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Performance Food Group Co. (PFGC)

Q2 2021 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day and welcome to PFG's Fiscal Year Q2 2021 Earnings Conference Call. [Operator Instructions]

I would now like to turn the call over to Bill Marshall, Vice President, Investor Relations, for PFG. Please go ahead, sir.

William Marshall

Vice President-Investor Relations, Performance Food Group Co.

Thank you, Laurie, and good morning. We are here with George Holm, PFG's CEO; and Jim Hope, PFG's CFO. We issued a press release regarding our 2021 fiscal second quarter and first half results this morning, which can be found in the Investor Relations section of our website at pfgc.com.

During our call today, unless otherwise stated, we are comparing results to the same period in our 2020 fiscal second quarter and first half. The results discussed on this call will include GAAP and non-GAAP results adjusted for certain items. The reconciliation of these non-GAAP measures to the corresponding GAAP measures can be found at the back of the earnings release.

Our remarks on this call and in the earnings release contain forward-looking statements and projections of future results. Please review the cautionary forward-looking statements section in today's earnings release and our SEC filings for various factors that could cause our actual results to differ materially from our forward-looking statements and projections.

Now, I'd like to turn the call over to George.

George L. Holm

Chairman, President & Chief Executive Officer, Performance Food Group Co.

Thanks, Bill. Good morning, everyone, and thank you for joining our call today. I'm excited to share PFG's second quarter results with you this morning. I'm proud to say that our company has continued to weather the challenging market conditions and distinguish ourselves as leaders in the food distribution industry. It is our hope that we will soon be able to gather together at our favorite restaurant with friends and family. And we all look forward to the day when our lives resume a more normal pattern.

In the meantime, our associates have been working hard to position our business for long-term success. We also want to say we are humbled but not surprised by the creativity, tenacity, and resilience our customers have shown. We are proud to be partners with so many hardworking individuals in the restaurant industry, doing our part to help make each of them successful. As expected, the winter brought its challenges; and like the rest of the industry, our business did experience a modest slowdown in December. And while January is typically a seasonally softer month for PFG, we are encouraged by a modest acceleration in sales trends in recent weeks in our Foodservice business.

With that said, until the pace of vaccination picks up dramatically, we do not expect to return to a more normal operating run rate for some time. However, once the public feels comfortable gathering in groups, we anticipate a surge of volume at restaurants. Therefore, we are prepared for this acceleration with appropriate levels of

inventory. We feel very good about our capabilities to execute this plan and are equipped with ample liquidity. Jim will share more about our financial position in a moment.

Meanwhile, the integration of Reinhart continues to meet our original expectations, truly a great feat considering the external challenges that could have been a distraction. This speaks to the dedication of our associates who have worked diligently to accelerate growth and capture our targeted cost synergies.

We also continue to believe that we will achieve the roughly \$50 million of annualized cost synergies in the third full fiscal year following the closing. And, furthermore, we are pleased to announce that we have completed our transition services agreement with Reinhart. We are pleased to see the pace of sales recovery at Reinhart.

While still not quite at the growth level of legacy Performance Foodservice, Reinhart sales trends have steadily improved. Importantly, the sales compensation structures have been fully aligned and we are moving ahead on all plans to accelerate Reinhart's growth profile. As you know, as of the beginning of our fiscal third quarter of 2021, we are fully lapping the acquisition of Reinhart. In a moment, Jim will provide color on how this will impact the modeling of our business in the quarters ahead.

As we have said over the past several quarters, many of Vistar's channels continue to be significantly impacted by the current environment. Still, the resilience in several channels, including convenience stores, value, retail and corrections, plus the focus on cost containment have kept that segment profitable. When people return to work, begin to travel and once again gather in groups, we anticipate a full recovery in Vistar. We continue to expect a much slower recovery in theater and office coffee services. While we have been hopeful there would be a modest rebound in some of these areas early in 2021, it is now evident that we should not expect a pickup until the vaccination plan is more fully executed.

It is difficult to predict whether occupancy in movie theaters and professional offices will return to normal levels. However, we do expect these lines of business to improve from where they are currently and remain profitable streams of business for PFG. Meanwhile, Vistar remains focused on executing on the plan that has made it so successful for decades, finding new channels and lines of business to provide long-term profitable growth.

One of these areas is our Eby-Brown convenience store business which has been a bright spot for our Vistar segment, a testament to the team's hard work and the resilience of that channel. We have successfully opened and are currently shifting from two new distribution centers in the Southeast to service the C-store channel.

Looking at our entire business, I am extremely pleased with how our organization has responded to current headwinds. Including the benefit of Reinhart, our total case volume increased 8.4% in the quarter. And importantly, our independent case volume rose 26.5%. Excluding the Reinhart acquisition, total organic case volume – our total case volume fell 16.9%, but was down only 5% in the independent channel. And we enjoyed the margin benefit from the mix change. We believe that these results validate our strategy around investing for growth in the independent channel. We feel extremely well-positioned for a full recovery later in the year.

Now, I would like to briefly address the current operating environment. As I mentioned earlier, along with the total industry, our Foodservice business did experience some modest slowdown in December. We believe this was a result of greater restrictions, fewer holiday parties, and some impact to outdoor dining in colder weather states. With that said, we have experienced a modest rebound in January more in line with year-over-year comparisons that we experienced in October and November.

However, remember that we had a strong start to calendar 2020 before the shelter-in-place orders took effect. Our fiscal third quarter 2020 results only began to reflect the impact of the pandemic very late March. And as you know, the year-ago quarter also benefited from the acquisition of Reinhart which closed in late December. As always, our intention is to run our business for the long-term and invest as appropriate for sustainable growth. We are pleased with how the strategy has played out over the past year and strived to continue our momentum.

Before turning it over to Jim, I want to highlight a few ways that PFG associates have helped us do more for our company, our customers, and our communities during these extraordinary times. Many of our operating companies reached out into their local communities making donations to support the elderly, healthcare workers and families in need. While those actions were local, the generosity, care and commitment to serving others are universal across our family of companies.

Last quarter, PFG published its first annual ESG report. Sustainability and social responsibility have long been important focus areas for our organization. To support these efforts, we've developed an internal governance team to oversee our ESG efforts as we continue to address the issues that are most important to our business and stakeholders. We also celebrated our customer service professionals who, along with our dedicated sales teams, are helping our customers find success in difficult times. Finally, we are so proud of our drivers, selectors and frontline supervisors who are essential to our business and keeping our country's food supply chain moving.

Last quarter, 21 of our drivers were officially inducted into the IFDA Hall of Fame and one of our drivers, Darrell Breeden, recently retired after more than 42 years with zero accidents, zero tickets, and a commitment to delivering service that has been second to none, that is truly an amazing accomplishment.

The bottom line is, supporting our local communities and our customers with such care shows in our results. I am proud of all the ways our people have risen to the occasion both for our business and all the stakeholders we serve.

With that, I'm going to turn things over to Jim, who'll give you more detail on our second quarter and our financial position.

James D. Hope

Chief Financial Officer & Executive Vice President, Performance Food Group Co.

Thank you, George, and good morning, everyone. Let's start with a quick overview of our results for the second quarter of fiscal 2021 which demonstrates the resilience of our business. As a reminder, unless we mention otherwise, the fiscal 2021 results include the acquisition benefit from Reinhart.

Total case volume increased 8.4% in the second quarter compared to the prior-year period, driven by the acquisition of Reinhart. Excluding the impact of the Reinhart acquisition, case volume declined 16.9% in the second fiscal quarter. As George mentioned, independent cases were up 26.5% in the quarter, including Reinhart, and were down just 5% when the impact of the Reinhart acquisition is excluded. Even with a more challenging December, we saw our year-over-year independent case volume declines improve sequentially from the first to the second quarter.

Net sales grew 12.8% in the second quarter of fiscal 2021 to \$6.8 billion. The acquisition of Reinhart contributed approximately \$1.3 billion to net sales in the quarter. Overall food cost inflation was approximately 2.6% in the second quarter, driven by cheese, disposables and produce.

Before moving on, a quick word about inflation. We've experienced higher rates of inflation of late, particularly in the Foodservice segment. However, at this point in time, we're confident in our ability to pass inflation on quickly without any major disruption to the business at all.

With that said, we know that it's a dynamic time in the market and our team will continue to monitor the situation closely in the weeks and months ahead. Gross profit for the second quarter of fiscal 2021 increased 14% to \$811.1 million as compared to the prior-year period. Gross profit per case was up \$0.26 in the second quarter versus the prior-year period. Gross profit margin as a percentage of sales was 11.8% for the second quarter compared to 11.7% for the prior-year period. The increase in gross margins was due to positive mix shift due to better performance in our independent restaurant channel and the addition of Reinhart.

Operating expenses rose by 18.9% in the second quarter compared to the prior-year period. The increase in operating expenses is primarily due to the Reinhart acquisition. We also want to highlight a positive development in operating expense in the second quarter driven by an improved medical and safety experience rate, which resulted in lower insurance payments. Some of this was due to a smaller and more experienced workforce. Altogether, this resulted in about \$12 million of lower operating expense.

In the second quarter, net income declined 57.3% year-over-year to \$17.6 million. Adjusted EBITDA rose 10.6% compared to the prior-year period to \$158 million. Diluted earnings per share was \$0.13 in the second quarter, representing a 66.7% decline over the prior-year period. Adjusted diluted EPS was \$0.35 in the second quarter, a decline of 39.7% year-over-year.

Let's now turn to second quarter results for our two segments. Our Foodservice segment's fiscal second quarter net sales grew 27% to \$4.9 billion, driven by the acquisition of Reinhart. Foodservice EBITDA increased 36.7% in the second quarter to \$155.3 million. Net sales for Vistar decreased 11.9% in the second quarter to \$2 billion. Second quarter EBITDA for Vistar was \$38.7 million, a 31.6% decline over the prior-year period.

Let's now briefly discuss our liquidity and cash flow profile. As we mentioned on our last earnings conference call, working capital gains we saw in late fiscal 2020 began to reverse to start fiscal 2021, as expected. In the fiscal second quarter, we continued to work down our payables, resulting in another cash outflow on that line item.

However, this was partially offset by \$118.7 million income tax refund and cash generated from lower levels of inventory and receivables. As a result, cash from operations was just \$24.4 million negative for the first six months of the fiscal year. I remain very pleased with our organization's continued management of our working capital position.

PFG invested \$83 million in capital expenditures during the first six months of fiscal 2021, an increase of \$34 million over last year. We will continue to spend to support future growth opportunities, including increased capacity and expansion into new lines of business.

We ended the quarter with another strong total liquidity position of about \$1.9 billion. Our liquidity at the end of the fiscal second quarter consisted of approximately \$417 million of cash plus nearly \$1.5 billion of availability on our ABL facility. We believe our liquidity puts our company in a strong position to continue to invest in the business.

As George mentioned earlier in the call, we expect to ramp up our inventory position as the market begins to return to a more normal rate of sales. While the exact timing is uncertain, our financial position should allow us to use our balance sheet at the appropriate time to meet market demand. Also, PFG remains well-positioned to take advantage of M&A opportunities that may arise over the intermediate term. As always, we intend to be disciplined

with our capital allocation and strive to pursue targeted transactions that we believe would enhance shareholder value.

In summary, our Foodservice business is in a strong position. It's performing well in the current environment and prepared for a robust recovery. The highly successful Reinhart acquisition is meaningfully contributing to our organization and we have completed the transition support agreement. We have consistently invested in our sales force and our customer service support which has driven a steady and encouraging sales volume recovery, particularly in the independent channel.

And while we expect a slower recovery in several Vistar channels, we still see avenues for growth over the long term. All of this is supported by our liquidity position and capital position, and we are committed to running our business for long-term success and feel that we have the people and the financial flexibility to do so. We're very proud of our organization and how our associates have risen to the challenges in the past 12 months. We'll begin lapping the effects of the pandemic in a few weeks. And while we recognize there is still some time before normal life will resume fully, we are prepared and look forward to a robust recovery.

We appreciate your interest in Performance Food Group. And with that, we'd be happy to take your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from the line of John Heinbockel of Guggenheim Partners.

John Heinbockel

Analyst, Guggenheim Securities LLC



Hey. So, George, I want to start with the two things on the independent side. If you look at the markets that are the warmest, right, the ones that are the most open, are you actually seeing growth there versus that minus 5%? And then, secondly, can you sort of segregate out the minus 5%, right, in terms of existing accounts – penetration with existing accounts, new account pickup, lines per existing account, kind of break that out for us if you can?

George L. Holm

*Chairman, President &
Chief Executive Officer,
Performance Food Group
Co.*



Okay. We have several markets where we're actually doing more independent sales in the previous year in sum – total company. And I would say that, right now they are mostly in warm weather areas, are really challenged markets, are Metro New York, parts of New England, Chicago, Minneapolis, and then in the West Coast is really cold. Our new account growth is pretty consistent with what it's always been, last quarter a little bit better than normal. We are running less lines per order but more dollars per order and more cases per order, and we're running more dollars and cases per account as well.

John Heinbockel

Analyst, Guggenheim Securities LLC



Okay. Maybe to follow up on that, right, that obviously should translate, right, if you're – I guess, that suggests your drop size, drop sizes are higher, right, the economics being better. I assume that's having a positive impact

on profitability of the business, and do you think that continues, what happens in a recovery, will we still see higher drop size that you think that will tail off?

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

A

Yeah. I guess, I would kind of answer that, I don't have a crystal ball. But I don't see what would change that. I would hope that it would get better because the customers should be doing more business then. We've seen people reduce their menu and – particularly for a takeout. So, that's kind of affected our lines, but actually helped our sales per line. So, it's just a different environment than we're used to. And I don't see any big change to that other than we should see volumes increase. Now, I would imagine, some of these menus will go back to being expanded.

John Heinbockel*Analyst, Guggenheim Securities LLC*

Q

Okay. Thank you.

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

A

Thanks, John.

Operator: Your next question comes from the line of Alex Slagle of Jefferies.

Alexander Russell Slagle*Analyst, Jefferies LLC*

Q

Great, thanks. Good morning. On the Vistar business, the EBITDA contribution improved a bit versus the first quarter levels, and wondered if you could comment a bit more on the moving pieces in that business and what change versus the first quarter really drives the improved margin performance?

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

A

Yeah. There's a very gradual and I mean gradual improvement in sales. So, that helps. I mean, we dialed the business back as much as we're comfortable dialing it back. And we've got a little help on the expense line. And then, Eby-Brown has done very well. And that's the bulk of the improvement is in our convenience part of our business.

Alexander Russell Slagle*Analyst, Jefferies LLC*

Q

Got it. And just more broadly, it looked like another big mix contribution driving that delta between the sales and the case growth, and just wondered if you could provide a little more color on that and if that's going to continue to the same magnitude, start to moderate into the third quarter, what your thoughts are there?

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

A

Yeah. I think that's going to really depend on mix. We got a great benefit from mix, but we really didn't see much of a change in margins in each area, adding two more convenience markets which we had three weeks of shipping in last quarter and out of one of those and they both have been shipping, starting in early January, we've had both shipping. So, that's going to add volume to the tobacco area which is extremely low gross margins albeit good gross profit per unit.

So, that could have some impact as we get into the third quarter. But that's – it's great incremental business. So, I'm probably not comfortable to comment on what benefits we'll get from mix, but I don't see us having any margin issues versus where we're at now or versus the previous year in any of the businesses.

**Alexander
Russell Slagle***Analyst, Jefferies LLC*

Okay, great. Thank you.

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

A

Thanks.

Operator: Your next question comes from the line of Edward Kelly of Wells Fargo.

Edward J. Kelly*Analyst, Wells Fargo Securities LLC*

Q

Hi, guys. Good morning. So, my first question is really around sort of like the investment around the recovery. You've had an outstanding history of sort of managing the business for the long-term. Can you provide a bit more color around how you're positioning for the COVID recovery from an investment standpoint? And I ask this because your peers have had issues recently that, I guess, it seems like with your numbers there you avoided to-date. But as we think about the next quarter or two, how do we think about the progression of sort of the cost ramp versus revenues? Do we get some temporary mismatch around that and how does that impact the way we should be thinking about the progression of EBITDA?

George L. Holm*Chairman, President &
Chief Executive Officer,
Performance Food Group
Co.*

A

Well, I think there's some things that – we got some puts and takes there. I think there's some things that are going to help us. We never really managed the business for short-term and we were – we didn't panic and we were really consistent going through this. Our customers had a lot of disruption and we didn't want to add to that disruption. So, we've been real consistent.

But we have markets, as I mentioned, where we're exceeding last year in sales. In some markets, it's fairly significant. And I go back to last February where we were really performing well and we were having labor issues. And where we now have more employees than the previous year and how does that add back fairly significantly, those same issues have come right back up. So, I think there's a potential for some disruption. We're trying as

best we can to be ahead of it. We've continued to invest in capacity. We haven't done any consolidation of distributions between Reinhart and Performance Foodservice, because we don't want to give up any capacity. So, I think that's going to help us moving forward because we don't want to add disruption in the recovery either.

As we downsized our business, we were careful. I mean, we had to dial it down. I mean, we are the responsible people, so we only wanted to dial down so far. And almost all of the people that we reduced were furloughs and we did furloughs with benefits. So, we had an easier way of getting them back as we really wanted them back. And we were able to get some of them work in the retail business and we have some that are still doing that.

I think what's going to help us is, as we bring people back, we're not going to have to train those people. Maybe some retraining would be involved particularly with the salespeople. I mean, there's such a long learning curve. And the only sales people that we furloughed were less than 90 days.

I think that it's not going to be easy and you got to have people ready to go. But I don't think it's going to be an enormous issue. I do have concerns that people won't want to come back to work, you always worry about that, right. We've had that issue as people basically got paid not to work. We did have some issues with that. So, I'm giving you probably a way too long an answer, but we have a level of comfort that we're ready to go. But it's got to be right labor market.

Edward J. Kelly

Analyst, Wells Fargo Securities LLC

Q

So, George, on the other side of this, right, it does seem like as volumes come back, it's not going to be easy, I guess, to the match is sort of like inventory and expenses and all against that, and you obviously are thinking about things the right way. But there's a large portion of the industry that has been really short-term focused. How big is the opportunity when things come back as, call it, like your non-publicly traded peers are tempting to sort of ramp up against that, it just feels like there would be almost a bigger opportunity for you then than what there was when things were sort of like getting softer and everybody was just cutting working capital, but generating cash, and maybe not having as many problems.

George L. Holm

Chairman, President & Chief Executive Officer, Performance Food Group Co.

A

Well, I think that is the tipping point, is when people do have to invest more in receivables, more in inventory; and, quite frankly, get caught up on their payables. I think that's an issue out there in the industry. If you look at our balance sheet, I mean, we obviously tried as best we could not to panic around anything, but did we ask for some support from our suppliers and we got it. And you can see that that reversed itself last quarter.

So, we don't have that concern from a liquidity standpoint to deal with. So, we'll see when it comes back. I think another advantage that we have is that, we haven't had a great customer mix to deal with this type of situation, particularly in Vistar. But I think that we've had an advantage. We have an excellent pizza business and that hasn't suffered as much. It centrally has whether sit-down restaurants that didn't have a good history and take out an ability to deliver. But some of them have done well.

And then, when you get to the non-commercial business excluding Vistar, we do very little lodging business. We do very little contract feeding business, and that business has suffered more than the restaurant business. But then, the flipside of that is that, our national account business has suffered more because we're so big in casual dining and we think that that's going to have a real strong comeback. So, lot of puts and takes. But I think we're in a good position to be ready for it. And if it – if there's acquisition opportunities because of an inability to reload on inventory receivables, we'll certainly be as opportunistic there as we can be.

Edward J. Kelly*Analyst, Wells Fargo Securities LLC*

Great, great. Thank you.

Q

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

Thanks, Ed.

A

Operator: Your next question comes from the line of Kelly Bania of BMO Capital.

Kelly Bania*Analyst, BMO Capital Markets Corp.*

Hi, good morning. Thanks for taking our questions. George, just wanted to ask about Vistar. It sounds like you do expect a full recovery there eventually, maybe some parts do take a little longer. But can you just remind us how different or the same profitability by channel is there, just thinking if we do end up with a little bit of a different mix in terms of channels longer-term, how that could impact the kind of ultimate recovery for the margins in that channel?

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

Yeah. First of all, I think we've made a lot of progress surprisingly in Vistar. It is – our flagship business has been the whole time – its level of profitability, if you talk about EBITDA margins, has always been our best, just kind of like our most profitable places are big broad liners followed by Vistar. And I see that continuing. Once it comes back, I did mention there's two channels that I do have concerns with, that's theater and that's office coffee service. There's been some changes in the makeup of the feeder business that could impact us negatively. I think that's going to take a while because there's a lot of great products sitting on the shelf. So, we're going to see really good movies coming out one after another when things come back.

But a little concern there and then two ways to look at that – at the people coming back from work. First of all, if less people come back to offices, that's going to have a negative impact on our office coffee service business. But the flipside of that is, in our micro market business we had many people, I mean, many that have cafeterias today that have already come to us and said, look, as people come back, we're not going to have this many and we're not going to be able to support the cafeteria, and we want a micro market program. And we've got some big customers that are really effective at putting those micro markets in. So, I think that could benefit us.

I also feel very good about the vending area. From a top line standpoint, that's still our biggest business in Vistar. And it's – those are most – the heavy users there are mostly in jobs that you have to be there to perform that job. It's not something you can do from your home. And I do feel that manufacturing, which is the biggest heart of that business for us, I think we're going to see more manufacturing come back to the US. Not a short-term benefit, but I think that's going to be a benefit for us.

So, in my mind, if I put all those things together and some of the things that our people have worked on at Vistar and I see us doing well. And we've made some management changes there – not changes, but additions, but we have appointed Patrick Hatcher there, who's been both the CFO and the Senior VP of Sales, as the President and Chief Operating Officer, still reporting in to Pat Hagerty who's run that business for years. And it will give Pat more time to spend in the convenience area and on these projects that we have gone on that we think are going to

really help Vistar in the future, and then fairly near future. Long answer, Kelly, but that's kind of where we sit today.

Kelly Bania*Analyst, BMO Capital Markets Corp.*

Q

No, that's very helpful. And just to follow up, you did – or there was a comment about M&A and, I guess, you've always been acquisitive clearly, but I was just curious what are you looking for today, what is the right fit, is there a geographical fit or capability either on Vistar or PFS, just would love to hear what you're seeing and ideally what would be the right fit for you next?

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

A

Yeah. Well, and I feel that we've developed a pretty organized approach there where we were, in the past, just kind of more opportunistic and our deals were more relationship-driven. And we have what we think is a pretty robust pipeline in both the Vistar side of our business and in the Performance Foodservice. But nothing that we could say today is actionable. And I do feel that, when some normalcy comes back, I think that's when the opportunities are going to present themselves.

James D. Hope*Chief Financial Officer & Executive Vice President, Performance Food Group Co.*

A

Yeah. And I think I'd also add that what we're looking for, of course, is something similar to Reinhart or an Eby-Brown, that was strong cultural fit. Their folks fit in the organization well and we embraced each other quickly. They added strong shareholder value and they've built in some spots in the supply chain, making the supply chain and our distribution chain much, much stronger.

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

And we look very hard at culture. It's just kind of the way we're built. We're trying hard. We felt like we were getting a very well-run company. We felt like culturally it would be a good fit, knew a lot of the people. And it ended up exactly that actually extremely well-run company, it just needed to grow. And we're so pleased with the growth that they're starting to show. And fiscal January is over for us and it's the first month where we had overlapping business there. We haven't moved – well, we moved a little bit of business around, very, very little, not even material. And they had an excellent January. So, we're just really encouraged. And it just gives us more confidence to be acquisitive.

Kelly Bania*Analyst, BMO Capital Markets Corp.*

Q

Thank you.

Operator: Your next question comes from the line of Jeffrey Bernstein of Barclays.

Jeffrey A. Bernstein*Analyst, Barclays Capital, Inc.*

Q

Great. Thank you very much. Two questions. The first one, as we look through the current pandemic and think the other side here, and did you expect the largest foodservice distributors including yourselves to have achieved greater benefit on revenue or expense? I'm just wondering your thoughts there. Some of your peers have noted specific sales gains and expense reductions. I'm wondering whether you're seeing similar and prefer not to specifically itemize or maybe not seeing to the same magnitude? Any thoughts in terms of the outlook in terms of revenue or expense for yourself and your largest peers post-COVID. And then I had one follow-up.

George L. Holm

Chairman, President & Chief Executive Officer, Performance Food Group Co.

A

Yeah. I mean, if you took the share gains that we believe we made, based on the information that we do get, it doesn't cover the entire market, but, definitely, our biggest benefits have been on the revenue side. And if things get back to normal, okay, if we go back to 2019 industry size, then we're going to get a great benefit particularly if things come back similar to pre-COVID in the Vistar part of our business.

As far as expense goes, I'd like to believe that we were always very expense conscious. I think we learned going through this that we weren't as good as we thought we were. But we also want to continue to really invest in people. So, I would say that, clearly, the revenue side is where we're going to get the best benefit. And from an expense standpoint, I know we will benefit. I can't begin to put a dollar amount to that. I just – I don't think we know enough today. We got to see what things are like when it comes back.

Jeffrey A. Bernstein

Analyst, Barclays Capital, Inc.

Q

Understood. And then, as you think about the small- to mid-sized players, whether it's in the restaurant industry or in your own foodservice distribution industry, I'm just wondering who you think was hit harder, maybe how much capacity was likely removed? It seems like on both restaurants and foodservice distribution maybe the capacity reduction was less than some had initially feared. Just trying to get your perspective on both industries in terms of how the small- and mid-sized players are faring versus yourselves.

George L. Holm

Chairman, President & Chief Executive Officer, Performance Food Group Co.

A

Yeah. I'm going to preface that because, remember, we don't have – we're fortunate we're a large company but we don't have a huge share. So, I can only tell you what we see based on the business that we have, but we're seeing that the independent is incredibly resilient. I mean, amazingly so. And we're maybe mid-single digit as far as number of customers that have just gone away, but many of them have been hit hard from a volume standpoint, but not really gone away.

The big chains, most of them have retrenched, the ones that we do business with, but not hugely. And I think they're going to get a big benefit. And then where – for whatever reason in our business, the ones that have been mostly – most hardest affected have been the regional chains, like – it's almost like not small enough to get the PPP, not big enough to be able to go to the public markets and redo your capital structure. And that seems to be where the more difficult times have been.

With our competitors, it's very hard for us to see. I mean, I finally, in the last few weeks, have heard of some smaller ones that just went out of business. But that's new and they're not real big. So, once again, I use that same word. They've just been really resilient, and we just don't know how much their balance sheet has been affected and what their availability to get the capital to dial back up, that's the wildcard to us.

Jeffrey A. Bernstein*Analyst, Barclays Capital, Inc.*

Q

Understood. And one just last clarification. I know in your prepared remarks you talked about the holiday season challenges. But just to clarify, December was the month of weakness. It seems like, I think you mentioned that January was maybe back to October, November levels. And otherwise your question around the near-term, it seems somewhat factual in terms of, right, you're lapping strength through late March last year and you did fully lap Reinhart, but are there any other near-term concerns to be aware of? I think you addressed that you don't expect a major labor shortage or anything along those lines, maybe something around inventory or anything else to be concerned about in the short term, or just the factual strength of what you're lapping and the Reinhart [indiscernible] (00:41:57).

George L. Holm*Chairman, President &
Chief Executive Officer,
Performance Food Group
Co.*

Yeah. No. I think there's three things that really impact us today. Two more short-term, one longer-term, but it's restrictions. When restrictions get lifted, you see a benefit immediately. Stimulus: when stimulus money comes out, we see a positive impact really quite immediately. But the big one is the vaccine, right. I mean, as the vaccine gets out there more, I think that's going to be a big help.

As far as ability to get product, we went through some pretty difficult times on our Vistar side. We're still running historically poor inbound fill rates. Foodservice has improved. And when we do see issues, it's typically virus issues within their manufacturing facilities, so they tend to be short-term. So, I'm feeling pretty good on – as far as our suppliers go. And I think a lot of the issues that we're dealing with in Vistar is just that many of those suppliers are retail packaging, and retail kind of got more attention, I would say, than maybe our channels.

And secondly, many of them – because they could sell everything they could produce, they don't want to change their lines as often. So, if they used to have 15 flavors of an item, they won't maybe to the 8 bigger sellers. So, our customers and our buyers continue to order. And it shows an out-of-stock, but actually it's a discontinued item, as to whether or not when things recover, if those items will come back in the fall, that we don't know.

Jeffrey A. Bernstein*Analyst, Barclays Capital, Inc.*

Q

Understood. Thanks very much.

George L. Holm*Chairman, President &
Chief Executive Officer,
Performance Food Group
Co.*

Thanks.

Operator: Your next question comes from the line of Peter Saleh of BTIG.

Peter Saleh*Analyst, BTIG LLC*

Q

Great, thanks. I want to come back to the conservation that you'd said around stimulus, clearly there was a little bit of a benefit in the month of January from the stimulus. And it does seem like there may be more stimulus yet to come in the weeks or months ahead. So, can you just remind us how far advanced you're going to be to plan in terms of inventory to capture that, and how do you guys think about the benefits of stimulus over the coming weeks and how you prepare on the inventory side and the investment side to capture that?

George L. Holm

Chairman, President & Chief Executive Officer, Performance Food Group Co.

A

Yeah. We're just trying to run heavier in inventories. It's really tricky in the perishable area, but that's what we're doing. And the thing about stimulus, when it gets announced and then it comes out fast, it is harder to be prepared. Now, what we have seen is a trend, when restrictions get eased, but not being an immediate, that was really difficult, because our customers would be starving for product. And they're all starving for product at the same time.

So, even like the New York situation, I mean, when it's on 25% and they give it to you that it's Valentine's Day, I mean, I'd rather, in many ways, be immediate. But that's when we can get on – we can get in there to these customers and find out what their plan is, are they going to have a reduced menu for it, those type of things.

So, I would just say we're as prepared as we can be. We're running high service levels, but not the kind of service levels that we would like to run. It's – this industry was really fine-tuned and you learned that going through this. And we operate with really short lead times from our customer. We try to get as shorter lead times from our manufacturer as possible, and we're turning that product very quickly. And that level of disruption was – it was difficult and it is not back to normal yet, but it's getting there.

Peter Saleh

Analyst, BTIG LLC

Q

Thank you. Very helpful. Just one last question on independents. I know you said mid-single digits maybe of independents have maybe gone away. Has anything surprised you? I know you said also they're fairly resilient, but has anything surprised you in the markets that are maybe a little bit more open for business these days. Any sort of key learning or takeaways that you can apply to some of the other markets as they reopen, including New York, Chicago, West Coast?

George L. Holm

Chairman, President & Chief Executive Officer, Performance Food Group Co.

A

Well, we keep real accurate records on what 25% means versus zero and what 50% means versus 25%, varies a lot by type of customer. But there probably isn't a situation that we haven't had to deal with and our OpCos have a pretty extreme amount of independents and autonomy, and they speak a lot to each other. So, they know who to talk to that's had similar circumstances and they, for the most part, have companies close enough that they can grab some products if they need to grab some products, so we've had more of that kind of intercompany transfers than normal. And it's – you can plan or you want to plan, but it's really the ability to be creative and to react fast when you have issues. And I think that's the biggest thing we've learned, is that we want to be extremely consistent and not be disruptive with all the other disruption, and you can't plan well enough and you just got to try to get these things done without the customer being affected.

Peter Saleh

Analyst, BTIG LLC

Q

All right. Thank you very much.

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

A

Thanks.

Operator: Your next question comes from the line of Greg Badishkanian of Wolfe Research.

Frederick Wightman*Analyst, Wolfe Research, LLC*

Q

Hey, guys. Good morning. It's actually Fred Wightman on for Greg. I wanted to circle back on the Reinhart commentary. The comments that you had made on the top line are really positive just as far as closing the gap with that legacy PFG business. But how should we think about the delta as we move through the next few quarters and sort of get closer to a more normalized environment?

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

A

That's a good question. I mean, they're – when we get our numbers, and like I said, it doesn't follow the entire industry. But we will get how we did from – versus the previous year and market share, of course, information, we didn't have the market share, but our sales we got, and then we get rest of the industry. That's the only two things that we get. So, we don't necessarily know. But we asked to get Reinhart's numbers separate from Performance Foodservices for the first year. We want to stop using legacy Reinhart or whatever. It's us now.

They were about the same as the rest of the industry early right after shelter-in-place. And they're about midway between how we do and the rest of the industry now. So, they've made up a lot of ground. And we have several that are growing, are actually doing better than last year, because they're very heavy in the north. And some markets that have been pretty shut down; Wisconsin was difficult for a period of time, it's a good market for them; New England, fairly good market, difficult for a period of time. Then, when you get to their more southern ones, not doing as well but are really closing the gap quickly. These are good experienced people that have been around the industry a long time and we haven't changed what they do day-to-day very much, but they do like what few changes they've been subjected to.

James D. Hope*Chief Financial Officer & Executive Vice President, Performance Food Group Co.*

A

I think that's important to say here, what George said there as well about the fact that when you think about a delta between Reinhart and the rest of the business, as it's happening right now and it's soon really coming to be – it's just one business, it's one food distribution company, and we're going to start letting that go. We won't think about a delta. We'll think about that one company performing well, and that one company is the Foodservice segment. So, those people fit so well that I'm not sure they're even bigger themselves as Reinhart or PFG were.

Frederick Wightman*Analyst, Wolfe Research, LLC*

Q

Okay, great. And then, Jim, you called out a \$12 million benefit from lower medical costs on the OpEx line. Was that a one-time benefit, is that something that we should sort of annualize going forward? Any help that would be great.

James D. Hope*Chief Financial Officer & Executive Vice President, Performance Food Group Co.*

A

Yeah. I can give you some color on that. I think there's a combination of things that happened. We actually paid our operators, paid a lot of attention to safety, and workers' comp, and health and welfare of our employees. And so did our employees, of course. Everyone was thoughtful about how they went about their job. And that helped improve our experience, right, in a very costly and painful part of the business, as well as the fact that we had less employees in the workplace and that helps with the congestion and frequency and risk also.

So, those two things combine nicely our attention and the number of folks combine nicely to give us a healthy benefit. As always, we want to be fully transparent and make sure that folks knew that and, at the same time, we're pleased to see that happen. I would think that it's probable that as we return to a robust period of growth and that will happen inevitably, we'll have more people in the workplace. We're going to continue to focus on safety and keep taking care of our employees. It's really important to us. I wouldn't see it as a one-time event, but I think there's a possibility that the magnitude could fade a bit over time.

Frederick Wightman

Analyst, Wolfe Research, LLC



Real helpful. Thank you.

Operator: Your next question comes from the line of John Glass of Morgan Stanley.

John Glass

Analyst, Morgan Stanley & Co. LLC



Hi. Thanks very much and good morning. I wanted to ask about digital and how your thoughts are maybe evolving or not evolving. Obviously, you need a different go-to-market strategy with respect to your sales force, but your key competitor is now raising the bar on digital. There's a lot of businesses that are more fully digitizing this business. One, is there a risk you might look back over time and say that actually was an opportunity our consumer – our customers are getting younger, they're more digitally savvy, and therefore we need to keep pace?

And can you talk about digital penetration as a percentage of sales? Among your big businesses, your broadline business, and Vistar is run different, and maybe did Reinhart have a different approach you could learn from, is there something you could teach them? How do you think about all of that combined, please?

George L. Holm

Chairman, President & Chief Executive Officer, Performance Food Group Co.



Yeah. Our digital business, what I would call just the customer facing the order themselves, that has always grown quarter-after-quarter. It's always been something that's gone up particularly early in the shelter-in-place. But throughout it, that actually went down for us. I think it's just a simple thing of customers having more questions and more issues to deal with and wanted somebody to talk to them. In some cases, they furloughed the person that enters the orders they didn't have anybody else to have to do it. It was that simple.

So, we got a little stall there. If you get outside of our independent, basically 100% of our business is done that way, in Foodservice, it's done digitally. Vistar is very close to 100% as a company, almost all of that is done digitally. Performance Foodservice and Reinhart are somewhat similar. I don't off hand know the percentages because they've gone down. So, it's just not sticking in my head. We did get learnings from Reinhart. We felt like their remote order entry system was better than what Performance Foodservice had. And soon, everybody will have the same one. And we feel it's a good system and it will really be effective. We hope that people continue to adopt it. And we are really careful that we don't force adoption of it. So, I'd like to think that we're going to it at the

rate in which our customers want that. I'm not sure that's not 100% the case, but that's our goal and that's what we continue to look to do.

John Glass

Analyst, Morgan Stanley & Co. LLC

Thank you.

Q

Operator: Your next question comes from the line of Lauren Silberman of Credit Suisse.

Lauren Silberman

Analyst, Credit Suisse Securities (USA) LLC

Thanks for the question. With light now at the end of the tunnel, can you share how you're thinking about the growth strategy in a post-COVID era and the composition of that growth across new business, wallet share expansion, M&A, do you think you can accelerate organic case growth levels relative to what we saw pre-COVID?

Q

George L. Holm

Chairman, President & Chief Executive Officer, Performance Food Group Co.

Well, we took a lot of pride in going – many years, many quarters in a row, we're – on the independent side, we grew our cases somewhere between 6% and 10%, and we fell off of that for a few quarters. Pre-COVID, we were back to those type of numbers. So, we went into this kind of back on track. I think we should then come out of it back on track and probably we'll compare our numbers more to 2019 than to 2020 because obviously those would be extremely soft comparisons.

A

When you get outside of our independent Foodservice business, I think in the chain area, we've got some good wins. We've got some that are pretty deep in the discussion period. I don't see us being really aggressive, like from an RFP standpoints or that, I mean, what we can go get and negotiate I think will be really important to us. We've always been a company that does a significant amount of chain business.

Then on the Vistar side, we've got some good plans around additional types of business that we can be in. Obviously, we're most focused on getting that business getting ready for the post-COVID world, but I think that they'll continue to grow above the numbers that were pre-COVID. Like I said, we have two categories there we worry a little bit about. And then, M&A, like I said, we've got a pretty good pipeline right now, nothing that I would say is today actionable, but we're encouraged. But it won't be...

Lauren Silberman

Analyst, Credit Suisse Securities (USA) LLC

Somewhat...

Q

George L. Holm

Chairman, President & Chief Executive Officer, Performance Food Group Co.

...I mean, we won't be any different than we were before, but...

A

Lauren Silberman

Analyst, Credit Suisse Securities (USA) LLC

Somewhat related to that, have there been any changes in restaurant customer behavior that you expect to stick, whether there's an increased willingness to have a smaller group of distributors, kind of I know you just spoke

Q

about digital perspective, any color? I know one of your competitors is talking about incremental opportunities of wallet share.

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

A

Yeah. Well, we always feel that the restaurateurs should buy from less people, it's more efficient. So, we like that as long as we're one of the ones they buy from, obviously. But there's changes I see. I think takeout is going to be certainly not what it is today, but takeout is going to be an important part of the business. And having a great disposable program and being really tuned into what the customers' needs are there, I think, is going to be real important. And third-party delivery goes right hand-in-hand with that. I think that's going to drop off and we'll have winners and losers in that, but it's here to stay. So, I think that's a change.

The purchasing behaviors of a restaurant, I really – I got to think that they've changed their habits for such a long period of time now that maybe that's the new habit, but maybe that's just being hopeful. But it's definitely a change.

Lauren Silberman*Analyst, Credit Suisse Securities (USA) LLC*

Q

All super helpful. And just kind of a last follow-up on January case growth trends. Any color you can share regarding consistency throughout the month from a restaurant perspective, we're hearing kind of some volatility related to both benefit from stimulus and perhaps from weather?

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

A

It's been a little volatile in January. I try always to be careful with the comments about January, because it's a soft month even when it's really good and our fiscal third quarter, calendar first quarter ends up quite often to be all about March. I guess, what I'm saying is, I've been at this a long time. I've had bad Januaries and really good third quarters, and I've had really good Januaries and not so good third quarters. So, keep – you just keep that in mind. But it has been improved and it has been volatile, both – both of those things.

Lauren Silberman*Analyst, Credit Suisse Securities (USA) LLC*

Q

Great. Thanks so much for the comments.

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

A

Thanks.

Operator: [Operator Instructions] Your next question comes from the line of William Reuter of Bank of America.

Q

Hi. This is [ph] Mary Ann (01:01:13) for Bill. Thanks for taking our questions. So, first, what are you seeing in labor inflation and what percent increase in wages are you expecting on a per employee basis?

George L. Holm*Chairman, President & Chief Executive Officer, Performance Food Group Co.*

Go ahead, Jim.

A

James D. Hope*Chief Financial Officer & Executive Vice President, Performance Food Group Co.*

Yeah. Look at the constant labor – excuse me – yeah, we are seeing some labor inflation. I'm not prepared to give the number and I certainly don't want to project in the future. But I can tell you one of the things that's helped us is, as George mentioned, we furloughed people with benefits and we brought them back as quick as we possibly could to take care of the business and to take care of them, of course. So, we'll manage it well. And I think I'll leave the answer at that. It's a tough one to predict. We've been through tough times before. So, I'm confident that our operators will be able to manage the crew and have the supply chain running smoothly.

A

Q

Got it. And do you expect that food cost inflation will contribute to gross margin expansion? And if so, how much?

James D. Hope*Chief Financial Officer & Executive Vice President, Performance Food Group Co.*

Yeah, it typically does. And we talked about the current inflation rate we have right now. We're very in tune with inflation and the cost of product daily. Difficult to predict where it will go, but I can tell you we'll be watching it and we'll be ready.

A

Q

Great. Thank you so much.

Operator: Your next question comes from the line of Carla Casella of JPMorgan.

Carla Casella*Analyst, JPMorgan Securities LLC*

Hi. A couple questions. On the – have you changed your leverage target or do you expect to at least get the low 4 times? I guess the target would be by mid-next year given what the original was, is that correct?

Q

James D. Hope*Chief Financial Officer & Executive Vice President, Performance Food Group Co.*

Yeah. We haven't changed our thinking around leverage and our targets. We've talked about how we like to be in a typical run rate in a normal economy, a normal environment anywhere between 2.5 times and 3.5 times absent a major acquisition. That's still where we'd like to be. And the numbers you just mentioned do make sense.

A

Carla Casella*Analyst, JPMorgan Securities LLC*

Q

Okay, great. And then, if you had Reinhart in for a full-year, I guess, prior to the pandemic, I'm trying to understand how big the theaters and office segments would have been as a percentage of revenue. Can you give us any sense for that?

James D. Hope

Chief Financial Officer & Executive Vice President, Performance Food Group Co.

A

Yeah. We haven't actually disclosed that number before. But we like that business, we appreciate it. It's helpful, but it is immaterial.

George L. Holm

Chairman, President & Chief Executive Officer, Performance Food Group Co.

A

No, it's not at all.

Carla Casella

Analyst, JPMorgan Securities LLC

Q

Okay. And then, just one last one. Did you – I may have missed it, did you provide what Reinhart's organic growth would have been in the quarter?

James D. Hope

Chief Financial Officer & Executive Vice President, Performance Food Group Co.

A

No, we did not.

George L. Holm

Chairman, President & Chief Executive Officer, Performance Food Group Co.

A

We did not.

Carla Casella

Analyst, JPMorgan Securities LLC

Q

Okay. Can you say whether it's similar in terms of trends with any of your existing businesses?

George L. Holm

Chairman, President & Chief Executive Officer, Performance Food Group Co.

A

Well, I think what I could say is best we can determine we share our numbers, and like I said, the information we get it's outside of our company, is not the entire industry, but it's a big portion of it. And that they've gone from trending with the same as the rest of the industry to about halfway between how we're doing and the rest of the industry. So, they're making some good progress. And it appears as if the rest of the industry is, for last quarter, were somewhere in the low-20% declines. So, I think you can kind of figure it out from there.

Carla Casella

Analyst, JPMorgan Securities LLC

Q

That's really helpful.

George L. Holm

Chairman, President & Chief Executive Officer, Performance Food Group Co.

A

Okay.

Carla Casella

Analyst, JPMorgan Securities LLC



That's great. Thank you very much. That's all I had.

Operator: That was our final question for today. I'll now return the call to Bill Marshall for closing comments.

William Marshall

Vice President-Investor Relations, Performance Food Group Co.

Thank you for joining our call today. If you have any follow up questions, please contact us at Investor Relations.

Operator: Thank you for participating in PFG's fiscal year Q2 2021 earnings conference call. You may now disconnect your lines and have a wonderful day.

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