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Conagra Brands, Inc. (CAG) CEO Sean Connolly on Q1 2020 Results - Earnings Call Transcript

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FQ1: 09-26-19 Earnings Summary

Press Release SEC *10-Q* *Slides*

EPS of $0.43 beats by $0.04 | Revenue of $2.39B (30.33% Y/Y) misses by $-88.86M

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Conagra Brands, Inc. (NYSE:CAG) Q1 2020 Results Conference Call September 26, 2019 9:30 AM ET

Company Participants

Brian Kearney - IR

Sean Connolly - President and CEO

David Marberger - EVP and CFO

Tom McGough - EVP and Co-COO

Darren Serrao - EVP and Co-COO

Conference Call Participants

Andrew Lazar - Barclays

Ken Goldman - JP Morgan

Bryan Spillane - Bank of America

Robert Moskow - Credit Suisse

David Palmer - Evercore ISI

Chris Growe - Stifel

Steve Strycula - UBS

Jason English - Goldman Sachs

Operator

Good day. And welcome to the Conagra Brands First Quarter Fiscal Year 2020 Earnings Conference Call. All participants will be in a listen-only mode. [Operator Instructions] After today's presentation, there will be an opportunity to ask questions. [Operator Instructions] Please note, this event is being recorded.

I would now like to turn the conference over to Brian Kearney of Investor Relations. Please go ahead.

Brian Kearney

Good morning, everyone. Thanks for joining us. I'll remind you that we will be making some forward-looking statements during today's call. While we are making those statements in good faith, we do not have any guarantee about the results that we will achieve. Descriptions of risk factors are included in the documents we filed with the SEC. Also we will be discussing some non-GAAP financial measures. References to adjusted items, including organic net sales growth, refer to measures that exclude items management believes impact the comparability for the period referenced. Please see the earnings release for additional information on our comparability items.

The reconciliations of those adjusted measures to the most directly comparable GAAP measures can be found in either the earnings press release or in the earnings slides, both of which can be found in the Investor Relations section of our website, conagrabrands.com.

Finally, we will be making references to Total Conagra Brands, Legacy Conagra Brands, and Legacy Pinnacle. References to Legacy Conagra Brands refer to measures that exclude any income or expenses associated with the recently acquired Pinnacle Foods business.

With that, I'll turn it over to Sean.

Sean Connolly

Thanks, Brian. Good morning, everyone, and thank you for joining our first quarter fiscal 2020 earnings call.

Fiscal 2020 is on track following a very solid Q1. We continue to implement the Conagra Way to profitable growth by executing against the principles and plan we shared at Investor Day. We're applying our value-over-volume playbook to the Legacy Pinnacle portfolio, and we've made important progress strengthening the foundation of the business and repositioning Pinnacle’s leadership brands for profitable growth. We're also pleased to report that our ongoing integration and synergy capture related to the Pinnacle business and our deleveraging progress remain squarely on track. In Legacy Conagra, we continued to deliver solid execution and maintained our momentum in the first quarter, particularly in our leading frozen and snacks businesses.

Looking ahead, we remain confident that our second half results will reflect stronger growth than the first half. We'll lap the anniversary of the Pinnacle acquisition, and the easier comps due to the start of our value-over-volume execution across its portfolio. We'll also begin to benefit from the exciting new innovations that are being introduced to the market. Therefore, we are reaffirming our fiscal 2020 guidance for all previously communicated metrics.

Our agenda this morning is to provide an update on our work on the Legacy Pinnacle business, discuss our continued progress on Legacy Conagra, and share some additional details on our expectations for the remainder of the year.

Turning to the Legacy Pinnacle portfolio. Before diving into the details here, I'd like to take a step back and review the central tenets of our value-over-volume playbook, which is essentially our approach to optimizing the base business and establishing a stronger foundation on which to build. As you've heard me say before, value-over-volume is a disciplined approach to growth that acknowledges not all volume is created equal and consumer demands are always evolving. The approach dictates that we consistently apply rigorous portfolio management. Value-over-volume involves eliminating weaker SKUs in advance of the launch of higher performing new products and the associated brand building investments. It also involves renovating the core and getting the fundamentals right. These fundamentals include pricing, promotion, assortment, distribution, product quality and packaging. We've previously shared that our application of value-over-volumes of a Legacy Pinnacle portfolio would be a key priority.

As you can see on slide seven, we're making real progress. In fact, we're seeing very similar patterns to what we saw in Legacy Conagra a few years ago. We've trimmed low quality SKUs from the marketplace, we've seen TPDs decline near-term. But importantly, we've also seen base velocities improve sharply. We demonstrated on brands like Banquet and Healthy Choice in Legacy Conagra. This creates a much stronger foundation on which to infuse brand building investments.

Wish-Bone is one of the key Legacy Pinnacle brands, where we're furthest along in strengthening the foundation. As we've discussed previously, Wish-Bone was challenged by several issues, service, quality and the label change executions. We identified the issues and took action, fixing the service challenges, improving labels for better variety communication and also upgrading the product quality.

As you can see on slide eight, we’ve stabilized the business; in fact, we grew it in Q1. We also remain highly focused on executing our playbook on the Birds Eye and Duncan Hines brands. Low performing SKUs have come out of the market and fundamentals are improving. Keep in mind that we're in the very early stages of recognizing the benefits from our new innovations in these categories. The shelf reset windows at large customers are different than they are for Wish-Bone. So, the timing of their recoveries is different. We do anticipate improvement in the second half of fiscal 2020 for both of these brands as they begin to benefit from the addition of our new innovation slate. We're confident that the Birds Eye and Duncan Hines brands will continue to stabilize and are on track for profitable growth.

We also remain on track across all our integrations, synergies, and deleveraging initiatives as highlighted on slide 10. Across the board, we're very pleased with the execution of our integration activities. Our employee related transitions are now substantially complete. And since the close of the transaction through the end of Q1, we've realized $71 million of cost synergies.

From a balance sheet perspective, we're on schedule with our deleveraging plan, having reduced total gross debt by $148 million in the first quarter and by more than $1 billion from the transaction close through the end of Q1. As we consistently said, we remain firmly committed to maintaining a solid investment grade credit rating.

Overall, we had a solid first quarter on Legacy Pinnacle; we've made good progress in strengthening the foundation across the portfolio and look forward to continued improvement in the back half of the year as we begin to benefit from the new innovations.

Turning to Legacy Conagra. The business started the year well, and we're pleased with the trends we're seeing. The Legacy Conagra business delivered solid performance during the quarter. Together, the two large domestic retail businesses outperformed their planned organic net sales growth. Yet again, we saw terrific momentum in our Legacy Conagra frozen and snacks businesses. As expected, our grocery sales performance in Q1 was impacted by some holdover from the Hunt's and Chef Boyardee dynamics that we detailed last quarter. As we'll share with you today, we have action plans in place and trends are already improving.

But we also experienced some unplanned softness in our International and Foodservice segments during the quarter. And this negatively impacted our top-line performance. This softness relates to some onetime issues, and both segments are expected to recover in the second half. Importantly, despite these top-line headwinds, our International and Foodservice segments overdelivered their profit plans for the quarter. Let's get into each of these items in more detail.

Turning to slide 13. You can see that total retail sales for the Legacy Conagra business were up 0.9% from the same period a year ago, demonstrating 2.7% growth over the two-year period. While I'll walk you through the year-on-year drivers of the fiscal year in a moment, you can see in this chart that the two-year growth rate has been fairly stable for the past four quarters and we're entering a period of easier comparisons on a one-year basis.

On slide 14, you can see that we continued our momentum in the Legacy Conagra frozen portfolio throughout the first quarter with retail sales growing 2.5%. In addition, our Legacy Conagra frozen meals business continued to outperform our peers in Q1. In fact, it has become the industry leader in the frozen category. Our Legacy Conagra meals -- frozen meals business now has the number one position in share of total retail sales and gained share of category dollars in Q1.

Slide 16 demonstrates that we’re also gaining share of shelf. As we’ve discussed, in some instances, our actions to remove low-performing products drives lower TPDs as we create more holding power for our higher velocity items. In other cases, we've seen TPDs expand. In either event, our goal is to grow share of shelf. And that's exactly what we're doing.

As we know, our retail customers run the ultimate meritocracy. They will give more space to the products that move up the shelf the fastest. This data demonstrates that we're earning more shelf space by having products that consumers demand. Importantly, shelf space is a leading indicator that bodes well for our opportunity to grow sales.

Frozen wasn't the only leader in our Legacy Conagra portfolio in Q1. Snacks also maintained momentum through the first quarter and delivered strong results across a variety of brands and categories. Total retail sales in snacks were up an impressive 7.2% versus a year ago. Meat snacks and seeds emerged as particularly strong leaders with an increase in retail sales of 9.4% and 8.5%, respectively. Overall retail dollar sales in snacks demonstrated sustained performance improvement throughout the first quarter, having grown 9.8% on a two-year basis.

Similar to frozen, our Legacy Conagra snacks business is also outperforming its peers and gaining share as demonstrated on slide 18.

Turning to the Legacy Conagra grocery portfolio for a moment. If you recall, last quarter, we faced headwinds in our grocery portfolio related to pricing and promotional challenges. As the cost of steel cans increased, we implemented inflation justified pricing on Hunt's canned tomatoes and Chef Boyardee to partially offset the increased cost. However, our private label competition in canned tomatoes kept prices flat and in some instances, actually decreased prices. And on Chef Boyardee we lost some high quality merchandising. The effect of these dynamics was a higher than expected volume decline in Q4. We planned for this decline to continue through the first quarter as a carryover from Q4, and it did. We've already begun implementing action plans for each of these brands to reverse this trend.

Before I get to the year to go, I'll cover Foodservice and International. As I mentioned earlier, we faced some unplanned softness in the top-line performance in our International and Foodservice segments during the quarter. International segment was impacted by external events in Puerto Rico and India that shifted the timing of sales previously expected in Q1 to the second half. While this shift in timing impacts our quarter-to-quarter results, we expect that it will have no net impact on the top-line for the fiscal year. Partially offsetting this timing shift, our International segment benefited from growth in snacks and frozen, the improved mix as well as cost savings resulted in higher than planned operating profit and margins in the quarter.

In our Foodservice segment, we made the strategic decision this quarter to opt out of a particularly low margin contract, consistent with our value-over-volume strategy. While this decision negatively impacted our top-line in the near term, it was the right thing to do for the health of the business, and benefited our Q1 margins in the segment. Furthermore, we expect stronger top-line performance in Foodservice for the balance of the year with new items coming to market. We also expect better than anticipated performance from Gardein within the Foodservice segment, which will start to be included in our organic number during the second quarter.

Looking ahead, we're excited about what's to come in the back half of the year. First, we are providing more promotional support on Hunt's and Chef Boyardee to better compete in market. Second, we've got a strong investment plan for Q2 for the new innovation that's about to hit the market. In fact, the second quarter will mark the peak of our investment cycle as we incur launch expenses to tee up our slate of new products. And third, we expect terrific second half growth. We'll see innovation build across many of our segments in the second half of the year. We expect our in-store presence to be much stronger and drive growth. Some categories this will be on the back of increased TPDs and in others, it will come on the back of increased facings on high velocity items.

We'll also benefit from easier comparisons in the back half of the year, as we ramp prior year value or volume activity and increased competition. In addition, we'll lap the anniversary of our Pinnacle acquisition, discreet supply chain disruptions, and the higher interest expense and share count that started in Q2 of last year.

Let's go into each of these items in a bit more detail. Starting in the second quarter, we began launching new, smart promotional support for Hunt's and Chef Boyardee to improve volume trends. Remember, Hunt's and Chef Boyardee continued to maintain the number one position in their categories among branded competitors. Both brands are of critical importance to consumers.

We're already seeing early traction on both brands, as demonstrated on slide 23. The first two weeks of our second quarter have shown the benefit of these strategic promotions. It's certainly early days, and we have some tougher comps in the weeks ahead, given the year ago hurricane activity. But, we're confident that we have the right marketplace strategies now in place to deliver sequential improvement throughout the second half of the year.

We're also excited to introduce exciting new products to our $2 billion snacks portfolio throughout the remainder of the fiscal year. Our latest innovation slate, a portion of which is shown here, will premiere at NACS in October. We're delivering products with bold flavors, new forms, and optimized price pack architecture. Any of you are at NACS, please stop by our booth to see this great work for yourself.

We're proud of our snacks portfolio; it's one of the fastest growing. We're confident that our continued innovation in the space will further differentiate and elevate our already iconic brands. We're also excited about our new Conagra Brands Center for Food Design, which we expect to open in the first calendar quarter of 2020, next door to our headquarters in Chicago. This is an expansion of our state-of-the-art, R&D and culinary capabilities, and will be exclusively focused on snacking related innovation. This facility will combine culinary, food and packaging design expertise in one space, enabling the rapid development of even more contemporary snacking products.

We're also introducing reinvigorated innovation to our sweet treats portfolio in the back half of the year across both Legacy Pinnacle and Legacy Conagra Brands. Duncan Hines is being reframed as a sweet treat to unlock significant growing demand spaces with refreshed packaging, fun and novel flavors and new snacking platforms.

Legacy Conagra's snacking brands will also receive an injection of innovation to capture consumer excitement with trending kid friendly themes.

We plan to build upon our category leading position in frozen by introducing our strongest innovation slate to date throughout the balance of fiscal 2020. We've been strategically tailoring our products to fit the needs of today's busy consumers by providing them with premium, nutritious ingredients and increasing sustainability, all at affordable price points.

Birds Eye is expected to benefit meaningfully from these efforts. We expect Birds Eye performance to accelerate in the second half as we see the impacts of our recently launched innovation slate, as well as upcoming new product introductions, including spiralized zucchini. As one of the largest brands in frozen vegetables, we're confident that Birds Eye is well positioned to capitalize on contemporary forms and trending flavors.

Another brand in our portfolio with significant growth opportunity is Gardein, which we spoke about at length last quarter. We're working hard to continue to build out the Gardein brand to capitalize on the explosive growth in the plant-based meat-alternative space. The Gardein foodservice business grew an impressive 25% in the first quarter, and continues to accelerate penetration across multiple Foodservice channels. As we shared with you last quarter, the brand is the second largest in the plant-based meat alternative space, and has already quadrupled in size over the past four years.

In retail, we expect our Gardein to gain prominence in both frozen and refrigerated as we introduce more high-quality innovation. On-trend brand with modern attributes, Gardein is uniquely positioned to generate superior velocities by leveraging Conagra's culinary capabilities, differentiated packaging techniques, and our diverse portfolio of power brands. And we are well-positioned to support Gardein's continued growth with new capacity coming on line during Q2.

Overall, we're pleased with the progress Conagra has made in the first quarter of fiscal 2020. We're on track with our plan and confident in our ability to accelerate growth in the second half of the year and deliver our fiscal 2020 guidance.

With that, I'll turn it over to Dave.

David Marberger

Thank you, Sean, and good morning, everyone.

This morning, I'll walk through our first quarter fiscal ‘20 performance before we open it up for questions. As a reminder, starting this quarter, Conagra no longer reports Pinnacle as a standalone reporting segment. Pinnacle's business components have been allocated to the four Legacy Conagra reporting segments to reflect how we are now managing the business. You can find historical segment financial information that reflects this recast in an 8-K furnished with the SEC on September 23rd.

Slide 31 outlines our performance for the quarter. I'll walk through more detail in a moment, but I'll start here by noting a few highlights. Compared to the same period a year ago, net sales for the first quarter were up 30.3%, primarily reflecting the acquisition of Pinnacle Foods. Organic net sales were down 1.7%. The decrease in organic sales was primarily driven by the unplanned softness in International and Foodservice, and the planned declines in our Grocery & Snacks segment that Sean discussed.

Adjusted operating profit for the first quarter was up 40% and adjusted operating margin increased 108 basis points to 15.7%, which was ahead of our internal expectations.

I'll walk you through the adjusted EPS bridge in a moment. However, I want to highlight that while our adjusted EPS decreased 8.5% to $0.43 for the quarter, adjusted net income increased 12.5%. Our increase in operating profit more than offset the impact of the increased interest expense associated with the Pinnacle transaction.

Slide 32 outlines the drivers of our first quarter net sales versus the same period a year ago. We continued to drive an increase in price mix, even after taking into account our increases in retailer investments to support brand building. It should also be noted that the 32.1% increase from acquisitions and divestitures includes 3.7 percentage points of decrease from the sales of the Wesson oil, Gelit and Canadian Del Monte businesses and the Trenton production facility.

Slide 33 provides a summary of net sales by segment for the first quarter. Again, the Legacy Pinnacle business has been allocated to the four other reporting segments. So, we are not showing in Pinnacle segment anymore. I will discuss Pinnacle Q1 net sales in more detail shortly.

Grocery & Snacks net sales increased 26.9% in Q1 as the acquisition of Pinnacle added 34.7% and the divestiture of Wesson oil subtracted 4.1% from the net sales growth rate. Organic net sales for Grocery & Snacks decreased 3.7% as the planned declines in Hunt's tomatoes and Chef Boyardee were partially offset by continued strong in-market performance and innovation success in our snacks business.

The Refrigerated & Frozen segment benefited once again from our robust slate of innovation across multiple Legacy Conagra brands, including Banquet, Healthy Choice, P.F. Chang's Reddi-wip and Sandwich Bros.

During the quarter, Refrigerated & Frozen net sales and organic net sales increased 51% and 1.5%, respectively with organic growth in both volume and price mix.

Our International segment increased net sales 5.5% in Q1 due primarily to the acquisition of Pinnacle. International organic net sales continued to benefit from growth in the snacks and frozen businesses in certain regions. However, the segment's organic net sales were down versus plan in prior year due to discrete items in our businesses in Puerto Rico and India. As Sean mentioned, these items shifted the timing of sales previously expected in Q1 to the second half. This timing shift contributed to a decrease of 3% in organic net sales during the quarter.

In our Foodservice segment, we made the strategic decision in Q1 to opt out of a lower margin contract, consistent with our value-over-volume strategy. As a result of this decision, Foodservice organic net sales declined 3.2% for the quarter. Reported net sales increased 6.3% during the quarter with the acquisition of Pinnacle adding 15.3% and the sales of Wesson and Trenton subtracting 5.8% from the net sales growth rate. We expect a stronger balance of the year performance from this Foodservice segment with new items coming to market and improved performance from Gardein.

Slide 34 outlines Pinnacle's fiscal ‘20 net sales for Q1 versus fiscal year ‘19 pro forma net sales for the same period. The 9.2% sales decline was largely in line with our expectations. As we increased brand building investments with retailers, eliminated some low-quality promotions and saw some inventory reductions with retailers in advance of implementing new shelf sets. While these dynamics led to a wider than typical difference between shipments and consumption in the quarter, we don't expect this dynamic to continue for the year to go period.

Slide 35 outlines the puts and takes of our Q1 adjusted operating margin versus the prior year. It's worth noting that the impact of the Legacy Pinnacle gross profit was a decrease to operating margin of 46 basis points during the quarter versus the prior year. Our Legacy Conagra realized productivity initiatives are progressing as planned and helping to offset inflation, which approximated 2.8% in Q1. We're also seeing a margin benefit of Pinnacle synergies in Q1, particularly in SG&A.

Slide 36 outlines the significant progress on Pinnacle synergy capture, which remains on-track in all areas: SG&A, cost of goods sold, and trade spending. We realized approximately $40 million of cost savings in the quarter, which brings total cost synergy capture to approximately $71 million since the closing of the acquisition through the first quarter. We continue to expect synergies to increase throughout fiscal ‘20. And as previously announced, we expect to achieve the majority of our $285 million in cost synergies related to the transaction by the end of fiscal ‘20.

Moving to slide 37. Conagra's total adjusted operating profit increased 40% in Q1. Our adjusted operating margin came in at 15.7%.

Each segment's adjusted operating profit benefited from the addition of Pinnacle's profit. The International segment was the only segment to see a decline in adjusted operating profit in the quarter. And that was driven by the impacts of divestitures, unfavorable FX, and the volume impact from the discrete items in the quarter.

The Grocery & Snacks segment margin decreased year-over-year. Approximately half of the margin decline was a result of the legacy technical Grocery & Snacks business being dilutive to overall segment gross margin with the rest of the decline coming from inflation and brand investment with retailers, exceeding pricing and realized productivity.

The Refrigerated & Frozen segment showed very good margin expansion in the quarter. While the Legacy Pinnacle business was slightly accretive to the segment's margins, the segment benefited from strong cost of goods sold realized productivity and synergies in the quarter.

The International segment's decline in operating margins was primarily attributed to the impact of FX, and the lower margin Pinnacle business being included in the segment. Operating margins improved for the quarter on an organic basis after excluding FX and M&A. Finally, the Foodservice business saw nice margin expansion in the quarter as it continued to execute its value-over-volume strategy.

Slide 38 outlines the drivers of our Q1 adjusted diluted EPS from continuing operations versus the same period a year ago. As you can see, Conagra's adjusted EPS decreased $0.04. Approximately $0.02 of this decline were from divested businesses, and $0.02 were from a decline in the Ardent Mills joint venture. The increase in adjusted operating profit and taxes, offset the impact of increased interest expense and shares outstanding.

Slide 39 summarizes net debt and cash flow information and shows the solid progress we've made over the last four quarters to improve our balance sheet. Compared to the end of Q4 fiscal '19, net debt was approximately flat as we used cash on hand to fund a reduction in gross debt of approximately $150 million during the quarter. This was in line with our expectations given the quarterly seasonality of the business.

In total, I'm happy with our progress to-date. Since the close of the Pinnacle acquisition in the second quarter of fiscal ‘19 through the end of the first quarter of fiscal ‘20, we have reduced gross debt by over $1 billion. And with the recently announced pending divestiture of our DSD snacks business, we'll have some additional cash on hand for debt repayments after we close. As we stated, we don't need divestitures to achieve our deleveraging targets, but they can accelerate our progress.

Overall, we remain on schedule with our fiscal ‘21 target of a net debt to trailing 12 months adjusted EBITDA ratio of 3.6 to 3.5 times. As we've consistently said, we are committed to a solid investment grade credit rating. As noted in our release, we are reaffirming our fiscal ‘20 guidance.

Slide 40 outlines our fiscal ‘20 outlook across all metrics. Please note that the organic sales growth rate excludes the impacts of fiscal ‘20’s 53rd week. All other metrics on this slide include the impact of the 53rd week.

It is also important to note that the financial information included in our presentation today includes the expected full fiscal year results of the DSD snacks business. As disclosed earlier this month, we expect this transaction to close by the end of the calendar year as it remains subject to customary closing conditions. The expected annualized impact from this divestiture is approximately $110 million of net sales and $0.02 of adjusted EPS.

I'd also like to highlight that we continue to believe in the planning assumptions that we noted during our Q4 fiscal ‘19 call.

Overall, we see fiscal ‘20 results being more heavily weighted towards the second half. With respect to our organic net sales growth, our plan calls for higher innovation related investment with retailers during the first half of fiscal ‘20, with investment peaking in the upcoming second quarter, resulting in expected second quarter gross margin coming in below our Q1 levels.

The related sales growth is weighted towards the second half of fiscal ‘20 as our distribution, trial and repeat builds throughout the year. We expect margins to improve during the second half of fiscal ‘20. Innovation related investment will be higher in the first half, as I just mentioned. The impact of synergies will also increase as we move through the year, helping margins.

We expect Pinnacle to continue to be dilutive to our year-over-year total gross margin until we anniversary the acquisition in late October. Finally, in the second half, we will be lapping the higher levels of interest expense and share count, allowing for easier comparisons.

That concludes my remarks. Thank you for listening. I'll now pass it to the operator as Sean, Tom McGough, Darren Serrao and I are ready to take your questions.

Question-and-Answer Session

Operator

Thank you. We will now begin the question-and-answer session. [Operator Instructions] And the first question today comes from Andrew Lazar of Barclays. Please go ahead.

Andrew Lazar

Good morning, everybody. And thanks for the questions.

Sean Connolly

Good morning, Andrew.

Andrew Lazar

Hey. So, first off, you talk about the -- what you see is still strong momentum in the Legacy frozen business specifically. I guess, in some of the more recent data, we've seen a little bit that both some of the -- on a sequential and sort of two-year basis, some of the trends slow a bit on again those Legacy frozen brands. I guess, what do you attribute this to? And do you expect this to perk up as fiscal 2Q progresses? And if so, what drives that?

Sean Connolly

Sure, Andrew. Let me address that. First, let me give you my perspective on our top-line trends overall. As you heard me say in my prepared remarks, top-line is tracking pretty much how we planned it with the obvious exception being International and Foodservice, which is again timing. Frozen is thriving, snacks is thriving; grocery is on track, navigating some competitive dynamics on a couple of brands, and value-over-volume is doing its thing on Pinnacle. So, one quarter down, we're on track.

Now, in Q2, we're investing meaningfully to tee up a terrific innovation slate that will support our strong second half growth. That's always been the plan, and we're excited to see it unfold. What you're seeing much more recently is a function of the fact that we are in a transitionary period at some major customers with respect to new shelf sets in frozen. And we have in fact seen some out of stocks as the new tags are being set. So, to be clear, no drop-off in consumer pull. This is a temporary dynamic; it's fairly typical in -- right in advance of the new shelf sets. And in terms of share of shelf and share of market that we're seeing in the very early days of these new shelf sets, we continue to see positive momentum. So, that bodes well.

Andrew Lazar

Great. That's really helpful on that one. So, thank you for that. And then, I guess lastly, just I wanted to zero in a little bit on the sales bridge for a moment. Specifically price mix, excluding the retailer investments, accelerated significantly from 4Q to 1Q. Retailer investment declined at a greater rate sequentially. I assume some of this is spending against the Hunt’s and Chef sort of competitiveness and reflected in those retailer sort of spending investment bucket. But, maybe you could talk about that a bit. In other words, I guess, what part of retailer investments is sort of promotions on these brands, maybe versus actual brand building at the point of sale?

Sean Connolly

I'll give you some big picture on that Andrew. And Dave, fill in any details. When we partner with our customers to drive mental and physical availability on our brands, it's kind of a holistic discussion. Again, it may involve merchandising off the shelf, it may involve pricing incentives. It's the total package. It may involve online programs, things like that. So, that's really a holistic program. But, with respect to Q1, keep in mind, we had particularly strong growth in frozen and in snacks. And part of what drives that growth is the investments that we are making with our retailers. On Hunt's and on Chef, you're really talking more of a Q2 and beyond investment, because those programs are just now hitting the marketplace as we speak. So, that's more of a Q2 and on function than what we saw Q1. Anything I missed there, Dave?

David Marberger

Yes. Just to add, as you see on the bridge, Andrew, we invested 1.7% of organic net sales in investment in Q1. We do expect that Q2 net level will be higher. And I made that in my comments that will impact Q2 gross margins relative to Q1; and that in the second half, we expect those levels to be lower than the first half.

Operator

The next question today comes from Ken Goldman with JP Morgan. Please go ahead.

Ken Goldman

Sean, I wanted to ask about the comment that you said, we expect terrific second half growth. I appreciate the reasons why, and you laid them out well. I just wanted to follow up a little bit on the distribution part of that. To what extent do you have locked in a lot of these TPD gains for especially the Birds Eye business that you talked about in the second half, or is some of it's still, hey, you're negotiating with your retailers for this shelf space?

Sean Connolly

Ken, we keep a new item tracker on every single new item we have that has our targeted ACV, our targeted TPDs, and then has our progress in terms of what has been accepted and what has not. So, we've got a roadmap. And by now, we have a pretty good handle on what has been accepted, we feel very good about it. That's a large part why we feel so good about the inflection in the back half of the year. It's really the combination of much, much easier comps on a lot of these brands, plus basically the polar opposite of what was happening last year at this time unfolding, where items were coming out that were particularly weak velocity items. Now, we've got our largest slate of innovation yet frankly across the board, not just Legacy Pinnacle and Birds Eye that is hitting the marketplace now through the back half of the year. So, feel very good about customer acceptances and the innovation slate in the back half.

Ken Goldman

And then, I guess, the philosophical question I would have as a follow-up is, you're many, many months into the Pinnacle deal now. You talked, when Pinnacle first started coming in a little bit below your expectations about some of the things that maybe prior management had done that you wouldn't have. In hindsight, is there anything substantial, anything meaningful that you and your team could have done differently or would have done differently? Any learnings from that that you might apply to any future deals that you do, just again, in hindsight with the benefit of 2020 vision?

Sean Connolly

Well, as we've passed through multiple times, after we closed on the deal, we did learn some things about the business that had to be addressed. And our approach is to address them head-on. And we are doing that. And in fact, you can look at the absolute numbers on Pinnacle in the quarter as an example and say, well, how could it be on track? And the short answer to that is, because it is. When we realized that we had to deal with some of these things on the Pinnacle portfolio head-on, we knew right then that we had to execute our value-over-volume playbook.

And keep in mind, value-over-volume is about cleaning up and strengthening the base. It may not be pretty optically when you're in the throes of it, particularly when you're in close proximity to the shelf sets and inventories adjust, which is what we saw in Q1. But, it is an absolutely critical step to improving velocities and establishing that stronger foundation on which we can build. And if you look at what we've done on Banquet on Healthy Choice and Marie and now even Wish-Bone, you've got to have the courage of your convictions to build brands the right way for long haul, and we do. So, we definitely had some things unfold on this business that we did not plan for. But, once you're at that point in time, it's really a question of how do you respond to it. And this is how we're responding to it. Not to mention the synergies that we are managing to extract from the combination are proving to be quite attractive.

Operator

The next question today comes from Bryan Spillane with Bank of America. Please go ahead.

Bryan Spillane

So, I guess, a question for me is just around, with a lot of this innovation hitting in the second half of the year, is it -- is the innovation on its own margin accretive, or are you supporting the margins, because you're going to be pulling in more synergies? So, I understand the dynamic with the slotting fees in the second quarter and that might sort of dilute margins initially. But, I was just trying to get an understanding of run rate wise how much -- what the impact of this innovation will have on margins over time?

Sean Connolly

Well, principally, we always aim for margin accretive innovations. Now, that is not always the case. We talked about spiralized as an example over the last several quarters where the Pinnacle organization previously opted out of spiralized, because it would be margin dilutive. That is a kind of an exception, when you have the consumer absolutely demanding an innovation and in the short term, it requires a dilutive gross margin profile, my position is you've got to get in the game. You can cede that beachhead to your competition.

So, there will be examples where in the short-term the margins could be dilutive. And certainly in the short-term, you've got some startup investments. We're putting a lot of the startup investments, as an example for -- which will help us in the back half into Q2. But in general, we are looking for margin accretive innovation. And quite frankly, we've been quite successful at that over the last several years. Dave, do you want to add to that?

David Marberger

And Bryan, if you look at Q1, I know it gets a little bumpy with us now having Pinnacle in there. But if you look at Refrigerated & Frozen, and you can see the margin improvement. And you can see that Birds Eye really helps with the overall margins of the segment. And so, with a lot of innovation in Birds Eye, obviously that's margin accretive. And in our snacks business, great margin there on innovation. It's hard because it's combined in a segment that has other businesses with it. So, a big part of our focus is looking at the margins whenever we launch new products.

Sean Connolly

Just one other point on that that's worth the folks on the line keeping in mind is, if you think about the Legacy Conagra portfolio, and even to some degree, the Legacy Pinnacle portfolio, it was heavily skewed toward the value -- or value tier, a value orientation. So, we have been working nonstop for five years to premiumize our Legacy CAG portfolio. We're certainly working now to premiumize the Pinnacle portfolio. And while the old school thinking is that when you add more COGS, your margin comes down, actually we've experienced the opposite. When you build better quality products and better quality packages, you can price for it. And when you can price for it, you can build back not only your margins, but your retailer margins, which we've done. And that's one of the things that has helped our relationships with our retailers to grow progressively stronger over the years.

Operator

Next question today comes from Robert Moskow with Credit Suisse. Please go ahead.

Robert Moskow

Hi. Thanks. I just wanted to dig a little bit deeper into the sequential progress of Pinnacle. If I'm looking at that operating margin dilution chart correctly, it said that Pinnacle was dilutive by 10 basis points. And just using that, I get to about $90 million of operating profit for the quarter, which I think is a little bit down from the prior quarter. And then, you said, sales down 9% from prior year. So, is this really in line or was the retailer inventory reductions I guess a little more than you expected? And am I doing the math right?

Sean Connolly

Well, let me take the inventory piece, Rob. And Dave can weigh in on the balance of it. Because it is very consistent with what we expected and it's very consistent with what we've experienced before. And frankly, it's something that -- it's something that we have experienced from time to time on our broader business. So, just a broader comment on this notion of shipments vis-à-vis consumption. Again, Dave add any more detail.

I want to remind you, our business historically shows shipments and consumption track pretty closely together. But, from time to time, they will diverge. And in our case, if you see that divergence, it's likely tied to one of four factors. One is value-over-volume driven reductions in retailer inventories. And this is because when SKUs get eliminated, so do the safety stocks on those items. And it usually occurs in close proximity to shelf resets. And that's what we saw in Q1 on Pinnacle. As you saw, consumption was tracking on Pinnacle very consistently with where we've had it in that 4 to 4.5 -- down 4.5% range.

The second factor is increased brand building investments with retailers that are accounted for above the line. And in Q1, we saw that on both Pinnacle and on legacy CAG. The third occurrence where you might see the divergence is when we take deliberate actions that you can't see in the scanner data. We did this in Q1 on legacy CAG because we exited some private label products that were not the margin profile we liked. And then, the fourth factor when you'd see it is declines in unmeasured channels. And we saw a bit of that in Q1 on our Duke's brand tied to the supply chain disruption we experienced in Q4 and recovering from that, but that root cause is behind us. We expect normal distribution to be in marketplace on that business in the second half.

So, we saw some divergence both in our grocery snacks business and in the Pinnacle business. It's not typical for us. But, when it happens, it's tied to those four things. And we can bridge those out. And every element of it makes sense with how we anticipate it to fold out. Importantly, we don't expect shipments to lag consumptions in the year ago period, the way they did in Q1, either on Legacy Pinnacle or our Grocery & Snacks business.

David Marberger

Yes. And just to add, Robert. When you look on the operating margin bridge, which is one of the things you're referring to, we do show that Pinnacle's 46 basis points dilutive, and that's just to demonstrate that -- and this was when we reported Pinnacle separate last year, you could see the Pinnacle gross margins are below the overall Legacy Conagra gross margin. So, by bringing that business in is to show that it's dilutive. But, what gets a little complicated now that the synergies coming in and SG&A going out, a kind of standalone Pinnacle at this point is really not relevant. We're not reporting it that way. But, that's just to show that the gross margins for Pinnacle coming in are lower than overall company average, which is what you saw at the end of last year.

Robert Moskow

So, just to follow up, Dave, this 46 basis points, does that include the benefit of the synergies or is that separate from the synergies?

David Marberger

Yes. It's a good question. It includes some benefit, the way that we actually capture a synergy and unallocated it, some of it can go to a Pinnacle item, some of it can go to Legacy CAG. Right? So, if it's in procurement and you're able to get a benefit of reducing your overall buy on a certain ingredient, it may benefit the ingredients that you use on Conagra products and Pinnacle products. Right? So, that synergy gets allocated. So, some of it’s in there, but not all of it.

Operator

The next question today comes from David Palmer with Evercore ISI. Please go ahead.

David Palmer

You mentioned that brand building will be outsized in fiscal 2Q and the impact will be greater to gross margin than in the first quarter. I guess, I'm most curious about the magnitude of that increase. And just to be clear, is it largely going to be contra revenue and gross margin hit rather than a traditional advertising and consumer marketing expense?

Sean Connolly

Well, first of all, welcome back, David. Good to have you on the line. Yes. The answer is yes to your question. This is -- the way to think about this is we've got -- both in Q2, you see some Birds Eye stuff, that's recently hit the marketplace in the back half of the year, we have a ton of stuff hitting the marketplace. We've got to tee that up to get this kind of shelving we want, the eye level placement we want. Basically, all the awareness drivers have to get in place and then the trial drivers get in place. And we're doing a lot of that as we've done consistently over the last couple years in store because we find it far more effective in spotlighting our new items than running TV commercials at 3 o'clock in the morning, as an example. So, that does hit add a peak in Q2 and it is a central piece of making sure we've got that buzz out there in advance of when we expect to see the takeaway kick in, which is in the back half of the year.

David Palmer

And then, just on frozen, the frozen business, in the quarter, and I think you touched on it that the shipments were less than consumption. And perhaps that was somewhat the reshelving that's happening rather than some trade inventory dislocation, because Nestlé shifted out of DSD into warehouse that was a little bit of a concern. So, maybe you can clarify that. And then, also, I know that when you did some of your more rapid innovation periods past, particularly when you did bowls, which were a premium offering, that was perhaps not as incremental, the shelf as you would have liked or thought as some of the retailers instead replaced some of your lower priced, older varieties. So, I'm wondering if you're making adjustments this time around to make sure you get that incremental shelf as you put out these new varieties. Thanks.

Sean Connolly

All right. So, there's a lot in there. Let me try to hit the piece there. First of all, in terms of some inventory reductions at retailers, it's really not a lot noteworthy in frozen. It was really a concept around the Legacy Pinnacle business and value-over-volume and a bit of the Grocery & Snacks business that I already talked. With respect to the shelf and the dynamics with customers right now, I would say, these are certainly very dynamic times, but our relationship with customers is very strong. And I feel very good about the progress we're making in terms of getting new items on the shelf.

Certainly creating space for new items always starts with us proactively spotlighting our own items that need to come out. That's kind of value-over-volume. And in the simplest sense, our customers want to grow and they understand that their shoppers demand modern products. And our innovation capabilities are clearly well respected with our customers as we drive growth in their priority categories of the innovation. So, they continue to embrace our innovation.

We are also working very collaboratively with many of our traditional customers though to help them navigate their exploding e-commerce business, particularly the in-store pickup piece or what some people call click and collect. And what we're doing with them there is trying to create more holding capacity within the store for top movers, think of that as high velocity items. And the reason we're doing that is to avoid out of socks, because they not only have their old foot traffic on the ground, now they've got all the people that are doing click and collect and doing pickups. So, you've got to create more holding power on those high velocity items. And that's particularly important in space constraint spaces like frozen where you would seen and we'll continue to see the actual number of TPDs coming down. But, I think, it is critically important, you don't confuse that TPD read with linear feet of shelf space being reduced, because that is not happening. In frozen single-serve meals as an example, we actually see real estate expanding. TPDs are coming down intentionally collaboratively with us and our customers. We have to have more holding power on our high velocity stuff because that leads to better sales and those are the things that really turn. But, it's a more limited assortment with more facings for big brands that have high velocities and those are brands like ours.

Operator

The next question today comes from Chris Growe with Stifel. Please go ahead.

Chris Growe

I just had a question for you, if I could, first on this -- the drag on volume from Foodservice and International. It looks like it was about half of the volume decline, if I'm calculating that properly. I don't know if you quantify that exactly, but that's what I got came out. Does the remainder of that drag then on volume -- it looks like it mostly came from the grocery division. Does that -- is that what you expect to improve in the second quarter as you think about some of those investments you're making?

Sean Connolly

Yes. The grocery piece, as I said in our prepared remarks, the decline in grocery was planned; it was highly focused on the two brands we discussed. And that is where -- we planned it that way because we didn't put the action plan in place until the very end of the quarter which really impacts Q2. And that's pretty much how it's played out. So, while it is early days on those action plans, you could see some of the numbers that we showed you today. We do like the traction we see. And those typically are very responsive brands. They are number one market share brands. When we're fully competitive, we tend to move a lot of volume. So, that's what we expect to improve as we move through Q2.

Chris Growe

And then, just to be clear on that Foodservice and International drag, does that get better in Q2 or is that more just better than -- does that continue in Q2 and better in the second half?

David Marberger

Yes, Chris. So, the biggest driver in the first quarter was the timing of sales, both in India and Puerto Rico. So, assistance programs in Puerto Rico were delayed in the quarter and that had a significant impact on our export shipments in our sales. And shipment patterns changed certain sales in India which caused timing shifts between quarters as well. So, we expect these businesses to remain on track to plan for the full year. That's just a timing push for international.

Chris Growe

So, a push into 2Q or a push into second half?

David Marberger

Year to go.

Chris Growe

Okay, got it. And a just one quick one, if I could, on the innovation costs. Are those -- is that reflected in your retailer investment category you still do in the sales breakdown? Is that what we should see some of these incremental costs coming through in Q2 for the new products?

David Marberger

Yes. So, when you talk about innovation, if you are talking about the cost to get to market and distribution, yes, you will see that above the line. There is obviously all the developmental costs of innovation, R&D and manufacturing resources and test runs and all that. And all of that hits in SG&A or cost of goods sold. But the actual distribution commercialization push with the customer is above the line.

Chris Growe

Slotting fees for example as well would be in there. Right?

David Marberger

Right.

Operator

Our next question today comes from Steve Strycula with UBS. Please go ahead.

Steve Strycula

So, the question, Sean, one of the feedbacks I've gotten -- received this morning is that there's a little bit of a disconnect between I guess where you guys had planned internally for sales were seem to be online as you say, and externally just having it down 1.7%. How do we think about the trajectory of the business for Q2 through the balance of the year for some of your investors who want to kind of be more aligned and familiar with what you are planning internally for how that business rebounds? Clearly, you're emphasizing the back half. But, do we see directional progress in Q2 to get halfway there, I mean, like closer to flat territory for your organic sales? Just help us understand kind of that shipment aligning versus consumption as we move through the back half.

Sean Connolly

Yes. Steve, one of the reasons why I think consensus was a little farther off with our internal plans because we don't guide to the quarter, and we're not going to guide to the quarter, but we want to be helpful in getting the shape of the curve right. And I think the message today is quarter one is on track. The back half we're counting on being big in terms of growth. And Q2 is really a quarter that sets up the back half in terms of investment, which is why Dave made the comments on gross margin that we've got, because we've got some contra gross margin and contra net sales investments hitting in Q2. So, that suggests that the real inflection that we're going to see is really coming in the back half of the year. Dave, do you want to...

David Marberger

Yes. Just to add, and here again, we don't guide quarterly. But to give a little bit more context, you should see sequential improvement in organic net sales from Q1 to Q2, and then improvement from Q2 to the second half to get to our full year outlook of 1% to 1.5%.

Steve Strycula

Okay. Thanks. That's helpful. And then, Sean, for clarification, I think going back to Andrew Lazar's question and I think maybe Palmer's question, but your frozen piece of the business for Legacy Conagra, it seems like you have confidence that that is in intact. And would you say that because we see -- we're paying attention to the distribution losses and as it’s tracked in Nielsen, you're saying that is kind of a -- that's a little bit misleading? Could you kind of like run through that one more time? And Dave, can you confirm on the $40 million synergies, whether that's a net or gross number? Thanks.

Sean Connolly

Yes. So, let me try to simplify frozen. There's a lot going on right now in frozen. Dynamic times, we've got shelf sets being kind of reshuffled at major customers. Big part of that is to accommodate this whole higher holding capacity on high velocity items to support the click and collect business, which by the way, is not just a customer priority, it's our priority. Our sales look better when we've got more holding power on high velocity items. So, a lot of dynamics going on.

Within that, in space constrained spaces, you may and likely will see TPDs coming down. And I think this is important because sometimes TPDs are assumed as a proxy of real estate, and it is not an accurate proxy of real estate, where actually, as I pointed out, single-serve meals is growing in real estate, but it's -- we're getting more facings on high velocity items. So, a lot of this is happening right now as we speak. And not only I'm very pleased with leading up to those shelf planogram change with how we perform, because if you look at our data, our sales are the best in the industry, our share of shelf is the best in the industry, and no one else is even remotely close. So, that's good. And then, as we see the new planograms unfold, I continue -- even though we've had some near-term out-of-stocks in the shelf that is getting reset, I continue to see positive things in terms of our overall market shares and our overall share of shelf within the new shelf sets. So, nothing but -- it's dynamic times, but nothing has changed in terms of the consumer pull and the appeal of our brands to consumers and customers alike.

David Marberger

And Steve, to your second question, it is a net number.

Operator

The last question today comes from Jason English with Goldman Sachs. Please go ahead.

Jason English

I guess, I'll jump off of the net synergy number. Congratulations by the way on net synergy realization, impressive uptick from the run rate you guys finished last year. Is the full year number of 130 still the right way to think about it,, given the pace you're running at right out of the gates here? And if you could remind me, is that 130 -- is that a cumulative number for the full year, or is that incremental over and above the $31 million you realized in fiscal ‘19?

David Marberger

Yes, Jason. So, let me -- let me take it from the top. We're obviously very pleased with the progress we're making with synergies. We're focused on it. We track it closely. In the first quarter, we delivered $40 million in synergies. About two-thirds of that was SG&A, which is what we expected. We're still estimating the total synergies of 285 through fiscal ‘22. One quarter under our belt still early in the year. So, we’ll provide an update at the end of the second quarter on exactly where we see synergies coming in for the full year. We had said previously that we would be at 55% of total synergies by the end of fiscal ‘20. We're going to update that at the end of the second quarter as we continue to see our progress. In terms of cost to achieve, just to hit that, that's $87 million program to-date, we're still on track with the $320 million through fiscal ‘22.

Jason English

Awesome, I appreciate the incremental detail there. And then, one more, I guess sort of a multilayer question. First, the step-up in trade spend, I totally understand how that's going to our retailer market. I totally understand how that contra revenue is going to weigh on price realization in margins next quarter. But, it sounds like we should be expecting a nice little volume response on grocery. And then, we've got these international issues, which sound like they were kind of isolated. Those go away. And I imagine a lot of your activation on frozen, while you're not going to see the consumption ramp for some time, it sounds like it's been accompanied by the distribution build. So, we should at least still expect some degree of pipeline fill. So as I stack those up and I contemplate the shape of how year progresses, while organic may not really accelerate in earnest for the back half, is it fair to say we may actually see some real evidence of the uptick coming through in earnest on the volume line in the next quarter?

Sean Connolly

Well, on the volume line, you are going to see volume diverge obviously from sales, because the contra net sales items are really about setting it up. So, there will be some new items that are going to build momentum in the second quarter volumetrically. The net sales piece of it you're going to see inflect more in the back half of the year.

Jason English

Got it. Yes. So, it sounds like we will see some evidence at least building in volume, a little earlier than the back half, which would obviously be encouraging.

David Marberger

Yes. With organic, as I said, Q2, we expect to be better than Q1; and then, the second half to be better than Q2. So, that's sales but obviously with the higher investment in there. You can do the math on volume.

Sean Connolly

And part of that Jason is, the gap between shipments and consumption on Pinnacle in Q1 is -- again, that is a typical thing in close proximity to the shelf resets. Those are basically unfolding now. So, on a year-to-go basis, we don't expect to see that kind of lag. And that will begin here as we go into Q2. And that's the volume piece of it.

Jason English

Got it. So, there could be some bleed over that issue into Q2, which we should contemplate then, if it's ongoing now, fair to say?

Sean Connolly

I wouldn't say it's a straight line for the balance of the year. But, over the course of the year-to-go period, we don't expect there to be a lag between shipments and consumption.

Operator

This concludes our question-and-answer session. I would like to turn the conference back over to Brian Kearney for any closing remarks.

Brian Kearney

Great. Thank you. So, as a reminder, this call has been recorded and will be archived on the web as detailed in our press release. The IR team is available for any follow-up discussions that anyone may have. Thank you for your interest in Conagra Brands.

Operator

The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.