continue to make sure that Jack Daniel's Tennessee Honey has every opportunity to realize its full potential. And I'll remind everybody it's in year, I think, 4, 4.5, I guess, of – maybe in the United States, it would be early …

Jane Morreau

Starting its fourth.

Paul Varga

Yes, starting its fourth year. So part of this is to not have these things be a flash in the pan and to make sure they're nice, enduring, profitable, growing brands of Brown-Forman. So if you think about that and you approach Tennessee Fire, it being a second line extension in the flavored area, in a short amount of time, we're being cautious. That's why we went and tested it. For Jack Daniel's Tennessee Honey, we immediately went to a launch nationally in the United States in a relatively short amount of time. So with this, we wanted to make sure that what we were doing was well received in the consumer marketplace and…

Jane Morreau

And understand what it was doing to our own brand.

Paul Varga

Yes, you bet. And understand cannibalization, understand competitive reference, understand how the trade puts the brands into distribution and promotes them. So all these things that are just a little more complicated on the second one. Now the one thing I will say that is really encouraging to us, that has sort of enabled us to go ahead and announce the national rollout is how well it has done in test market. I mean, we've seen exceptionally strong test market results. And of course, we're reading not only what's happening volumetrically in the marketplace with sales and trial and all that, but really also focusing in on brand equity perceptions, doing a couple of ways of research to understand how the consumer is viewing Tennessee Fire. And I will just say, of course, one of the most important things that really points to great opportunity is that there's already a very large player in the cinnamon whiskey market that is both a potential source of volume, but also creates the opportunity for additional entrants. Now the one thing about it is the leader in this case is popular-priced. And we're going in at the premium level, and that's something we accept as a reality. But even with that, one thing that we've learned from the research is that Jack Daniel's Tennessee Fire against the marketplace today is seen as having great advantage on really important dimensions, at least they're very important to us, such as taste, premiumness, quality, authenticity, masculinity. So those are the types of things that we look to, to help us make these decisions. So price will always be an inhibitor for some on any product, and we would expect that to be one of the things that we, for any period of time, would be dealing with as it relates to this particular product. But nonetheless, we've been really encouraged by what we've seen. And just remember the other thing. The results of Tennessee Fire in its test markets have been as strong or stronger than what we would have seen for Tennessee Honey in its early days. And what really heartens us is that we really have had no media support behind it to speak of. It's mostly been promotional, some social media and word of mouth and in-store. So as we go national, we think there's an opportunity to build awareness and appeal at a higher level, similar to what we did with Tennessee Honey's launch. So I hope that gives you some background on why we've approached it the way we have. We'll continue to be both enthusiastic and optimistic about it but also appropriately conservative about it.

Operator

Your next question comes from the line of Bill Schmitz of Deutsche Bank.

William Schmitz

Can you just talk about cash flow in the quarter? I think a lot of it had to do with like the accrued tax liability, but it seems like you had negative cash from operations in the quarter. So can you just tell us if it's timing or something else? And then maybe the outlook for the rest of the year.

Jane Morreau

Sure. So if we look at – you're right, our cash flow was down, I think, about – as – cash flow from operations is really the driver. If you look at it, it was down about $130 million from same period last year. And if you think about what drove that, I think – I like to break it down in a couple of buckets. The first piece is what you would expect. You're going to have a small piece of it just due to just normal seasonality or, in our case, working capital increases because we've got a growing business and we're laying down more whiskey for our expected demand as we get out 3, 4, 5, 6 years from now. So set that aside. The majority of it, as you pointed out, 80% to 85% of it, was due to tax payments. And essentially, really all of it is timing. But let me explain the timing to you a bit. About

40% of that timing will clear itself out in the current fiscal year. And the remaining pieces of onetime in nature, that relates to some restructuring that we did in our European business, that onetime item is really spread over this year, where we had a payment that we made, last year where we got a benefit and next year where we're going to get a small benefit. So those 3 things together, net to the onetime item, is really just timing, if you will. And so when we look at the rest of the year, expect our cash flows to grow year-on-year, if you will. And our forecasts would suggest that as our business grows. So nothing unusual as you look at the rest of the year. I hope that helps you.

Operator

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

Bryan Spillane

I guess just a follow-up first on Bill's question. Just – and I might have missed it, but did you give an update on your capital spending guidance for the year?

Jane Morreau

I did not, but I'll be glad to. We're still projecting somewhere in the $120 million to $140 million range.

Bryan Spillane

Okay. And then I guess a second question just related to some of the earlier questions you had related to the sales outlook for the balance of the year. And I guess just the one thing, if you could help maybe shape how the environment – I mean, if you look at all the variables that went into projecting sales over the balance of this year from where we stand today versus sort of where they would have been when the year started, the – are there more negatives or positives in terms of kind of what you're looking at going forward today versus maybe what you were thinking about at the beginning of the year? And, I mean, I guess as I go through the list in my head, it just seems like Russia and maybe some emerging markets a little bit worse, Germany maybe a touch worse from a macro perspective. But on the other hand, you've seen some positive momentum in terms of some of the actions you've taken in the U.S., and then, of course, we're layering Fire on. So I'm just trying to get a sense, just sort of maybe your confidence in the 6% to 8% now maybe versus where it would have been at the start of the year relative to maybe some of those headwinds and tailwinds.

Paul Varga

I'll try. I mean, I think, well, the first thing, of course, Bryan, is that we've got 6 months behind us. So – but I think by nature, you're more confident about 6 months ahead of you versus 12. You always have the holiday season that you in this industry particularly you worry about it. But I think it's about the same. I think you had mentioned most of the – and I would say they largely offset each other. If I think about my own confidence level, I think U.S. is probably stronger, and it's a big – it's our #1 country. I would say I feel stronger about it today than I would have back in, say, May or something. And – but I think you're right to call out Russia and actually the prolonged nature of the excise tax increases in Poland. I would have hoped there would have been a – the consumer and the trade would have adjusted more rapidly than we've seen them. But again, that gives us some of the confidence in the back half because you'll go against some pretty soft comps in the fourth quarter there particularly. And part of it is, too, this will be a year away from the sort of sticker shock that comes from these excise taxes. So I think you hit it about right. I mean, you have some regional reallocations. But generally, I mean, I kind of said at the beginning, I like – continue to like the balance of our growth across the globe. And that diversification we have allows us to make adjustments. The other thing is, they're smaller levels, but things like Herradura continuing to do better and the premium products, Woodford Reserve. I mean, if you just look at, over the years, particularly a brand like Woodford Reserve is just getting bigger and bigger. And so something like at that size, it's growing 30%-plus, starts to have an impact. And so I think a lot of it – we'll, of course, reevaluate this after we see the December results because it's such a big period for us. But we do think we're going to have pretty favorable comps in Q4 for the company generally. And so that gives us a lot of confidence about the range we've provided today.

Operator

— ***Operator Instructions*** — Your next question comes from the line of Mark Swartzberg of Stifel.

Mark Swartzberg

Yes. And that perspective on Tennessee Fire was very helpful, Paul. I guess a few questions. Firstly, Jane, the $0.05 you mentioned from FX in the quarter, can you just repeat what that was? It's not going to be recurring here at least as far as you can tell for the second half?

Jane Morreau

Sure. The $0.05 that I was referring to was actually the first half, $0.02 of which happened in the first quarter related to a onetime item, intercompany item. The other $0.03 relates to our net current assets, primarily cash, in Europe, by the way, that are denominated in euros and exchanged to U.S. dollars. So it's just the revaluation impact on that. And so this – again, we have to use today's spot and say, okay, here's what your exposure is. And we've got that all captured, whereas if you look at your transactional aspect of it at today's spot rate, you still have downside relative to the prior year as a result of the spot rate.

Mark Swartzberg

Got it, great.

Jane Morreau

Does that help? Yes, so it helps, yes.

Mark Swartzberg

Yes, it does. And that's great. And then on Germany, I – really a follow-on to Judy's question. You're talking about the fourth quarter benefiting there. Can you speak to takeaway or give us a little more color on why you expect this down performance to reverse in the second half and into next fiscal year?

Jane Morreau

And so – actually, I want to start with Poland. We actually have seen some recent take-away trends that are showing some positive improvement on both Finlandia and Jack from a takeaway perspective. So they are growing again. So that bodes well for the rest of the year. Plus in that market, as well as Germany, because of the price increases, so there was a large buy-in, in the third quarter in both those markets in advance of price increases on January 1. One was excise tax driven. That was Poland. And the second one was a price increase on – in the German market on our brands. There was a large buy-in, in the market on both those brands in the third quarter, which resulted in, of course, in Poland the sticker shock. There was a buy-in, in the fourth quarter. So we know we will back – we'll get back in balance in terms of our inventory levels. And if we see takeaway trends accelerating, we would expect to see our results to have a benefit, not only cycling against a weak comp, where no activity was going on or very little activity was going on, to where we're seeing some growth now.

Paul Varga

Also I think in Germany, there – just the retail activity itself is – the retailers in that market, I mean, the takeaway trends have been softer this year than they were 1 year ago. And – but part of that, I think, is associated with, since there are some very large retailers there and a couple have changed – one in particular has changed their manner in which they price to the consumer, I mean, where you and I might call it one of these sort of everyday low pricing version of that. And that always, I think, takes the marketplace time to adjust to their – at the consumer level – time to adjust to new buying patterns as well. So some of those show up in our consumer takeaway numbers, of course. And so I think part of it is just time away from higher prices. As you move from month-to-month or quarter-to-quarter, I think your confidence level raises. And that's beyond the levels of just favorable comps because there was buy-ins and then basically very low sales afterwards. But I do think some of it is really, in the end, one of focus on the consumer level, and we think just time away from those higher places and acclimation to them helps.

Mark Swartzberg

Got it. And can you speak to order of magnitude, what takeaway rates you're seeing right now in Germany?

Paul Varga

Hang on just a second. We can refer to – let's see if we've got something we can refer to.

Jane Morreau

Yes. So Germany, categories are growing – whiskey category itself was growing in the mid- to high single digits. And in Poland, whiskey's back growing in high single digits.

Mark Swartzberg

So a very good backdrop here once you got these inventory adjustments taken care of. That's great. Okay.

Paul Varga

Yes. And acclimation to prices, yes.

Mark Swartzberg

That's great. Okay. And then 2 final ones. One is vodka segment here in the United States heading into the holidays. Anything notable in terms of pricing behavior among the competition? Any changes there? And then finally, capital allocation. You authorized another round of repurchase. You're below 1x EBITDA in terms of leverage. I think you're going to continue to be below 1x when you look out a year absent any deals. Can you just speak to why you're not returning more cash more aggressively to shareholders?

Jane Morreau

Yes.

Paul Varga

Why we're not returning more cash to shareholders? I think…

Mark Swartzberg

Yes, taking the opportunity to lever up a bit, nothing crazy. But get a little more leverage and return more cash.

Paul Varga

Yes, I mean, we always look at that, as you've seen. I mean, we tend to look at that over much longer periods of time than just what's happening in a particular year or quarter. But, I would certainly say that over the past several years, we've been returning more shareholders than, for example, making acquisitions – returning more to shareholders than making acquisitions. And of course, that's been a good investment on behalf of the company and the shareholders. But we'll always look at that. I just think that compared to what we've seen out there as the uses of cash, particularly around the acquisition area, it's been pretty thin as it relates to things that we've found attractive and advisable. So – and that's reflected in sort of the absence of really any acquisitions in some time at the company. On the – contrast, we've been very successful with innovation. So as companies think through how to win in the marketplace, you always have the opportunity to buy it or to build it. And in the case of the last few years, we've been successful in innovating. Around vodka, I mean, my general comment about that globally is it is brutally competitive right now. I mean, the – if you think about the large markets for it, you've got

Russia, Poland, the United States as being the premier markets. And we've already talked about Russia and Poland quite a bit here. So with excise taxes and people repositioning or innovating to hit lower price points, I mean, it's just very, very competitive, particularly in Poland and Russia. And then I would say over in the United States, I mean, a lot – it's really been interesting to watch. It's harder to get prices these days. The flavored aspect of the U.S. vodka market has gone soft here in the last couple of years, and the winning brands happen to be coming from – as was the case 5 years ago, to the established brands – from upstarts. And so there's – it's undeniable that Tito's is the sort of leading growth brand. And it's not in the flavored business, it's benefiting from the organic and local, and sort of craft benefit – there's – and so one of the lessons that you see over time from vodka is that you – once you think you have an established brand, because there's very few barriers to entry, particularly in this U.S. market – you really see new brands come in and capture the imagination of consumers. It's true of both Tito's and this Gallo entrant, New Amsterdam, so.

Mark Swartzberg

That's great. And one quick follow-up on that. On the margin here in the U.S., price competition, similar to what it was 3 months ago? What's the dynamic here in the U.S. on price in vodka?

Paul Varga

Oh, it's stable. I mean, tough to get prices, it looks like to me. I think the big dynamic that's influencing growth in vodka right now is the flavors have, in terms of their ability to add to growth versus the prior year, have become soft. And it's always been the case that the ability to get price in whiskey was far greater than it was in vodka in most of the key markets.

Operator

Your final question comes from the line of Bill Chappell of SunTrust.

Stephanie Benjamin

This is actually Stephanie on for Bill. Just kind of going off of Judy's question earlier, first in terms of what's going on in Russia. Now is this primarily impacting just the vodka sales? Or is it more broad- based across brands? And then secondly, just on your rollout of Tennessee Fire, are we going to start seeing maybe shipments for like half the country starting in the third quarter, with the majority of the launch in the fourth quarter? Or is it all kind of primarily in 4Q?

Paul Varga

On the last question, you should just expect Q4.

Jane Morreau

Yes.

Paul Varga

It'd be – it'll be sort of February and beyond for us. And on Russia, the impact, I mean, I'd break it into the consumer impact, because of the weakening Russian economy, would apply to all categories. I mean, it's just really – it would be difficult – whatever impacts the consumer will influence their purchasing patterns generally. I mean, overall, the whiskeys in that market tend to be more premium- priced than the vodkas, generally because there's so many local – important vodka brands in Russia. But the – as it relates to our company, some of the concerns and risks we've identified through this first half have been more associated with some of the things that have been, in the public side, related to Jack Daniel's and would not have applied as much to Finlandia. So in Finlandia, we would worry more about the competitiveness and the economy in Russia, whereas, on Jack Daniel's, we'd worry about that, we'd worry about also some of these regulatory concerns we've surfaced and, on both of them, of course, for our company, worry about the translation effect of the ruble, so.

Stephanie Benjamin

Got it. That's very helpful. And then just quickly on housekeeping, are you still expecting the 29.5% tax rate for the year? Because I noticed it was just a little bit higher in the second quarter.

Jane Morreau

Just I would pencil in – just use 30%.

Stephanie Benjamin

30%? Okay.

Jane Morreau

Yes.

Paul Varga

Okay.

Jason Koval

Okay. Thank you, Paul and Jane. And thanks to all of you for joining us today for our second quarter earnings call. Many of you have already RSVP-ed for our Investor Day on December 10. But for those of you who haven't yet, please feel free to follow up after our call, and we'll make sure you have all the details. Have a great week, and we look forward to seeing you next week in New York. Thanks.

Jane Morreau

Thanks.

Operator

Thank you for participating in the Brown-Forman Second Quarter Fiscal Year 2015 Earnings Conference Call. You may now disconnect.