Sysco Corporation (SYY) CEO Tom Bené on Q1 2020 Results - Earnings Call Transcript

Nov. 4, 2019 3:26 PM ET1 comment
by: SA Transcripts

FQ1: 11-04-19 Earnings Summary

Press Release *10-Q* *Slides*

EPS of $0.98 beats by $0.01 | Revenue of $15.3B (0.58% Y/Y) misses by $-227.48M

Earning Call Audio

Subscribers Only

0:00:00 -1:00:12

Sysco Corporation (NYSE:SYY) Q1 2020 Results Conference Call November 4, 2019 10:00 AM ET

Company Participants

Neil Russell - Vice President of Corporate Affairs

Tom Bené - Chairman, President and Chief Executive Officer

Joel Grade - Chief Financial Officer

Conference Call Participants

Edward Kelly - Wells Fargo

Christopher Mandeville - Jefferies

John Heinbockel - Guggenheim

Judah Frommer - Credit Suisse

Marisa Sullivan - Bank of America

Jeffrey Bernstein - Barclays Capital

Andrew Wolf - Loop Capital Markets

Kelly Bania - BMO Capital Markets

John Ivankoe - JPMorgan

Bob Summers - Buckingham Research

Operator

Good morning. And welcome to Sysco's First Quarter Fiscal 2020 Conference Call. As a reminder, today's call is being recorded. We will begin with opening remarks and introductions.

I would like to turn the call over to Neil Russell, Vice President of Corporate Affairs. Please go ahead.

Neil Russell

Good morning, everyone. And welcome to Sysco's first quarter fiscal 2020 earnings call. Joining me in Houston today are Tom Bené, our Chairman, President and Chief Executive Officer and Joel Grade, our Chief Financial Officer.

Before we begin, please note that statements made during this presentation that states the company's or management's intentions, beliefs, expectations or predictions of the future are forward-looking statements within the meaning of the Private Securities Litigation Reform Act and actual results could differ in a material manner.

Additional information about factors that could cause the results to differ from those in the forward-looking statements is contained in the company's SEC filings. This includes, but is not limited to, risk factors contained in our Annual Report on Form 10-K for the year ended June 29, 2019, subsequent SEC filings, and in the news release issued earlier this morning. A copy of these materials can be found in the Investors section at sysco.com or via Sysco's IR app.

Non-GAAP financial measures are included in our comments today and in our presentation slides. The reconciliation of these non-GAAP measures to the corresponding GAAP measures are included at the end of the presentation slides and can also be found in the Investors section of our Web site. To ensure that we have sufficient time to answer all questions, we'd like to ask each participant to limit their time today to one question and one follow-up.

At this time, I'd like to turn the call over to our Chairman, President and Chief Executive Officer, Tom Bené.

Tom Bené

Thanks, Neil, and good morning, everyone. Thank you for joining us. This morning, we announced financial results for the first quarter of fiscal year 2020, which reflect continued momentum in transforming our business and improved year-over-year performance. Our overall results were largely in line with our expectations.

From a top line perspective, we generated sales of $15.3 billion, a 0.6% increase compared to the same period last year. As we discussed during Q4 fiscal 2019, we saw top line softness and difficult comparatives during that quarter, which we said would also carry into the first quarter of fiscal 2020. We did, in fact, see that continued softness at the beginning of the quarter, but as expected, we saw sequential improvement throughout the quarter and therefore, feel confident about the future trajectory based on the exit rate of the quarter.

There were several things that contributed to our volume and sales growth rate for the quarter, including the continued growth of our local customers at a faster rate than our national customers, in part driven by the transition of certain large national customers, both in U.S. Broadline and SYGMA during the past year. Secondly, the divestiture of Iowa Premium, our beef processing facility, that was sold in the fourth quarter of fiscal 2019. This divestiture had an impact in the quarter of $114 million, and the negative impact of foreign exchange rates, which amounted to an additional $100 million for the quarter.

Gross profit for the quarter grew 1.4% to $2.9 billion dollars. And gross margin expanded 15 basis points, driven by continued shift in our customer mix as we grew local cases at a faster pace than total case growth. And we continued growth and penetration of our Sysco brand portfolio across the various business units.

Turning to cost. Adjusted operating expenses decreased 0.5% to $2.2 billion, driven by strong expense management during the quarter, including greater operational efficiencies and benefits from our transformation initiatives, such as the regionalization work in Canada and our finance transformation. As a result, for total Sysco, we delivered solid adjusted operating income growth of 7.3%, which led to adjusted earnings per share growth of 8.6%.

Looking at the broader economic and industry trends in the U.S., GDP growth was 1.9% during the third quarter, and unemployment remains at an all time low. Consumer spending, the main engine of growth, rose a healthy 2.9% but it was down from 4.6% in the spring, all signs that the economy is doing well despite some broader global concerns.

While some other economic indicators have recently been softer than expected, we haven't seen a meaningful impact to restaurant industry trends and therefore, continue to feel good about what we're seeing in the food away from home market. During the quarter, according to Black Box Intelligence, restaurant same store sales rose slightly, driven by average guest check increases. Although, traffic in the food service industry continues to be mixed, it appears that market conditions are modestly favorable for food service operators in the United States.

Turning to international markets. Traffic and sales in the UK and Ireland continue to be soft as uncertainties around Brexit affect food service operators, as well as other economic activity. However, these trends are relatively stable compared to conditions in the prior quarter. In Canada, GDP and consumer spending are stable and unemployment continues to decline, which is reflected in positive broader restaurant industry performance. In France, GDP growth is expected to continue. Household spending has picked up, and employment is trending down, boosted by labor market reforms.

I would like to now transition to our first quarter results by business segment, beginning with U.S. Foodservice operations. We were pleased with our top-line results and strong expense management in the U.S. Foodservice operations segment in Q1. Specifically, sales for the first quarter were $10.7 billion, an increase of 2.5%; gross profit grew 2.6%; adjusted operating expenses grew only 0.4%; and adjusted operating income increased 6.1%. Local case volume was solid within U.S. Broadline operations, growing 1.5% and has now grown for 22 consecutive quarters.

As previously mentioned, this performance reflects solid growth at local restaurant customers, especially as we cycled one of our largest growth quarters last year, which was partially offset by the loss of some less profitable traditional bid-type business, such as local schools. Total case volume within U.S. Broadline operations grew 0.5%, reflecting our ongoing disciplined approach in managing our national account business. We expect to continue to see the impact of certain customer transitions in U.S. Foodservice operations into the second quarter as well.

Gross profit grew by 2.6%, driven by higher inflation, the positive mix of local cases to total cases, continued growth in Sysco brand, up 36 basis points, and continued category management efforts. Food cost inflation was 2.9% in U.S. Broadline, driven primarily by the meat, produce, dairy and poultry categories.

From an expense perspective, adjusted operating expense for the quarter grew only 0.4%, driven by strong expense management throughout the business, including the impact of some of the transformational initiatives mentioned earlier, which drove down costs during the quarter. This was partially offset by higher labor and operational costs. Similar to the larger discussion we had in the second half of fiscal 2019, our labor costs were slightly higher due to our decision to retain driver and warehouse personnel in a tight labor market. And while we do see some signs of improvement in the overall labor market, we will continue to evaluate this practice is the right one for our business over the next couple of quarters.

Moving to International Foodservice operations, we had mixed results for the quarter. Our international results were impacted by changes in foreign exchange, and Joel will provide more details on that to you in just a few minutes. However, on a constant currency basis, sales increased 3%, gross profit increased 2.1%, adjusted operating expenses increased 1.3% and adjusted operating income increased 6.2%.

Canada and Latin America had improved performance for the quarter, driven by a combination of positive business environments driving the top line with positive synergies coming from programs, such as the regionalization effort in Canada. In Europe, performance in our UK business remained stable, although, uncertainties around Brexit certainly remained in the market. However, challenges with our operational and supply chain integration in France continue to negatively impact our overall performance there, and most likely continue through the remainder of our fiscal year.

The relatively soft gross profit performance was offset somewhat by solid expense management throughout our international segment, as we continue to see benefits from the various integrations and other expense management initiatives [Technical Difficulty] improved operating income growth for the quarter.

Moving on the SYGMA, as mentioned previously, we remain disciplined and focused on improving overall profitability of our portfolio of customers in this segment, which included gross margin expansion of 73 basis points as we saw total gross profit reduce by roughly 3%. In addition, strong expense management and the closure of a distribution location drove adjusted operating expenses down 8.8% versus the same period last year, resulting in significantly improved operating performance. We continue to feel very good about the progress we're making within this segment, and look forward to continuing to improve our operating performance throughout the year.

In summary, we feel good about the trajectory of our business for fiscal 2020. We continue to increase profitability through growth at local customers, our disciplined approach in managing our national customer portfolio, managing our expenses and making progress in the various initiatives we have discussed to transform our business.

As we look ahead, we are excited to celebrate our 50th anniversary this fiscal year. For half century, our company has been at the forefront of the food service distribution industry, passionate about our customers, dedicated to service and committed to being socially responsible. Our team is enthusiastic about the changes we're making in our business model to ensure we remain the market leader, and fulfill our vision to be our customers' most valued and trusted business partner for the next 50 years.

And finally, I'd like to thank our dedicated associates across the company for all their efforts to make Sysco the distributor of choice for so many customers. They are truly all in.

Now, I'll turn the call over to Joel Grade, our Chief Financial Officer.

Joel Grade

Thank you, Tom. Good morning, everyone. As Tom mentioned, sales for the first quarter increased 0.6% despite a number of factors, including a difficult comparison versus the same period last year, our disciplined approach in managing SYGMA and national accounts within our U.S. Foodservice segment, the divestiture of Iowa Premium and the negative impact of foreign exchange rates in our International segment.

Local case volume within U.S. Broadline operations grew 1.5% for the first quarter, of which 1.4% was organic. While total case volume within the US Broadline operations grew 0.5%, of which 0.4% was organic. Gross profit increased 1.4% versus the same period last year and gross margin increased 15 basis points. We saw growth in our sales of Sysco brand products, which increased 20 basis points to 47.7% of local U.S. cases and 36 basis points to 38.8% of total U.S. cases in the first quarter.

We are pleased with our strong expense management for the quarter. Our transformation initiatives continue to generate benefits to the business as adjusted operating expenses decreased 0.5% compared to the same period last year, and slightly ahead of our expectations. As a result, the gap between gross profit dollar growth and adjusted operating expense growth was 190 basis points and adjusted operating income grew 7.3% compared to the same period last year.

It is also important to note that our adjusted operating expenses grew only 0.4% within the U.S. Foodservice segment despite a challenging operating environment. Although, we have strong expense reductions throughout the quarter, we continue to invest in areas of our business that will help facilitate future growth.

For example, our technology spend was higher versus the same period last year as we continue to make advancements in areas that help us streamline workflow, while better supporting our customers and helping to support better growth. During the first quarter in the U.S. Foodservice segment, we saw 220 basis points gap between gross profit dollar growth and adjusted operating expense growth, which translated into strong adjusted operating leverage for the quarter.

As Tom mentioned earlier, our results in the International segment were impacted by foreign exchange rates. In that segment, sales decreased 0.3% on a reported basis and increased 3% on a constant currency basis. Gross profit decreased 1.7% on a reported basis and increased 2.1% on a constant currency basis. Adjusted operating expenses decreased 2.7% on a reported basis and increased 1.3% on a constant currency basis. And adjusted operating income increased 3.8% on a reported basis, but increased 6.2% on a constant currency basis.

As it relates to taxes, our effective tax rate in the first quarter was 22% compared to 20% in the prior year period. While higher than per year, this rate was lower than our guidance of 24%, primarily due to tax benefits from share based compensation. Our adjusted earnings per share grew 8.6% to $0.98 per share, which is an increase of $0.08 compared to the same period last year.

Cash flow from operations for the period was $172 million for the quarter, which was $100 million lower compared to the same period last year. Free cash flow was $1 million, which was $170 million lower compared to the same period last year. Net capital expenditures totaled $171 million for the first quarter of fiscal 2020, which was $70 million higher compared to the prior year period. The decline in free cash flow was due in part to an increase in working capital in the first quarter this year, driven primarily by an increase in receivables. Additionally, we saw planned higher capital spending due to the timing of investments in the prior year period. However, we continue to expect strong cash flow for the full fiscal year 2020.

In July of 2019, we adopted the new lease accounting standard that changes the way we recognize operating leases by including the related right of use assets and lease liabilities on our consolidated balance sheet as of fiscal 2020.The changes are also reflected in the consolidated results of operations and consolidated statement of cash flows. However, there's only minimal net impact. We remain focused on delivering long term results for our shareholders through a strong and consistent approach to our capital allocation priorities, which are as follows; investing in the business, consistently growing our dividend, participating in M&A and maintaining a balanced approach to share buybacks and paying down debt.

We typically review our dividend growth rate each November, and expect to once again increase our dividend later this month. We also have previously committed to a modestly higher rate of share repurchases than in the prior year.

In summary, we had a solid first quarter that reflects the sustained momentum of our work to transform our business. as fundamentals of the industry and our business remained strong, as we continued to deliver steady local case growth, good gross profit dollar growth and strong expense management. These results give us confidence that we remain on the right path to enhancing the customer experience and delivering a high level of execution in all areas of our business, as we continue our progress toward achieving our three year plan objectives.

Operator, we're now ready for Q&A.

Question-and-Answer Session

Operator

Thank you [Operator Instructions]. And our first question comes from Edward Kelly from Wells Fargo. Your line is open.

Edward Kelly

Good morning. And nice quarter on slower overall case growth, and that's really kind of what I want to ask you about, Tom and Joel. I was just hoping could you provide just a little bit more detail on your outlook for the case growth in U.S. business? And you've talked about an improved cadence throughout the quarter. Can you give us any color on the exit rate? You mentioned that you still expect some impact from customer losses in the second quarter. I'm kind of curious as to how we should be thinking about case growth here. And then just overall, as we think about the momentum of the business, what's an acceptable level case growth that you're thinking about as you progress through the year? And other than easing comparisons, can you maybe help us out with what helps to drive that?

Tom Bené

So specifically to case growth, as we talked about the quarter, nothing is too specific. But we did see, as we talked about when we came out of Q4 and we all know we had some softer numbers there, driven by both the lapping of a good quarter of the prior year, but also just some general softness in certain parts of the business. Specifically, we talked about some of the national accounts and these more the micro chains.

What we're seeing, as we came out of the first quarter, was the local independent customers maintaining solid performance and continuing to grow. And so we feel good about, as we come out of that, that we're -- if you think about, we finished this quarter in this 1.5% local case growth, we feel like that is the lower end of what you should expect from us going forward. And we feel like that we'll be more in the range of what we have historically talked about with you guys over time.

And so that doesn't mean every quarter is going to be the same. But this idea that you should see us back in the 2% to 2.5% range on local cases is where I'd tell you that you should think about. As it relates to the comment I made about some of the national account and some of the account transitions continuing, it's just really the timing of we know some fairly large customers and transition in the back half of last year, fiscal year. And we have that overlap still ahead of us. We had it in the first quarter that’s why you saw this softening in the total cases, and we'll have that again in Q2. So I think that's the headline there.

When you talk about what's an acceptable level. I think we continue to talk about the fact that we want to be gaining share, certainly, as it relates to the independent market. And we see that, even at the current rates, we're clearly close to being at parity with what the market is doing. And if we're at the levels I just talked about, we will continue to be gaining share, which is where we wanted to be throughout, really all of the last couple of years, and where we continue to be focused.

And so I think you should just think about that level being we want to be in a share growth in a shared gaining scenario. As you noticed from these numbers, very little case volume was attributed to any M&A activity. And as we go forward, you'll see a little bit more of that showing up in as we've had some recent acquisitions. So hopefully, that gives you a sense of what we're thinking about and where we're seeing things now and for the foreseeable future.

Edward Kelly

And just a quick follow up so on the competitive environment. Has anything changed really on that front? You have, over the last couple quarters, highlighted a little bit more competitive intensity in the micro chain. So I'm just curious as to what you're seeing there?

Tom Bené

Yes, I don't think we've seen anything change dramatically from what we had talked about. And if you recall, I had made a comment at the end of last quarter about, maybe us not being as competitive in some areas. And so -- and the point we're trying to make then and that we'll just reinforce today is that, that was really on us and we have kind of re-stepped up our efforts to make sure that we're not losing business, because of somehow we weren't being competitive. And so I'd say it continues to be obviously competitive out there, but we're not seeing any increased level of activity from what we talked about in the past.

Operator

Thank you. Our next question comes from Christopher Mandeville from Jefferies. Your line is open.

Unidentified Analyst

This is Blake on for Chris. Just wondering on the upcoming quarter, can you talk about any other details on timing of case growth in terms of year-over-year comparisons we should be aware of, or holiday timing, just anything like that.

Tom Bené

Blake, not really, I mean, there's nothing major there. As we called out that some of this national account business that we're cycling still will still be there in Q2. So I think that you should expect that based on the comments we made. But nothing else that's unique or different other than what I just mentioned.

Unidentified Analyst

And then my follow up is on, some of the capital spending. I know you mentioned free cash flow impact from working capital and in CapEx. On the CapExside, I think you mentioned some project timing. Can you just talk a little bit more about what was going on with that investment? And then maybe, can you give us the cadence of the free cash flow throughout the year? Any commentary about that would be helpful.

Tom Bené

So a couple things on that, specifically, on the CapEx piece. We had a little bit of an anomaly in our last year cash flow, because in Q1 of our last fiscal year, we had just come off of Q4 of the previous fiscal year, where we had actually accelerated some CapEx as related as the U.S. tax reform. So the tax reform has given us an opportunity to accelerate some CapEx at that quarter, particularly in the fleet.

So we actually had, what I'd consider, an unusually low first quarter of last year where it came to CapEx. So the year-over-year comparison, what I would -- I would characterize that as a bit of more of a normalized spend as we had it this year relative where we would normally be purchasing more fleet, particularly in that first quarter last year.

So that's where there's a little bit of a timing element. And again, it really relates to the Q4 and the U.S. tax reform actually in the year prior to that. We also, if you remember, we typically have a fair bit of just if you think about the overall kind of cadence and flow of our cash flow, we typically have a lower -- some seasonality related to our first quarter. The number we actually had last year, I would tell you, is actually somewhat of an anomaly relative to how we've actually looked over the last few years on our Q1.

And so I, you know, while somewhat, obviously, there's a bit of this timing and capital spend and again there's a bit of a word, there’s some working capital impact, we certainly look at as somewhat short term. This is not necessarily an unusual sequencing of our cash flow as that relates to our numbers historically, even though last year had a better number.

So I would just tell you, when you take a look at some of the way our cash flow has gone outside of over the last few years, I think you should get a pretty good sense of what that will look like here. And then obviously, it certainly ramps up a lot as we head into the latter part of our fiscal year. But again, certainly, feel confident of our ability to have a strong -- continuing strong cash flow here, despite some of the time issue here.

Operator

Thank you. Our next question comes from John Heinbockel from Guggenheim Securities. Your line is open.

John Heinbockel

So Tom, when you think about share gains, maybe parse that out between new accounts that you're taking over as opposed to existing account market share. So I think existing account market share is probably pretty static? Or is that not right? And then what are you seeing with regard to drop size? I assume that's getting a little bit larger.

Tom Bené

As we think about share, I mean, you're right. It comes from two different places. It comes from new business and obviously, maintaining our current business, so holding on and retaining our current customers and driving penetration, or more cases through them. I'd say it comes from both places. And I wouldn't look at it and assume that the new business is an opportunity. Given our relative share in the market, there's plenty of new business opportunities for us. And for us, it will define a new business as we haven't done business with someone for roughly a year, no business, then that would be new business. So there are customers in this business that cycle on a pretty regular basis. So I wouldn't at all think that new business isn’t still a big part of our opportunity to grow.

And then as it relates to penetration, I'd say we're very focused on penetration, because it's the more you can sell into any existing customer, that's obviously the most efficient case that we can ever get. And so we're very focused on that as well. And we've got some tools that are in place to help identify for our selling organization where some opportunities might exist in those customers. There might be some products that they either have bought from us in the past they may not be buying now, or based on the type of customer they are that they could be buying from us in the future.

So I'd say it's really pretty balanced between the two. And we always look at and talk about that mix of new retaining our current business and further penetrating our customers. And to the point, as we do better job on penetration that generally does help our drop size go up. So I wouldn't say there has been a significant increase in our drop size but overall, our drop size -- we're very comfortable with where our drop sizes are, and are always focused on trying to improve that as we improve our overall penetration.

John Heinbockel

And then maybe for Joel, the corporate expense adjusted, when I take out transformation, looked a little high. I think it grew 4%. Is that -- what drove that, and is that the new run rate, as we think about the rest of the year? Are you up in that 3% to 4% range, or $235 million to $240 million a quarter? Is that a run rate?

Joel Grade

Well, I guess, I would characterize that, John, and a couple of things. I mean, again as we think about -- again, where some of the transformation work is happening that some of those results in some further investments in our corporate spend that actually then, in some cases, coming out of our field organization. So I think some of what you're seeing there is a bit of a geography shift. Obviously, the net effect of which is actually a overall positive, when we look at our SG&A.

So I think, again, probably that's the way I would characterize the majority of that. So I think from that perspective, that's probably a reasonable way to view that. But again, I would just make sure we take a -- think about it more holistically in the sense of how we think about our overall G&A spend and again, we've made some good progress there, when you take that as a whole.

Tom Bené

And John, I might just add a point that Joel made in his earlier comments around technology. So like a technology investment, it's going to show up in that corporate expense line. But there are other offsets as you mentioned some of the transformative work that we're doing. So we're going to invest where we need to. And area like technology continues to be a big focus for us, so just to give you little more context behind it.

Operator

Thank you. Our next question comes from Judah Frommer from Credit Suisse. Your line is open.

Judah Frommer

One of the areas that was more impressive to us was certainly the gap in gross profit dollars and OpEx in the U.S. business. Can you talk a little bit about balancing the pullback on OpEx, and making sure that you're finding the business in the right way to grow the top-line and margins going forward, and the opportunity to further reduce OpEx as you move into the back half of this year or next year?

Tom Bené

I'll take a start at this, and I'll let Joel chime in. Judah thanks for the question. I think, look, the gap is important. We've talked about it a lot. And it continues to be something we focus on. Because when, if we're in a quarter where the volume may not be exactly where we all like it to be, we are very conscious of making sure that our expenses fit and flow accordingly. Having said that, I would say that, as we just talked about with technology as a great example, we're going to continue to make investments in the things that are going to drive and support this business. And you should absolutely expect that from us.

The types of things that we're getting the expense leverage on are the things we've been talking about. We've had some administrative costs focus areas here last year that we're still getting some benefit from. We've had this smart spending initiative, which is around just making sure that we're removing some non-value added expenses in parts of our business where possible. We talked about the regionalisation effort in Canada, and that's had some impact. And then we've had things like the finance transformation that's been a journey here, but we're still kind of benefiting from that work that's going on.

So I would say think about it as, we're going to continue to stay focused on cost, and we do believe there are additional opportunities there. But those areas of opportunity are not the areas that would, in any way, reduce or slow down our focus on both transforming the business and accelerating our growth and driving the share gains that we've been talking. Joel, if there's anything you want to add?

Joel Grade

I think it's well said. I think the only maybe small point I'd touch on part of your question in terms of what's the -- is there more to come on some of that kind of stuff. And I think the answer to that is that, in the context of what Tom talked about here, in terms of taking some of those things that are more, again, non-value added or transformative, or however you want to say it, there's certainly further run rate on some of that stuff. Again, we -- you know, obviously, we started receiving some of the benefits to that, a lot of that in the second half of last year. But obviously, we remain very focused on continuing to find additional opportunities.

And so that's something we certainly will continue to pursue, and you should expect to have some continued benefits of that over the course of the year. But again, just to reinforce Tom's point, none of those things are the things that are going to somehow get in the way of us investing for growth. And so that's a critical piece of that message I just -- certainly, we just can't repeat enough.

Judah Frommer

And just to follow-up on that. Historically, M&A is an important piece of both top line growth and I would say also, driving margin as you're able to strip costs that have acquired businesses. With what you've seen out of the regulatory bodies and kind of review of M&A over the last couple of years, largely on the larger size. But how does that affect your process going forward in terms of assessing deals and deal flow?

A - Tom Bené

Well, I think one of the points you made, again, our historical M&A has been pretty strongly focused on kind of the smaller fold-in tuck-in type deals. And so I think -- and that certainly continues to be our focus. Obviously, as we talked about from time-to-time, we certainly have our eyes open for larger strategic opportunities. But certainly, the vast majority of the work that we do is within that smaller fold-in tuck-in space.

So I can't say truthfully that that's had that much significant impact on our perspectives on that. Obviously, we've certainly paid attention to what's going on there. But I think, in general, again, the J. Kings deal we announced in the last quarter and just yet another example of one of those opportunities that we have that certainly fits really nicely into our existing portfolio. And so, I would just say, Judah, generally speaking, we feel good about our M&A pipeline. We feel good about the opportunities ahead of us. And I can't say a lot of that, even though we certainly took and to take a note of it, has been a real significant impact on how we think about overall M&A pipeline.

Operator

Thank you. Our next question comes from Marisa Sullivan from Bank of America Merrill Lynch. Your line is open.

Marisa Sullivan

I just wanted to touch on gross margin, and see if you could maybe quantify what the impact of inflation was on the gross margin improvement, and then what the outlook for inflation would be for the rest of the year, and then as we think about modeling gross margin? Any other puts and takes just to keep in mind in 2Q and the rest of the year? Thanks.

Joel Grade

Sure Marisa. This is Joel, I'll take that one. I think the -- in terms of quantifying the specific impact of inflation, I don't know that we'll do that. But I think the -- I think maybe the takeaway is, again, we've had -- again, we always think about this sort of 2% to 3% range is as sort of an optimal range for our industry, where we have the ability to pass those costs along and generally speaking, our customers to have the ability to pass those costs along to their customers over the longer term.

And so I think we find ourselves in a pretty good place there. Again, it obviously is always driven, depending somewhat on the categories that are inflating and certainly nothing, again, that we see as something that's either particularly problematic or an issue for us at this point. So I think my view on this would be that we have a modest level of inflation than we expect to over the next few quarters. And -- but again, nothing really to call out other than the fact that we certainly like the place we’re in from an inflationary perspective.

Tom Bené

And Marisa, I think you asked about kind of going forward what do we see? I think what I'd just say is, as we've talked about remaining competitive in the competitive environment. I don't think you should be modeling big gross margin increases. I don't think, on the other hand, you need to be hitting self on those numbers either. But I think we feel like, and we've talked about this a few times in the last couple of quarters, we feel pretty good about where we are from a gross margin perspective you know where we sit, relative to our peer group. And so I think we feel comfortable and confident where we are right now, but probably at the high end of where we can -- you should think about us going forward.

Marisa Sullivan

If I can just quickly follow up with just another kind of modeling question, on SYGMA. Should we think about the 1Q sales performance as -- is indicative of what you'd expect going forward, given some of the business rationalization. And if so, when do you start to cycle that?

Tom Bené

Similarly, I think Q1 was probably a little more aggressive than we saw in Q4. But as we talked about last year -- in the last year, we are in fact cycling some, some fairly large customer transitions there. So I would say for the next couple of quarters, you ought to think about similar numbers. And there is a balance of transition customers and also performance within existing customers. As you probably know, on the SYGMA side, not in every case, but when we have a customer we have majority of their business in geography. And so their relative performance will in fact affect our performance there. But the bigger numbers you're seeing are driven by the transitions we've been talking about.

Operator

Thank you. Our next question comes from Jeffrey Bernstein from Barclays. Your line is open.

Jeffrey Bernstein

Two questions, one on the topic of chain versus independents. And you mentioned the ongoing transition of presumably some of the chain accounts. So I'm just wondering how you would characterize maybe the health of each of the sub-segments being chain and independent. And importantly, maybe some changes in sequential trends for either in terms of top line performance, again recognizing that you're pruning some of the chain larger business. But just how you think about change in independents in terms of their performance of late?

Tom Bené

So as we mentioned earlier to some of the comments and you guys have access to the same kind of information. I think in general, the numbers you're seeing for us, have more to do with transitions than softness within certain customer types. I think we continue to feel good about the Independent growth potential out there, whether it's existing customers or our opportunity to gain new business as we were talking earlier. I think as it relates to some of the larger national type customers we have there are segments of the market that are growing faster than others.

Think about QSR is doing well, you see some of the casual dine maybe having a little harder time, but I think generally speaking, we feel like the environment is pretty good for the restaurant operators. And so I think we would say that the numbers you may see us talk about or reflected here will be more about decisions we made, or customers have made in doing business with Sysco. So right now, I'd say we feel pretty good about that environment, in that market.

Jeffrey Bernstein

And then just following up on the M&A discussion, I know you've often quoted that there's tons of room for growth for you guys, with only a 16% share in the US. And I think you mentioned you expected it to be a modest uptick for you guys, but still not huge M&A numbers expected. With that said the comment around the regulators in terms of seemingly being increasingly involved and scrutinizing. I'm just wondering, more so than just for yourselves. But do you think that changes the landscape of M&A and consolidation for the broader Foodservice industry?

Joel Grade

Yes, I don't know that we think about it that way. And again I think at Tom's point, I mean, look our M&A as we talked about, we anticipate between 0.5% and 1% of our total sales in any given year. And obviously that moves around a bit, given by quarter given what we may or may not have or lap. Again we feel certainly good about our pipeline of deals. Certainly feel good about the companies we brought on over the last couple of years.

And I think, I don't know, I think from an overall industry perspective, I just think there is plenty of room for consolidation, continues and again I think that will continue to happen. And I think you certainly should expect that from the broader industry and from ourselves as well. I think it's interesting to see how some of those things all play out. And what the regulators are interested in, in this math. But I would just, as I said earlier in the call, I don't believe, what's happening there as we have really significant impact on how we think about M&A.

Jeffrey Bernstein

And just lastly a clarification on what you said earlier about inflation. It looks like now, like I said, you're approaching 3% which is maybe the upper end of your two to three sweet spot. But has been kind of upticking the past number of quarters. I'm just wondering whether you would expect it to lag of that 2% to 3% range to the upside. And if it did, which commodity have you seen some more significant signs of inflation, whether it's protein, dairy or produce or otherwise.

Joel Grade

Yes, I mean as I think and again Tom can chime in here. I think our view would be that we still stay within that range for the most part again. Obviously, we've had some issues in terms of pork and some of the other pork related commodities that are on the higher end of that. Obviously, there have been some of the challenges certainly they are well documented. Obviously, produce has been certainly on the higher end of that range. A little of that's certainly is oftentimes the category of that that moves around a fair bit.

So I would just say, generally speaking, I mean, you're right. We're on the bit of a higher end of the range that we consider kind of the optimal place. But outside of that, I don't know if there's anything that, that we would see that would drive significantly. We get questions fairly often on the question on pork, just in general. But again, our pork certainly, a fairly small percentage of our overall business and not something that people are seeing, that our folks are seeing something that we should be overly concerned about over the near future.

Tom Bené

Jeffrey, I think, the only thing I'd add is, as Joel mentioned the center of plate items are the ones that can drive the biggest impact for everyone, because it's such an important part of the menu for the operator and where they struggled to pass things along. So I think we just have to stay focused on those key center plate categories meat, poultry, seafood, and certainly pork falls within the meat segment of that.

And then the last thing as Joel mentioned produce. I think it's something we just got to stay close to. There were some ups and downs a year ago, seeing where that ends up. And dairy has been on the higher end too. So I think you're right. We're feeling good about where things are now, we think that -- we hope that they maintain within this range, but if we have any concerns it would be around those center plate and produce items.

Operator

Thank you. Our next question comes from Andrew Wolf from Loop Capital Markets. Your line is open.

Andrew Wolf

On the acquisition side, I think you said you expect more -- you announced $155 million acquisition last, at the end of the -- toward the end of this quarter, the one you just reported. So doing the math that's about 25 bps, a little below what you think it sounds like you can get to. First of all, are there other acquisitions that we could model in right now that you've kind of would add to that 25 bps roughly. Secondly, kind of related to this, the next two largest distributors in the industry are involved in very large acquisitions at different stages, but pretty early on. How does the market look to you in terms of, as a buyer out there looking for targets in terms of availability and valuations?

Joel Grade

Well, a couple of things. First of all, as it relates to other acquisitions, obviously again the only thing I can reiterate there, obviously, I think able to reported anything specifically is that we continue to feel good about the pipeline that we have in front of us. And certainly, so again reiterating just our overall guidance around the sort of 0.5% to 1% in any given year, it's again moves around by quarter some. But all I guess I can say there is, without being able to go into specifics, it's again we certainly feel decent. We feel we're in a good place with our pipeline and obviously there's something we can talk about. We will certainly do that.

I guess just in general, I mean the sort of the view of the large, again, certainly, I don't want to speak for other competitors in the space. I guess the only thing I would say there though just in terms of context. You obviously the density of our network in this certainly are in the United States is, I would say, significantly higher than the others in our space. And so the ability for them to take on additional geographies or additional areas that you consider white space for them is obviously a bit different than the way we would look at some of those things. And so outside of the deals that we've done in Hawaii are recently and obviously outside of our core markets in North America.

But in our North American business, again the density of our network it puts us probably a little bit in a different place in terms of how we look at some of those deals and then are probably our two largest competitors. So I think just from that contextual perspective would be the way I would think about that. We certainly again have again lots of opportunities in front of us and we'll certainly continue to be aggressive in that space. But probably the best context I can give you there at this time.

Andrew Wolf

And then I just wanted to either circle back or just ask directly about this African swine fever in China and other parts of Asia that you hear different views on that from kind of semi catastrophic to sort of probably not -- not that great. How is Sysco sort of viewing this? I mean, I'm not asking you to make a prediction. But what kind of contingencies are you thinking about, what kind of scenarios you're looking at, and so on, if you have any? Thanks.

Tom Bené

Andy it's Tom. Look, I think it's something that's, it's out there. It's something that we are starting to stay very close to. We think over the next six months that there could be some impacts in that area that especially if you think about other markets may be beginning more import of that because of their needs. I think if you think about the pork segment, there are various components of that, some that are more important and our bigger part of the sales and others.

And so I think we're staying close to try to understand what impact might exist in some of those different areas. So I think there are two, probably two things you should just think about. I mean, it's been out there for a while, we haven't seen major impacts yet, but we believe there could still be some. And the way we think about that is, we work closely with our restaurant operators and certainly with our suppliers.

We're not going to be in a position where we're not going to have availability. That's not going to be the issue, it's really a matter of do the prices in some areas get to the point where customers start to transition those menu items or think differently about those menu items. And I think that's the work we're always doing with our customers to stay abreast of the impacts that might be happening on these certain product categories. And try to proactively work with them so that they are not in a situation where it dramatically affects their ability to drive profitable growth in their own businesses.

So I'd just say, we're very close to these kind of things. We have lots of resources that are involved both with our supplier partners and here. And right now, I think we're saying our sense would be, over the next six months, we'll probably see some increased impacts here, while we are proactively trying to manage that both in the company with our customers.

Joel Grade

And I would say just even in terms of just sourcing availability of product, as well as substitutes. So I think that's one of the things that we've certainly been very active in working with customers and managers navigate through those things in the past and certainly we are moving forward.

Operator

Thank you. Our next question comes from Kelly Bania from BMO Capital Markets. Your line is open.

Kelly Bania

Tom and Joel, I wanted to just go back to the independents. And I was wondering if you could or the local case growth and wondering if you could unpack that 1.4%. Just help us understand kind of what types of trends you're seeing underneath the types of restaurants, regional trends, open new customer openings. And regarding the improved exit rate, can you elaborate on that. Is that just comparisons, or is that internal or external factors. And then the last part is, I think you had been targeting closer to a 3%. And so, I'm curious is that still on the table or should we be thinking about a 2% to 2.5% kind of going forward for that segment? Thank you.

Tom Bené

So a couple of things, as we talked about earlier on the 1.4%, part of what we talked about is, we feel very good about the growth within the independent restaurants segment and including in that would be the this more of the regional or micro kind of change we've talked about as well. We did talk about we do see this from time-to-time. We talked about the impact from what we think about is almost local bid business. So we talked about local schools as an example. There is some of that that falls into these local numbers. It's not national business, because it's literally local school-type agreements or some kind of local governmental things that fall into that as well.

So I think what we see is and why we feel good and confident is that the restaurant side of it is strong, and we're seeing good growth there. And so I think that piece you should, rest assured that we feel good about the work we're doing. And I think it's a combination of, as we talked about, us making sure we're remaining competitive in that space. But also there are some, as I mentioned, also some tools that we're providing our selling organization that help them to understand where they can improve their overall penetration within those customers. So I think it's a good balance of both new business opportunities that exist and that we're able to pick up, as well as the penetration within those existing customers.

As far as the 3% number versus where we are today and maybe with 2.5%, I talked about earlier. I think we just have to continue to think about the fact that we're going to see improved growth in this segment given the fact that we have things like this local bid business in there. I can't sit here today and say that we still deliver the 3% overall for the whole time frame. But we still feel like that 2.5% to 3% is not an unreasonable number for us. So we are cycling two of our biggest quarters in Q4 and Q1 from prior year, as we've talked. And so I think we'll get some benefit of that may be going forward, but that really wasn't part of the sequential improvement, I talked about as we exited Q1.

Kelly Bania

And then, I think I heard you mention or maybe Joel mentioned some signs of improvement in the labor market. And I was wondering if you could elaborate on where and what you're seeing and what you're thinking about in terms of where -- how you are staffed appropriately for the rest of the year?

Tom Bené

Yes, I had mentioned that we are seeing some settling I guess right, I'd say it. As we all know over the last couple of years, the labor market has been very tight, it continues to be tight. But what I think we found is, and we see this in our own associate retention numbers is we're seeing better retention. And therefore, when I say we're seeing -- feeling a little bit better about that labor market, we feel like we're having a little more stability than we had there for a while, both in our -- and I'm mainly talking about our front-line operating associates warehouse and drivers.

And so what we have also talked about is, one of the things we've been focused on is, not naturally transitioning some of that business when the season has got softer, because then we'd have to ramp back up as we came into the new season. And so what we're still evaluating is we need to be thoughtful here. We'd rather maintain our good associates and continue to invest in them during the lower seasons to ensure that when time comes to ramp back up, we're not in a situation like we were in the past where we are now scrambling for labor having to potentially do a lot of training. There's a lot of expense associated with new hires and not the least, which is the training and development of them and getting them up to speed.

So that's really what I was referencing. I think we'll continue to evaluate, we think the model we have right now is a good one for us. But as we get into some of the lower parts of the year, I mean volumetrically that could have some impact and we're just trying to make sure we understand the pros and cons of that business practice that we've employed.

Operator

Thank you. Our next question comes from John Ivankoe from JP Morgan. Your line is open.

John Ivankoe

The Canadian regionalization was mentioned a couple of times, and it sounds like, at least in that market it's having some effect that at least in terms of delivering more profitability. And it looks like as well some more case volume as well. Are there any lessons to be learned from that project, as it relates to the United States? In other words, is that lagging the United States in terms of implementation of that structure, or might the United States to be able to learn something as to what is happening in Canada?

Tom Bené

So the Canadian regionalization is something we have talked about a few times. And it's an effort that we started about 15 months ago and we were implementing it throughout last fiscal year. So we're getting some continued benefit as we move into this fiscal. And I would say that it's a little different than the U.S., because just the sheer geography and types of facilities we had there. We had regular size operating companies like you'd expect to see in the U.S. and we had some smaller operating companies, significantly smaller than we have in the U.S.

And in the case of Canada, we had a similar management structure at every one of those facilities. And so we just felt like there was an opportunity to better structure ourselves up there from a cost perspective to take out some of that additional expense associated with some of those smaller facilities.

There is certainly been learnings there that we do believe over time might have some applicability to the US, but it is a little bit different setup than what we have in the U.S. and that drives some difference in the way we have opt to think about it going forward. But we feel good about the lessons we're learning and we've had many, and I would say it's still work-in-progress, but we're feeling good about the effort and time will show whether or not there is some similar opportunities here in the US.

John Ivankoe

And this wasn't really apparent in the results, maybe a little bit just in terms of the overall inflation numbers. But there was some very unusual pricing behavior this quarter that happened because of the beef processing plant fire that happened where number of different state cuts actually in the spot market spiked up considerably. Did you see anything unusual happen within your P&L that happened because of this kind of intra-week volatility, specifically on the beef side or is your company just big enough that, that would have been noise?

Tom Bené

Well, John, first of all, I mean, because of the way we go to market with the supplier partners, and our agreements, those things for us are probably a little bit of noise more than anything else, but not big impacts for sure. And that's one of the things as we've talked, I think over the years that their own should feel really good about is, the long-standing relationships, the way we've built our relationships with our suppliers are not short-term, they are longer term in nature, and that helps us I think dramatically as we go in and out of these type of events. It's unfortunate when they happen, and it's difficult for our suppliers. But we're generally able to manage through those pretty seamlessly.

Operator

Thank you. And we will take our last question from Bob Summers from Buckingham Research. Your line is open.

Bob Summers

Just a quick question on the calendar for second quarter, the period between Thanksgiving and Christmas has shortened. I think last time we went through something like this, Starbucks was impacted. I mean, I think it's really pent-up demand for restaurants. Did it impact you at all or should be expect any weakness associated with that?

Tom Bené

Bob, I don't think, you know from where we're sitting today, we don't necessarily believe so. It's a fair question and something we're certainly have to go do a little more work on. But we don't, at this point, see any historical impact or feel like that's going to be a problem.

Bob Summers

And then second, you guys seemed really confident with the acquisition pipeline. Just curious what you've seen on the seller expectation price point, point of view? I mean, arguably two big competitors are now out of the market for some period of time. I'm wondering if seller expectations have accordingly modified.

Joel Grade

Bob, it's Joel. I don't know that I'd say we've had a lot of seller impact. We have previously been asked a lot about just sort of the overall high price that U.S. Foods SGA deal was. I mean did that impact expectations. Just I would say generally no. I mean we've got a pretty steady -- every deal is very different. I can't say we've run into a lot of situations where we just -- again, that aren't very deal specific where we would say, hey, there is some inflated view of expectations, or the opposite direction.

So I mean, I think we had -- we've historically had a pretty, I'd say, normalized view of what we expect our M&A multiples to be. And I would say generally speaking, discussions we have with people today are generally within that range. So there is nothing, again, outside of what I'd call very deal specific situations that come up from time-to-time. There is nothing that I would say impact, either what direction of, either higher or lower related to the deals or the, as you suggested, possible timing today.

Operator

Thank you. And that does end today's question-and-answer session. Ladies and gentlemen, this concludes today's conference. Thank you for participation and you may now disconnect. Everyone have a great day.