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United Natural Foods, Inc. NYSE:UNFI

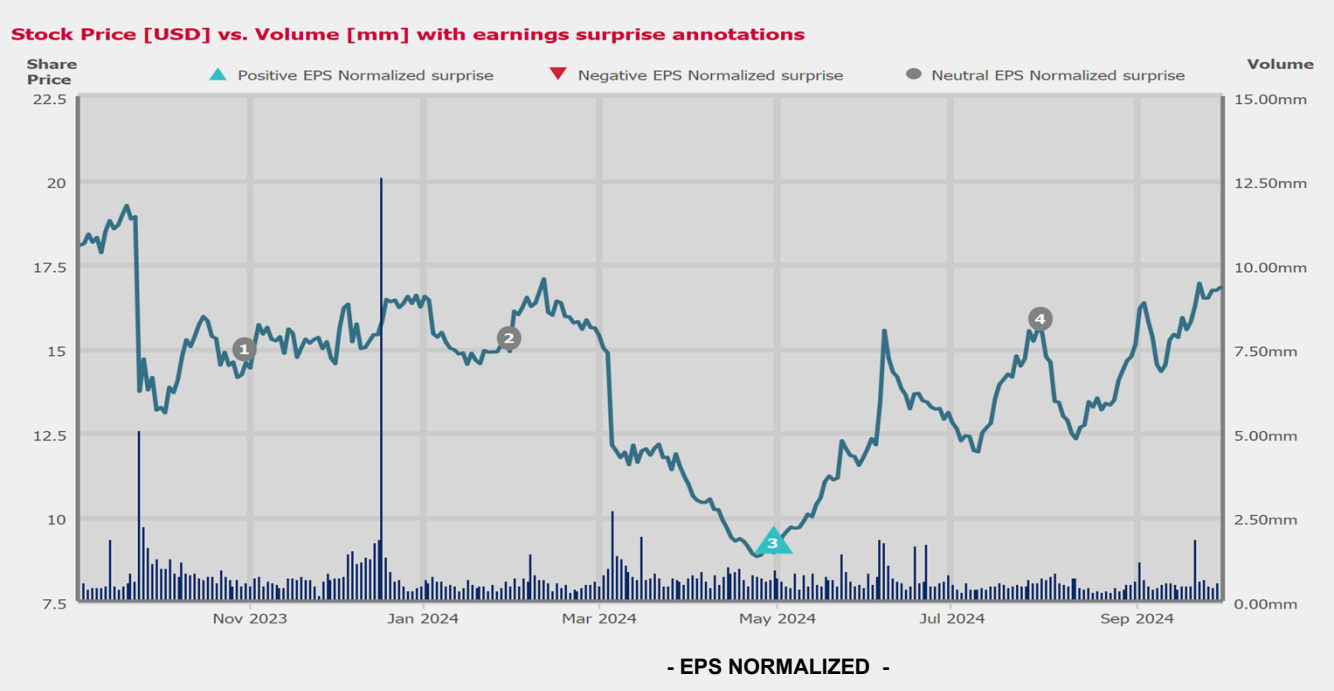
FQ4 2024 Earnings Call Transcripts

Tuesday, October 1, 2024 12:30 PM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2024-			-FQ1 2025-	-FY 2024-			-FY 2025-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS
EPS Normalized	(0.07)	0.01	NM	0.09	0.04	0.14	250.00	0.51
Revenue (mm)	7944.47	8155.00	2.65	7627.48	30745.55	30980.00	0.76	30717.36

Currency: USD
Consensus as of Oct-01-2024 1:10 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2024	(0.34)	(0.04)	NM
FQ2 2024	(0.02)	0.07	NM
FQ3 2024	0.03	0.10	233.33 %
FQ4 2024	(0.07)	0.01	NM

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Presentation

Operator

Hello, and welcome to the UNFI Fiscal 2024 Q4 Earnings Call. [Operator Instructions] I would now like to turn the conference over to Mr. Steve Bloomquist, Vice President of Investor Relations. You may begin.

Steven J. Bloomquist
Vice President Investor Relations

Good morning, everyone. Thank you for joining us on UNFI's Fourth Quarter Fiscal 2024 Earnings Conference Call. By now, you should have received a copy of the earnings release issued this morning. The press release and earnings presentation, which management will speak to, are available under the Investors section of the company's website at www.unfi.com. We've also included a supplemental disclosure file in Microsoft Excel with key financial information.

Joining me for today's call are Sandy Douglas, our Chief Executive Officer; and Matteo Tarditi, our President and Chief Financial Officer. Sandy and Matteo will provide a business update, after which we'll take your questions.

Before we begin, I'd like to remind everyone that comments made by management during today's call may contain forward-looking statements. These forward-looking statements include plans, expectations, estimates and projections that might involve significant risks and uncertainties. These risks are discussed in the company's earnings release and SEC filings. Actual results may differ materially from the results discussed in these forward-looking statements.

And lastly, I'd like to point out that during today's call, management will refer to certain non-GAAP financial measures. Definitions and reconciliations to the most comparable GAAP financial measures are included in our press release and the end of our earnings presentation.

I'd ask you to turn to Slide 6 of our presentation as I turn the call over to Sandy.

James Alexander Miller Douglas
CEO & Director

Thanks, Steve, and thank you, everyone, for joining us this morning. As you've seen in our release, we delivered fourth quarter results that drove fiscal 2024 performance to the upper end of our previously provided outlook. This capped a year in which we significantly strengthened our foundation and built momentum as we enter fiscal 2025.

During fiscal 2024, we drove strong same customer growth, extended our agreement with our largest customer until mid-2032, realized approximately $150 million in benefits from structural efficiency initiatives, significantly reduced shrink, lengthened the maturity on our term loan until 2031 and onboarded our new President and CFO, Matteo Tarditi.

We are confident that our new strategy and multiyear financial objectives, informed by our ongoing Board and management-led financial review, will continue to drive accelerating performance and create sustainable value for our customers and suppliers alongside our shareholders.

Today, I will go into more detail around our new strategy, business plan and the 3-year financial objectives that we expect to deliver by executing this strategy. As I outlined in our last call, our analysis of our current and potential customer base has identified a resilient portion of the industry that totals over $90 billion of wholesale sales today and includes many specialty, natural, ethnic and conventional operators.

This market segment is expected to grow at a low single-digit rate over the longer term and will likely be led by natural and specialty volumes. We are highly focused on this industry segment as it capitalizes on UNFI's strengths, including our heritage in natural and organic products, which grew around 5% in Q4 on a comparable 13-week basis compared to the prior year and are growing even faster so far in Q1.

Natural customers are broadly performing strongly. Customers are also gaining value from UNFI's margin-accretive digital and professional services business. We are actively positioning ourselves to add value to our customers and suppliers through a differentiated portfolio of products, services, programs and insights that help them both grow their businesses and succeed in a dynamic marketplace.

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Simultaneously, we're working to improve free cash flow by focusing on what we can control to become a more efficient organization, optimize our distribution center network and reduce the capital intensity of our business, enabling steady deleveraging. We expect these 2 elements of our strategy will work together to help us generate meaningful value creation for our key stakeholders, including our shareholders.

Let me take a few minutes to explain our new strategy in greater detail and provide a few early proof points around execution. I'll start with adding value. Our new strategy focuses on providing retailers with a strong value proposition, composed of an increasingly relevant portfolio of differentiated products and value-added services that help them grow profitably while offering suppliers the right go-to-market services and insights that help them grow within UNFI's large, diverse retailer network totaling over 30,000 customer locations.

For example, our revamped commercial go-to-market program for suppliers is a new partnership model that aligns our mutual interest around growth and makes doing business together easier. We streamlined 15 to 20 unique fees into one and are now providing suppliers access to our enhanced data and insights. The result is more value for suppliers and ultimately, more tools to help them invest and grow their brands faster and more profitably with UNFI's retailer base.

We have a sizable base of suppliers, including some of the largest CPGs in North America that are now enrolled in the new go-to-market model and are already seeing early returns, faster growth and less friction.

Our value-added digital and professional services portfolio is another differentiator that will increasingly be important to both customers and suppliers, offering mutually compelling economics for them and UNFI. We continue to add offerings to our sizable services portfolio that leverage our competitive advantages through UNFI's scale, relationships, data, programs and insights to help our retailers and suppliers more effectively meet their consumers' needs.

This includes our recently launched UNFI Media Network or UMN for short, which I described last quarter. We're seeing a lot of interest in UMN and are continuing to enroll both retailers and suppliers on to the platform. We expect to develop, continue to invest in or partner to provide other similar capital-light services in the future, which we believe will bring value to customers and suppliers while helping us drive margin expansion. We know that bringing value to our upstream and downstream partners will continue to make UNFI an attractive partner.

In parallel, the second element of our strategy is focused on shaping a more efficient distribution center network to better serve our customers and suppliers, lowering our cost structure and reducing capital intensity, which we expect will drive improving profitability, free cash flow generation and reduced leverage. We also expect these moves will help us increase process capability, service levels and responsiveness and enable us to strengthen our broader business, which should enhance the customer and supplier experience.

Over the last few months, we've executed some of our initial work on the network and optimizing to streamline operations and consolidate volume, focused on our conventional distribution business. In our Central region, we're moving volume from our Billings and Bismarck DCs into nearby facilities. Once we close these 2 DCs, all Bismarck customers and most Billings customers will transition to our nearby Fargo DC with the remainder transitioning to our Commerce, Santa Fe Springs and Centralia facilities.

We own the real estate in both Billings and Bismarck and are actively marketing these properties. And we'll use the proceeds to repay debt. These moves are expected to improve the customer experience in the region by leveraging our advanced DC technology solutions, including our modern cloud warehouse management system and case scanning technology.

In conjunction with our focus on employing rigorous lean management practices, emphasizing process, production and preparation, we expect this transition to deliver better quality, service and operational efficiency to both our customers and suppliers. In addition, our Fargo DC will provide customers with access to a broader product assortment and enable suppliers to reach more customers out of a single DC.

Actions like this result in both customer and supplier benefits and help to reduce the capital intensity of our conventional network while lowering our operating costs. Importantly, we see further opportunities to streamline our supply chain footprint. We will be working to evaluate and take action similar to what we've done in Billings and Bismarck over the next couple of years to consolidate volumes, generate operating savings, sustainably improve cash flow generation and potentially generate cash from asset sales, all while improving the customer and supplier experience.

We are extending our focus on reducing capital intensity beyond network optimization to improve the way we invest our capital. As you saw in our press release, we expect fiscal 2025 capital investments to be around $300 million, a decline of $70 million compared to fiscal 2024. This reduced intensity is being driven by a shift in spending based on asset utilization and wear and tear rather than

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a calendar approach where maintenance dollars get spent on a regular cadence with less focus on need. As we improve capital allocation, we will continue to prioritize safety and service levels.

Additionally, we are focused on reducing our investment in working capital and are seeking to improve capabilities to return our inventory days on hand to pre-pandemic levels. We expect to reduce days on hand by around 2 days during fiscal 2025 and have introduced processes to more efficiently manage this on an enduring basis.

To provide structure and ensure discipline, we have created a value delivery office. This group reports to Matteo and is charged with project managing and problem-solving on key initiatives and the progress being made against defined timelines and expected benefits. It is also focused on ensuring progress achieved is maintained through lean management practices and structural process improvements.

Turning to Slide 7. From a financial perspective, our new strategy and 3-year financial objectives are expected to result in revenue that is roughly flat as organic growth offsets the revenue impact of network optimization.

We will be focused on increasing UNFI's share of the resilient $90 billion priority market segment and expect overall margin expansion over the next 3 years to be driven by, first, faster growth in our higher-margin natural business compared to our conventional business, partially reflecting the prioritization of products we believe will help add value for retailers, particularly in our priority market segment as well as projected secular trends. As I mentioned earlier, our natural, organic and specialty business is growing strongly and represents the majority of our distribution profitability.

Our second margin driver relates to the benefits from our multiyear efficiency initiatives introduced on our last call, which are expected to approach a similar magnitude to the $150 million we realized in fiscal 2024. And lastly, growth from our digital and professional services, which add value to customers while carrying higher margins for UNFI.

As a result, we expect our average annual adjusted EBITDA growth rate over the next 3 years to be in the high single-digit range. We expect adjusted EPS growth to outpace that of adjusted EBITDA as we target net leverage reduction to 2.5 turns or less by fiscal year-end 2027 and benefit from lower interest expense. This reduction in net leverage is expected to be driven by higher adjusted EBITDA as well as strong free cash flow generation, which we plan to direct towards repaying debt.

Once we complete the initial execution of our planned key strategic initiatives over the next couple of years, we expect to generate annual free cash flow of well over 0.5% of net sales. In fiscal 2025, we expect to generate around $100 million in free cash flow, about $200 million better than fiscal 2024, which Matteo will discuss in more detail.

These 3 financial objectives assume a generally stable operating backdrop. Our Board and management-led review remains ongoing. And we continue to evaluate value creation opportunities beyond this updated strategy as we execute and drive toward the improved metrics embedded in our 3-year financial objectives.

We reduced management layers in 2024, allowing for faster, more streamlined decision-making and improve the customer and supplier experience. This includes the reorganization and reprioritization of our digital organization in the fourth quarter that integrated digital capabilities throughout the business and increased digital scalability.

As we embed a lean continuous improvement mindset in the organization, we will identify more opportunities for improved efficiency. As I stated earlier, we enter fiscal 2025 with momentum and a large stable business with significant organic growth and free cash flow generation potential through optimizing controllable variables.

Our focus remains on helping our customers compete through our products, services, programs and insights while bringing value to suppliers through the 30,000 diverse customer locations that we service. We believe this focus on adding value to customers and suppliers to sustain organic growth while also driving improving recurring free cash flow generation will result in meaningful shareholder value creation over the short and the long term. We expect fiscal 2025 will be a year of delivering and deleveraging as we pursue our new strategy.

With that, let me turn it over to Matteo to discuss our Q4 results, outlook and continuous improvement and process transformation work. Matteo?

Giorgio Tarditi
President & CFO

Thank you, Sandy, and good morning, everyone. I'm pleased to join you for our year-end earnings call. As Sandy stated, we finished fiscal 2024 at the upper end of the revised outlook ranges we provided in June for sales, adjusted EBITDA and adjusted EPS. Today,

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I will provide additional insights into our fourth quarter operational results, our year-end financial position and capital structure, the management process changes we've implemented guided by lean principles and our outlook for fiscal 2025.

With that, let's dive into our 4Q results. Let's turn to Slide 9. Our fourth quarter sales came in at $8.2 billion, which included close to a $600 million benefit from the extra week in the quarter as fiscal 2024 was a 53-week year for UNFI. On a comparable 13-week basis, which excludes the additional week, fourth quarter sales grew approximately 2.1%. Our fourth quarter performance contributed to a full year sales increase of 0.4% on a 52-week basis.

In Wholesale, we again saw sequentially improving volumes as well as declining levels of inflation, continuing the trends we discussed on our third quarter call. Wholesale volumes viewed on a trailing 4-week basis compared to last year turned positive in Week 49 and trended higher each consecutive week for the balance of the fiscal year and ended the year up 2%. This continued volume improvement was largely driven by the natural side of our business, although conventional volumes improved as well, but at a slower pace. This volume improvement has also continued into early fiscal 2025.

At the same time, inflation decelerated modestly to approximately 1.5%. And we continue to expect inflation to gradually slow before leveling out later this fiscal year.

Sales in our Retail business continued to see pressure as many consumers in our operating markets remain highly price sensitive. Excluding the additional week, Retail sales improved from the third quarter but were still down by slightly more than 4% compared to the prior year. This decline was primarily attributable to lower same-store sales. Our team is working to execute a robust plan expected to drive improving top and bottom line performance in fiscal 2025 and beyond.

Moving to Slide 10. Let's review profitability drivers in the quarter. Our gross margin rate, excluding LIFO, was 13.5% in the fourth quarter. We have now broadly cycled a period of large year-over-year declines in procurement gains and would expect margins to be comparable going forward.

Within our business segments, both our Wholesale and Retail gross margin rates were up compared to last year. Our improved Wholesale margin during Q4 includes the benefit of the shrink and margin initiatives we focused on during the year and more than offset our commercial investments and lower procurement gains. We are close to pre-COVID shrink levels and are working to drive shrink expense even lower as one of our efficiency initiatives, which I'll touch upon in greater detail shortly.

Last quarter, we spoke about focusing our efforts on what we can control. And within an environment that remains challenging, we improved our overall operating expense rate by around 30 basis points compared to last year's fourth quarter. This occurred despite a more normalized level of incentive compensation, which was about $12 million in the quarter, markedly higher than last year's fourth quarter when there was no material incentive compensation expense.

Within our operating expenses, we delivered another solid quarter of SG&A reduction as we further streamlined the organization and generated expense savings consistent with our strategic vision. The biggest driver of improvement was a broad-based reduction in labor expense, partly through spend in layers, which has reduced its total head count by around 4% since the end of last year. This also reflects some benefits from the actions we took to streamline and increase the scalability of our digital platform, which Sandy described in his remarks.

Adjusted EBITDA for the fourth quarter was $143 million compared to $93 million in last year's fourth quarter. This included an approximate $10 million benefit from the additional week, higher sales on a comparable 13-week basis and strong execution against our near-term cost savings initiatives. This was our fourth consecutive quarter of sequentially higher profitability, which means each quarter of adjusted EBITDA in fiscal 2024 was higher than the prior quarter in both dollar and rate terms, evidenced in the momentum with which we enter fiscal 2025.

This higher adjusted EBITDA during Q4 more than offset higher interest expense primarily driven by higher average interest rates. This led to adjusted EPS in the quarter of $0.01, which compares to a net loss of $0.25 in last year's fourth quarter.

Turning to Slide 11. Free cash flow in Q4 was $71 million, a decrease from last year as higher level of profitability was more than offset by higher capital expenditures related to the timing of payments for automation investments, higher cash interest payments and lower benefits from working capital changes compared to last year's fourth quarter. The change in working capital partially reflects the lower use of our accounts receivable monetization and similar programs as a result of a strategic shift focused on greater discipline, higher and more decentralized accountability and minimizing ongoing working capital use. We expect to employ vehicles like the accounts receivable monetization program less over time as we prioritize organic free cash flow generation.

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The $71 million of free cash flow in Q4 enabled us to reduce net debt to under $2.1 billion and net leverage to 4.0 turns, a decline of 0.6 turns from Q3. As Sandy highlighted earlier, we remain on track with our longer-term goal to reduce net leverage to under 2.5 turns by fiscal year 2027, and we'll continue to look for opportunities to accelerate this.

Moving to Slide 12. Since I've joined UNFI, we began the process of introducing a more detailed framework to manage and forecast free cash flow based on my previous experience and success in doing so. Previously, leaders and teams at UNFI have largely been focused on driving sales and profitability.

To better incentivize free cash flow generation, we have embedded this metric in the goals and objectives for our broader organization as part of our fiscal 2025 incentive planning process. As Sandy detailed in his remarks, improving free cash flow is an important focus of the financial review. And we have identified meaningful controllable levers that we believe will enable us to return to generating significant free cash flow starting in fiscal 2025.

Obtaining this sustained improvement in free cash flow generation will depend on rigorous daily management routines and action plans, which we have already put in place and helped us close out fiscal 2024 strong and set us up well for fiscal 2025. Daily management routines are one way that lean practices are already benefiting our organization.

We have completed the initial phase of lean training for our senior leadership team and have begun to more broadly roll this out across our organization. Associates will get a stronger sense for how daily actions and decisions influence how cash moves into and out of the organization.

We will more aggressively set operating metrics and goals across the company and more frequently measure results against these goals so corrective actions can be taken quickly where appropriate and more real-time learning can be reflected. We will look to balance short-term cost savings wins with longer-term breakthrough accomplishments that will further position UNFI for future success.

As for fiscal 2025, our goals this year are based on defined short- and long-term benchmarks that advance our long-term vision and drive a high do to say ratio of continuous improvement across all dimensions of the organization.

Looking at Slide 13. We have closed fiscal 2024 at the upper end of our previous guidance and are highly focused on generating continuous improvement in our financial performance in fiscal 2025. As outlined in our press release, the guidance ranges and increases compared to fiscal 2024 include sales that are expected to be in the range of $30.3 billion to $30.8 billion, an increase of 0.5% at the midpoint when adjusting for the 53rd week in fiscal 2024; an expected range for adjusted EBITDA of $520 million to $580 million, an increase of 8% at the midpoint on a comparable 52-week basis.

We expect our overall adjusted EBITDA margin rate to sequentially expand from Q1 to Q4 with first quarter adjusted EBITDA dollars expected to grow in the mid-single digits compared to the prior year first quarter. This reflects the cadence of actions we plan to take in fiscal 2025 executing our revised strategy and how they will benefit results over the year.

As Sandy mentioned, we're focused on generating annual adjusted EBITDA margin expansion. In our revised strategy, I could see fluctuations quarter-to-quarter: an adjusted EPS range of $0.20 to $0.80 per share, an increase of over 3x at the midpoint when adjusting for the 53rd week in fiscal 2024.

We continue to expect capital spending, including dollars for cloud implementation to be approximately $300 million, down from the $370 million spent in fiscal 2024. Our CapEx plan include one automation project, continued investments in safety and usage-based maintenance spending as well as the completion of our Sarasota DC, already under construction.

We believe we will be able to generate approximately $100 million in free cash flow, up almost $200 million year-over-year, which we plan to allocate to reducing net debt and improving our leverage. As Sandy stated, our longer-term goal is to generate recurring free cash flow of well over 0.5% of sales.

Note that these guidance ranges are all based on what I will call steady-state operations, which also applies to the longer-term metrics Sandy provided earlier. As Sandy mentioned, we made a strategic decision to close 2 owned distribution centers, which we expect will generate cash for us, save on future operating costs and provide the customer benefits he spoke to.

We will continue to evaluate other opportunities along these lines but have not yet included any incremental strategic initiatives in our outlook. This outlook for fiscal 2025 is the first year of the 3-year business plan and financial objectives Sandy described earlier. We will be focused on executing this year so that we can fully realize our financial objectives and continue to better realize the significant value creation and organic growth potential embedded in our large, stable $30 billion-plus business.

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Flipping to Slide 14. We took decisive action to strengthen our foundation during fiscal 2024 and expect to drive continued improvement in fiscal 2025 as we strive to become a more efficient business partner to retailers and suppliers to benefit from the full advantage of all the products and services we bring to the market.

Having been here for over 5 months now, I'm even more confident about the future of our company and the returns we can generate for our shareholders. There is so much opportunity to create value from improving processes and generating efficiencies, which is a vital aspect of my prior experience. We expect fiscal 2025 to be a year of delivery and deleveraging. I look forward to updating you on our progress.
With that, operator, please open the line for questions.

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Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of John Heinbockel with Guggenheim.

John Edward Heinbockel
Guggenheim Securities, LLC, Research Division

Sandy, I wanted to start with your view on the role of conventional in the portfolio, right? Because you said most of the profitability comes from natural, and that business is growing.

So the role of conventional, and I know to get to flat revenue, it means that you're probably giving up $1 billion or $1.5 billion somewhere. So there will be more closures beyond Billings and Bismarck, I assume. And do you think you managed conventional accounts out of the system in warehouses that you don't close? Is that part of this as well?

James Alexander Miller Douglas
CEO & Director

I think our view of our product portfolio is more broad-based in the sense that we seek to have the products that our customers need and want. What you see in our network rationalization is an effort to make sure that our supply chain is as efficient as possible and that all of the capital that we have invested is generating the best returns.

Ultimately, the consumer clearly is trending towards natural and better-for-you products. So that's a big focus of ours and also part of our heritage. But at this stage, we're designed for the customers we serve. And we believe inside the addressable market we talked about, there will be material amounts of both conventional and natural products.

John Edward Heinbockel
Guggenheim Securities, LLC, Research Division

Okay. And then maybe for Matteo. Can you speak to -- right, there's sort of 2 sides of the labor productivity aspect here, right? So number one, wage rate inflation, right? Do you think that is -- is that a 3% to 4%, 4% to 5% inflation rate going forward just given supply-demand?

And then the flip side of that is the productivity you can drive in cases per labor hour, right? And is the idea to offset the two? Where do you think the lean productivity gains can be in excess of your wage rate inflation?

Giorgio Tarditi
President & CFO

Yes, John, thank you for the question. Two things. So first of all, our goal is always through productivity and throughput to more than offset the pressure from inflation. So while you are correct, without necessarily pinning down a percentage point, that we will see some pressure between renegs and inflation on labor.

But our goal through lean, and we have some good proof points already is to continue to remove waste, improve the number of cases per hour and how do we continue then to drive productivity out of the large distribution center network. So in midterm, long term, the plan is clearly to continue to offset any labor pressure from a cost standpoint with more productivity.

Operator

Your next question comes from the line of Leah Jordan with Goldman Sachs.

Leah Dianne Jordan
Goldman Sachs Group, Inc., Research Division

Just seeing if you could walk us through the puts and takes to gross margin in your '25 outlook. How much could vendor promotions be a tailwind in the coming year? What are you seeing there? And how should we think about procurement opportunities, given your inflation outlook for some deceleration and then stabilization?

Giorgio Tarditi
President & CFO

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Yes. Thank you. So a couple of thoughts here. First of all, on the general guidance, we're looking at kind of high single-digit growth in the long term. And we're guiding $520 million to $580 million on EBITDA with a midpoint of $550 million.

Relative to gross profit, so what we expect is that, obviously, actions like shrink that have given great results and great benefits in 2024 will continue into 2025. And we also expect the pressure from mix to -- from customer mix to continue into 2025 broadly kind of balancing between these two.

As Sandy mentioned, part of the DC network optimization is going to help us remargin the business. That is going to be probably through '26 and '27. But relative to 2025, so on the specific question of gross profit, we expect to see some balance between the benefits of gross profit and -- sorry, the benefit from shrink and the pressure from mix.

Relative to promotions, we still don't see promotions going back to kind of the pre-pandemic levels. So for now, we have modeled some level of improvement but not kind of significant improvement back to the pre-pandemic levels. Sandy, I don't know if you want to add to that?

James Alexander Miller Douglas
CEO & Director

Yes, I think you covered the wholesale view really well. I think the added point would be that our digital and professional services give us a margin tailwind because they create value for our customers, and they're higher margin for us. And so they're a big part of our focus, which is a big part of our go-forward margin strategy.

Leah Dianne Jordan
Goldman Sachs Group, Inc., Research Division

Great. And just for my follow-up, I just wanted to see if you could provide more detail on the retail segment. What demand trends are you seeing within your banners there and the competitive environment where you operate? And how important is that business to supporting your Wholesale business as well?

James Alexander Miller Douglas
CEO & Director

Yes. I mean our retail business, think about it as a Minnesota, Twin Cities business. It's the Cub brand. It's a market leader in the Twin Cities. It's had some challenging performance over the last couple of years.

We have a new team in there that's building a new strategy, working closely with our franchisees. And we're optimistic that Cub will be a strong player for years to come, and there are a number of initiatives that are underway to improve the performance there.

From a competitive standpoint, Cub is competing against the widest range of local and national players. And like many, they're pursuing differentiation strategies to improve the performance.

And again, I mentioned the franchisees up there. We've got a unique structure. It's very collaborative. And I think we're increasingly constructive on the plan that's being built.

Operator

Your next question comes from the line of Mark Carden with UBS.

Mark David Carden
UBS Investment Bank, Research Division

Great. So in your 3-year plan, you're prioritizing natural, organic, which makes a lot of sense. Digging into what you're doing on conventionals, though, how are you thinking about the balance of growth between independent conventionals and chains over the next few years? Would you expect one to grow much faster than the other?

James Alexander Miller Douglas
CEO & Director

Mark, it's hard to generalize. And I'm not dodging the question. We find performance amongst our 32,000 approximate retail base to vary literally from one segment to the other based on the retailer and their positioning.

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What we see is, yes, the natural and organic and specialty retailers are growing faster right now. But we also see really well-positioned retailers in ethnic and other sort of specializations doing quite well as well. And some of them are one store operators who are just brilliant merchants, and others are larger.

So you can find across our entire customer base winners and then those who are going to win in the future. And our job is to try to help all of them from wherever they are do better tomorrow than they did yesterday. But you'll really see winners all over the market.

Mark David Carden
UBS Investment Bank, Research Division

Okay. That makes sense. And then on your higher-margin professional services, how is traction trending for your natural and organic business? I know historically, it's been more geared towards conventional, but are you seeing any signs of a step change on that front?

James Alexander Miller Douglas
CEO & Director

Yes. Well, the services business, as you said, was a -- it originated with a more conventional focus, but we've been ramping it up across our customer base. Services continue to significantly outgrow our general business.

And as I mentioned earlier, we're very bullish about the services business and generally think about it is any place where we can add capability, insight or scale to customers, either technology or products and services that they don't resell. And then typically, what we do is we aggregate, we help them on board. And retail media network is the latest example. And we're seeing interest across both the conventional and the natural customer base.

Operator

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

Edward Joseph Kelly
Wells Fargo Securities, LLC, Research Division

My first question, just as it pertains to the 2025 as we think about like the first year of this leg of multiyear high single-digit EBITDA growth, I think, but you tell us the back half of '24 and what is an improved level of EBITDA growth already kind of locks in, it seems like a portion of that growth in '25. Is that correct?

James Alexander Miller Douglas
CEO & Director

Ed, what I would say, and this was in Matteo's remarks, is the high single-digit compounded growth rate is the guide for the 3-year plan and is also the guide for fiscal '25. We believe that it will build as the year starts.

Matteo said that he expected the first quarter and the early part of the year to be mid-single digits. And that's because the number of the BDO or productivity initiatives are being implemented in the first half, and will be building as we get into the second half.

So obviously, it's a multiyear story. Last year, a number of the initiatives were in very early, so they cycled through the whole year but have some benefit that come over to the new year. But think about the first half as mid-single digits and then the second half being sort of at the upper end to get to high single digits for the full year.

Edward Joseph Kelly
Wells Fargo Securities, LLC, Research Division

Got it. Okay. That makes sense. And I wanted to ask you about vendor promo and the trends that you're seeing there, the impact that it's having on your customers' ability to drive better volume and then the impact that it's also having on your own P&L. Can you maybe update us there?

James Alexander Miller Douglas
CEO & Director

Yes. What we're seeing is promotions are starting to continue to come back. They're still below pre-pandemic levels. Consumer products companies spending is -- obviously varies by the company, but they're continuing to grow.

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As Matteo alluded to, units are starting to improve slightly. And we see growth-oriented energy from our suppliers continuing to grow. The impact to our company is that we benefit when suppliers promote because we service all of that for them through to our customer base, and our customers obviously benefit. And our merchants are very focused on driving the maximum amount of spend through to our customers.

I also mentioned the new program that we've developed over the last year for suppliers called the supplier go-to-market program, where we're trying to simplify a lot of the way we used to operate by reducing 15 to 20 fees into one and providing suppliers data so that they can be more laser like in the way they spend their trade dollars to help our customers grow, particularly the smaller of our customers who typically don't get called on by suppliers, which opens up new growth and profitable growth for suppliers and more investment for our customers.

Operator

Your next question comes from the line of Andrew Wolf with CL King.

Andrew Paul Wolf
CL King & Associates, Inc., Research Division

Could you provide more color on what drove the step-up in volume intra-quarter and I think you said currently? I know the press release referenced new customers and also increased penetration, just sort of maybe a lot that between those two things. And also was the increased volume kind of uniform across the customer segments? Or is it more concentrated with supernatural, for example?

James Alexander Miller Douglas
CEO & Director

So beyond the reported segments is probably as deep as I'll go into specific customers, Andy. But clearly, we saw natural, organic and specialty growth accelerate significantly in the fourth quarter. And it's continued to accelerate further in the first quarter.

We saw natural -- conventional in general start to improve but at a slower rate. And then I would describe the sort of differentiating growth for us was the expansion that we had with existing customers, where we expanded the work that we do in a couple of customers that were bigger and then in a number of them that were smaller. So they -- the all 3 of those were playing a role: broader industry factors, the success of our customers and then our expansion with certain customers.

Andrew Paul Wolf
CL King & Associates, Inc., Research Division

Got it. Okay. That's helpful. And just probably more for Matteo. Can you just tell me how kind of square if you're running 2% or better sales at least in the quarter, and it sounds like maybe now, but you're guiding to midpoint up 0.5%. I mean is the difference all network optimization? Or is there other expectations in there for maybe volumes to settle down a little less or inflation to come down? Just trying to understand that differential.

Giorgio Tarditi
President & CFO

Yes, that's a very good question. Thanks for asking. So a couple of thoughts here. So as we said in the script, starting in fiscal week 49, our volumes started trending favorably. And they are tracking favorably, as Sandy mentioned, primarily through the strength of the natural and specialty business.

And so far, this trend has continued into the year. I think it's very early. It's only second month of 12. But if this trend continues, it is possible that we're going to be able to outperform the midpoint of our outlook, which is why we're guiding $30.3 billion to $30.8 billion. $30.8 billion would imply 2% or so of kind of growth year-over-year, 3%, 4% on a case standpoint, on a case volume standpoint.

So we're trying to have a pragmatic and conservative approach to setting the outlook. I feel comfortable with the current outlook. And we believe that this $30.3 billion to $30.8 billion midpoint reflects a dynamic market backdrop. And if we see this volume sustaining, we will continue to relook at the forecast.

Now the thing that we got to bear in mind is that while again we see the volume improving, we are going to continue to look at the DC playbook and the network optimization. And so we will continue to balance what we see in terms of growth on the organic and specialty with the fact that we may see contraction in revenues coming from DC closures.

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Andrew Paul Wolf
CL King & Associates, Inc., Research Division

Okay. And is any more closures kind of contemplated in the guidance? Or is that still to be determined just what you already did is in there?

Giorgio Tarditi
President & CFO

Yes, still to be determined. So Billings and Bismarck are announced and ongoing. And then we continue to look at opportunities to serve the customers while improving our operating efficiency and cost position.

Operator

Your next question comes from the line of Kelly Bania with BMO Capital Markets.

Kelly Ann Bania
BMO Capital Markets Equity Research

Can you just help us understand the network optimization strategy a little deeper in terms of the magnitude of the sales impact that we should expect this year and in coming years? And should we presume that, that strategy impacts primarily chains or independents or both but not the supernatural channel? Can you just walk us through what the vision is there?

James Alexander Miller Douglas
CEO & Director

Kelly, it's Sandy. The network optimization strategy is a core part of our 3-year plan. And the way to think about it is how can we optimize the footprint, the capability from a technology as well as an automation, an assortment and efficiency perspective.

And we're really rationalizing a network that's been built over decades into a modern network that's fit for purpose for customers today. So it's principally focused on the conventional side of the business where a lot of the DCs have and legacy DCs are.

Most of the way our natural network has been built customer-backed anyway. But it's being enabled by technology and investments we're making in regional technology and DC technology. And it's all built around the metrics of excellent customer service, returns on capital and free cash flow.

The other point I'd make is we did announce 2 closures. We also have also announced a DC opening in Manchester, Pennsylvania, which is a significant expansion on an adjacent DC in York, which we will close. That is going to be employing all of our newest technology and will be automated sometime next spring.

So there's a lot involved in the strategy. There will be a net closure of DCs to improve returns on capital but always with customer metrics, first and foremost.

Kelly Ann Bania
BMO Capital Markets Equity Research

Okay. And can you just talk a little bit more about customer feedback on the new fee structure and how your fee structure -- this consolidated fee structure varies from competitors in the marketplace? And any impacts we should be considering in terms of volatility of margins or lack of volatility of margins or seasonality from this new structure?

James Alexander Miller Douglas
CEO & Director

Sure. A number of facets to that question. What I would say is that you should see our fees that we're collecting from suppliers be more consistent and allow for faster action by suppliers. I'll give you an example.

Suppliers who are enrolled in the program do not pay slotting fees. So once we decide together that an item is right for a DC, we get much faster with the goal of being faster or fastest to shelf. All of this strategy is designed to create value by earning retailer and supplier alignment for faster action and then to make the fee structure simpler and more consistent for suppliers and for us.

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From a competitive standpoint, you really need to ask our competitors. Our goal with suppliers is to be the most valuable distributor partner that they have and by doing so, help them see opportunity in our customer base and invest on it and then make the return that they're seeking so that it creates a virtuous cycle.

And it's early. We'll see how it goes. We have a number of suppliers that are enrolled today. I'd say we're kind of midstream in the implementation with more to come. And we're getting plenty of feedback on ways we can make it better, and we're listening and trying to do that as we go. But over time, it should show up more like a subscription and be more about growth and earn the suppliers' dollars and allow their promotional spend and retailer spend to flow directly through to the retailers.

Kelly Ann Bania
BMO Capital Markets Equity Research

Okay. That's helpful. And then just one other one for me. In terms of the professional services and digital services, I guess that means on the retail media side, can you just help us understand what percent of your customer base are engaged with some of these services today and what kind of growth you are planning in fiscal '25 and really over the next 3 years from these 2 components?

James Alexander Miller Douglas
CEO & Director

Yes. I'll give you a couple of ways of thinking about that. Some of our older, more analog services are highly penetrated. New services and digital services are new, and therefore, they're not penetrated highly.

We're seeing strong growth in services. We saw it for the last 3 years, and we expect it to only accelerate going forward. And we have a curation process where effectively whatever our customers need, and I'll use retail media as an example.

Retail media is going to be a $100 billion advertising business. Our customers didn't have access to it. We worked with a partner to create a facility where consumer products companies could invest into it and get the same kind of experience and returns on their investment that they have with some of the bigger players.

We have a team in professional and digital services that are looking for opportunities like that to drive penetration of existing services but then to figure out what's next so that our customers don't have to wait for years to participate in things that they would need to be successful.

Operator

Your final question comes from the line of Chuck Cerankosky with Northcoast Research.

Charles Edward Cerankosky
Northcoast Research Partners, LLC

We've got a repeated series of quarters here where the consumer is inflation-weary, very price sensitive, yet the United Natural management team sounds refreshingly confident about delivering and deleveraging. How sensitive to the economic environment do you think your recovery plan is?

James Alexander Miller Douglas
CEO & Director

Chuck, super good question. I think our recovery plan is focused on helping our customers be successful and taking the controllable self-help actions in our own business to make sure that we're healthy alongside.

Needs in the market are not a challenge for us, meeting them is and then taking the actions to make sure that our cost structure is managed tightly using, as Matteo outlined, lean principles and other management disciplines to make sure we're fit for purpose for the environment.

So the consumer is, as you said, very price sensitive. We're working very hard to give our customers the tools to appeal to the customer where they are. But our outlook is balanced in the environment that it's in.

Obviously, inflation has lowered down from a percentage growth standpoint, but prices are still high. Value is still important. Our Brands+ program is an important initiative there. But in terms of our own profitability growth, we are focused on the things that we need to do to control the controllables. And we built some confidence based on our performance in fiscal '24.

Charles Edward Cerankosky

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Northcoast Research Partners, LLC

Good. Sandy or Matteo, could you talk about the timing of selling those 2 distribution centers and what amount of cash you might get from them?

Giorgio Tarditi
President & CFO

Yes. Good question. Thanks, Chuck. So a couple of thoughts here. We are phasing down the operations, and we are starting the marketing process for these 2 facilities. We're being clear with the team that we're not going to trade time for value.

We do believe that there are good opportunities in the market up there. We're not going to rush into a transaction to cut economics. So we'll go through a disciplined process that we've implemented on both capital acquisitions and dispositions and provide an update as we go through the next few months. But again, we started the marketing process, positive response so far, and we'll go through that.

Operator

This concludes the question-and-answer session. I'll turn the call to Sandy Douglas for closing remarks.

James Alexander Miller Douglas
CEO & Director

Thank you, operator. We are focused on executing our new strategy, which, as I outlined earlier, emphasizes delivering value for customers and suppliers while simultaneously improving free cash flow and strengthening UNFI broadly.

We've already taken many actions that demonstrate that we're seeking to accomplish. And I'm confident in our ability to help customers, suppliers and in turn, UNFI grow and succeed.

Matteo has been a great addition to our leadership team. His emphasis on efficiency, free cash flow and process management is valuable as we embark on the first year of our 3-year plan, which I believe will create significant and sustainable value for our customers, suppliers, associates and shareholders.

With Matteo's onboarding, our senior leadership team is complete, well aligned and focused on driving operational improvement. The skill sets of the team are highly complementary. And it gives me confidence that we will execute our plan well.

For our customers and suppliers, we thank you for your continued partnership in the business we do together. For the UNFI associates listening today, our thanks to each of you for everything that you do for our business, our customers, our communities and each other.

And for our shareholders, we thank you for the trust that you continue to place in us. Thanks again for joining us this morning. I look forward to updating you on our progress in December.

Operator
This concludes today's conference call. We thank you for joining. You may now disconnect your lines.

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