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PRESENTATION

Operator

Good day, ladies and gentlemen, and thank you for standing by. Welcome to the J&J Snack Foods Fiscal 2023 Third Quarter Conference Call. (Operator Instructions) Please be advised that today's conference is being recorded. At this time, I would like to turn the conference over to Mr. Norberto Aja of Investor Relations.

Norberto Aja ***JCIR - MD***

Thank you, Michelle, and good morning, everyone. Thank you for joining the J&J Snack Foods Fiscal 2023 Third Quarter Conference Call. We will start in just a minute with management's comments and your questions. But before doing so, let me take a minute to read the safe harbor language.

Today's call contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. As such, all statements made on this call that do not relate to matters of historical facts should be considered forward-looking statements, including statements regarding management's plans, strategies, goals, expectations and objectives as well as our anticipated financial performance.

These statements are neither promises or guarantees that involve known and unknown risks, uncertainties and other important factors that may cause results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements.

Factors discussed in our annual report on Form 10-K for the year ended September 24, 2022 and our other filings with the Securities and Exchange Commission could cause actual results to differ materially from those indicated by the forward-looking statements made on this call today. Any such forward-looking statements represent management's estimates as of the date of this call, August 1, 2023.

While we may elect to update forward-looking statements at some point in the future, we disclaim any obligation to do so, even if subsequent events cause expectations to change. In addition, we may also reference certain non-GAAP metrics on the call today, including adjusted EBITDA, operating income or earnings per share, all of which are reconciled to the nearest GAAP metric in our earnings press release, which can be found in the Investor Relations section of our website.

Joining me on the call today is Dan Fachner, our Chief Executive Officer, along with Ken Plunk, our Chief Financial Officer. Following management's prepared remarks, we will go ahead and open the call for a question-and-answer session. With that, I would now like to turn the call over to Mr. Dan Fachner, J&J Snack Foods Chief Executive Officer. Please go ahead, Dan.

Daniel Fachner ***J&J Snack Foods Corp. - President, CEO & Director***

Thank you, Norberto, and good morning, everyone. We appreciate you joining us to discuss our fiscal 2023 third quarter results. I'd like to start by thanking our employees across all J&J segments for a record quarter. I am so proud of our team and their efforts to continuously improve on our business. Their hard work and dedication are allowing us to post record top and bottom line results and create added value for all our employees, partners and shareholders.

For the fiscal third quarter, revenue increased 12% to $425.8 million, and net earnings increased 124.8% to $35 million, led by strong gross margin performance and improved distribution expenses. Our gross margin initiatives and strategies are starting to gain momentum, helping us to drive improved profitability.

Like most of our industry, we are beginning to see cost inflation stabilize, and our pricing actions are now better aligned with costs. This, combined with improved margin mix and adding efficiencies in our manufacturing plants, should have us well positioned to deliver consistent margin performance. Ken will provide more details on our financial performance later in the call.

Today, I'd like to begin by talking about the operations and supply chain side of our business. As we have discussed in prior quarters, our team has been focused on several initiatives to create more efficiencies in our business and enhance our capabilities. Combined, these initiatives will help us transform how we operate as a company. Here's a quick update on these key priorities.

Our team has improved logistics management over shipping, warehousing and product distribution through our partnership with NFI. NFI now manages a 100% of our transportation network and is helping us improve truck capacity, minimize miles, reduce stops, enhance customer service, helping us lower shipping, handling and storage costs.

Next, we are transforming our warehouse network to simplify how we manage product through our warehouses. This includes the build-out of 3 geographically positioned regional distribution centers, adding freezer capacity, including more storage space for Dippin' Dots products in two of these three locations.

The first of these 3 RDCs recently opened in Terrell, Texas in June, and the other two locations are scheduled to open later this calendar year and early 2024. These initiatives will simplify our logistics network by moving from over 30 warehouse locations to less than 10, resulting in improved customer service and lower distribution costs.

Also, we have rolled out 6 state-of-the-art production lines, adding capacity to support growth in our key product categories such as pretzels, churros and frozen novelties. These lines are more automated, creating production efficiencies and higher output metrics, all aligned to support our growth opportunity in these core products.

Our operations team has implemented stronger discipline within the plan that is driving efficiency improvements in areas such as waste reduction, maintenance spend, SKU productivity and our utilization.

And we have improved our financial and operational foundation via the implementation of a new ERP system last year. This has enabled us to integrate processes and controls across our operations and is now providing better data to manage the key KPIs across operations, supply chain and finance. We expect to continue to see additional benefits from this initiative.

Together, these operational and supply chain initiatives are transforming our business and will play a pivotal role in reducing distribution and manufacturing costs and providing better service to our valued customers. One of our key strategy is to leverage the strength of our core products and brands to drive growth and improve profitability.

Our team is working across segments and channels to create new selling opportunities and drive innovation. I'd like to highlight a few of our brand priorities. Dippin' Dots is quickly penetrating new markets and gaining placements in new channels. One of our biggest growth opportunities is in the theater channel, where we are now in approximately 375 Regal theaters and actively testing with the other 2 largest theater chains.

Like we reported last quarter, we are leveraging our brand portfolio to create products like Dippin' Dots ICEE Cherry and Blue Raspberry, which is already the best new product launch for Dippin' Dots ever.

Finally, we are pursuing numerous vending opportunities as we find new ways to serve our customers. [Hola! Churros] has exceeded our expectations, with sales growing by over 19% in the most recent quarter and almost 30% year-to-date.

We now have significant market share and are confident in our ability to maintain our leadership position. We are finding growth opportunities that include bringing all our churros into the retail space in the fourth quarter and new business with major U.S. food distributors, QSR and fast casual channels.

SUPERPRETZEL is one of our most powerful brands, with endless potential it seems. In the fourth quarter, we will be launching SUPERPRETZEL BAVARIAN sticks, bites and mini dogs in the Food Service and Retail, creating new snack indications and solidifying our dominant position within soft pretzels. ICEE , it continues to benefit from a recovering theater industry as well as from its strong consumer appeal across a growing number of occasions.

There is recent momentum in the theater industry as attendance looks close to pre-pandemic levels and stronger movie releases are hitting the market. We continue to gain placement in QSR and are currently discussing a major opportunity with the club channel customer.

On the marketing side, a new campaign is currently being tested in the Atlanta market called Let the Kid Out. That includes out-of-home, [curve-in] and digital media support and is receiving very positive reviews. We continue to have strong plans to market and grow this brand across our portfolio.

We have really built a business balanced across multiple products, channels and customer segments, which together helps us adapt to changing consumer and snacking occasions. We manage this portfolio to maximize our growth opportunities across Food Service, Retail and Frozen Beverages segments. This quarter is a great example of our flexible business model and our capabilities to continue driving both sales and growth and profit growth.

Before transitioning to Ken, let me highlight a few additional insights within each of our business segments. Food Service continued its strong performance from prior quarters with sales up 11.9% to $255 million. SUPERPRETZEL BAVARIAN pretzel bite and Jalapeno-n-Cheese [bites] launched this quarter, and we gained placements of a SUPERPRETZEL BAVARIAN stick at a large family entertainment center.

Also, we launched Hola! chocolate-filled churros across Food Service, including incremental placements with distributors, cash and carry, national accounts and individual operators. We're also testing a significant opportunity with a large QSR customer, with full rollout scheduled in early calendar 2024.

Funnel Cakes Fries -- Funnel Cakes Fries are a big opportunity in QSR and casual dining, growing 10% in Q3. And Zaxby's , a fast casual restaurant chain with over 900 locations across the U.S., recently informed us that they will move from a test of our 5-inch Funnel Cake to a permanent menu item in Q4.

As it relates to the Retail segment, Sales were up 0.2% to $61.2 million. For the quarter, the consumer environment was a bit soft in the first couple of months as retailers and grocery stores reported lower traffic in their stores and smaller baskets. This trend did improve in June, but highlights the fluctuations we are seeing in Retail consumer spending.

We believe that impacted sales of soft pretzels and biscuits into Q3 as both were down 12.2% and 15.3%, respectively, compared to the prior year. We continue to see strong growth opportunities in Retail, especially in our SUPERPRETZEL, frozen novelties and churros. The SUPERPRETZEL brand continues to resonate with consumers, with purchases [stand up] 50% versus the year ago.

As previously discussed, we are currently launching SUPERPRETZEL BAVARIAN sticks, bites and mini dogs in the Retail, supported by strong sales plans and marketing. Frozen novelties continue to be an opportunity, led by Luigi's, Dogsters and ICEE stick as the performance of each product continues to outpace the category. Hola! Churros will begin shipping in the Northeast region this month as we bring this growing brand to Retail.

Moving to our third business segment Frozen Beverages, we saw a record Q3 sales of $109.6 million, reflecting the strong rebound in the theater channel as well as ongoing strength at our Mexico operations. There is a lot of excitement in the theater industry on the heels of stronger movie releases and higher food and beverage consumption per visit. Theater attendance is improving closer to pre-pandemic levels.

Beverage sales grew 26.1% in Q3, driven by 9% volume increases in the quarter. Our maintenance and service sales grew 5.5%. And equipment sales grew 17.1%, driven mostly by the continued Checkers rollout.

Finally, we continue to make progress growing consumption and placements in amusement, mass merchandisers and restaurants. As it relates to M&A, we continue to evaluate potential M&A opportunities that complement our brand portfolio and business model and that offer an attractive shareholder return.

Financially, we are well positioned to invest in growth when the opportunities align with our business model. In summary, I applaud the excellent work everyone across the organization is doing to improve every aspect of our business. I am confident that our team is aligned on our core strategies and executing the right initiatives to grow our business and improve our operations. We are well positioned in the market with a long-term focus on growing sales and profits and delivering shareholder returns.

I would now like to turn the call over to Ken Plunk, CFO, to review our financial performance. Ken?

Ken Allen Plunk ***J&J Snack Foods Corp. - Senior VP, CFO & Treasurer***

Thank you, Dan, and good morning, everyone. Like Dan, I am so proud of our J&J employees and their many contributions in helping us deliver a record quarter. We are executing the strategy across organization with a focus on driving top line and bottom line growth.

I am equally pleased with our ability to show marked improvements across most of our operational KPIs, including gross margin and distribution expenses. We believe that we have the [lifeline employees] to drive continued growth and deliver value to our shareholders.

I would like to take a few minutes to walk you through our results. Net sales for the quarter totaled a record $425.8 million, a 12% increase versus the prior period, and sales through 9 months totaled [$1.115 billion], a 13.7% increase versus the first 9 months of fiscal '22. The strong top line result was driven by growth across all 3 of our business segments and across most of our core products and reflects the health and resiliency of our business.

Our largest segment, Food Service, experienced a 11.9% increase in sales to [$255 million], representing [59.9%] of total company sales. This strong performance has resulted in healthy growth across the segment, including 176.4% increase in frozen novelties to [$47.4] million, which included an incremental $29.2 million in Dippin' Dots sales and showcases the benefits from the Dippin' Dots acquisition.

Also, a 19% increase in churros, a 13.6% increase in soft pretzels and a decline in handheld and bakery of 33.9% and 8.3%, respectively.

Moving to our Retail segment. Sales increased 0.2% to $61.2 million compared to the same period in fiscal 2022. Handheld sales increase 180.2%, driven by expanding growth in a major mass [merchandiser]. We did experience sales decline in soft pretzels, biscuits and frozen novelty of 12.2%, 15.3% and 0.4%, respectively, due to softness in traffic and basket size with retailers and grocery chains.

As it relates to our third segment, Frozen Beverages sales were at record $109.6 million or a 20% increase versus Q3 '22, led by strong growth across all 3 subcategories. Beverage sales increased 26.1%, led by gallon increases of 9%. Machine revenue increased by 17.1%, and maintenance revenue increased 5.5%, compared to the previous-year period.

As highlighted by Dan earlier, we made significant progress, including gross margins and distribution expenses, driving operating income growth of 127.2%, a $27 million improvement over last year. Starting with gross profit, Q3 gross profit improved to $142.9 million or [31%] increase versus the prior year.

Gross profit as a percentage of sales was 33.6% in Q3 2023 comparing favorably to 28.7% in Q2 '22 and was driven by a combination of better product mix, alignment of pricing and costs, production efficiencies as well as the stabilization of inflation pressures on the back of historic highs last year.

Overall, we experienced low single-digit inflation for the quarter. Cost of key ingredients, including flour, oil, dairy and meat, has declined. Though we are still experiencing double-digit inflation in sugar/sweeteners and mixes, which continues to impact products such as frozen novelties and churros.

Looking at expenses, total operating expenses increased $6.8 million or 7.7% and represented 22.2% of sales for the quarter compared to 23.4% in Q3 of 2022. Distribution cost was 10.4% of sales in the quarter, down sequentially from 11.3% and much improved from 12.7% in the prior-year period.

Our supply chain transformation initiatives, along with declining diesel prices and carrier costs, are starting to drive improvements in shipping efficiency, cost per truck and cost per pound. Marketing and selling expenses represented 7.4% of sales versus 6.3% in the prior-year period. And 74% in Q2 '23 and were driven primarily by the timing of spend for trade shows and sponsorships.

Administrative expenses were 4.4% of sales in Q3 '22 compared to 4.1% in Q3 '22 and 5.3% in Q2 of '22, driven mostly by the expected seasonal impact of adding Dippin' Dots. This led to an operating income of $48.3 million or 127.2% increase compared to $21.3 million in Q3 of 2022.

Adjusted operating income was $51.1 million or a 104.8% increase compared to Q3 '22. After the impact of income taxes of $12.6 million compared to $5.6 million in Q3 of fiscal '22, net earnings increased to $35 million, resulting in reported diluted earnings per share of $1.81 or $2.51 for the first 9 months of fiscal 2023. This compares to $0.81 per share and $1.56 a share in the prior-year period.

Adjusted diluted earnings per share was $1.92 for the quarter and $2.76 for the first 9 months compared to $0.95 per share and $1.72 in the prior-year period. Adjusted EBITDA increased 73.3% to $66.6 million from $38.4 million in the prior-year period, and our effective tax rate was 26.5% in the third quarter.

Looking at our liquidity position, we continue to maintain a healthy balance sheet, including [$70.2 million] in cash and marketable securities. In addition to the investments we are making across our business, we also continue to pay down debt of approximately $125 million when we acquired Dippin' Dots to $83 million at the end of fiscal Q3 '23.

And we intend to continue returning value to our shareholders via dividend payment, given the help of our balance sheet and our strong free cash flow generation.

We have ample availability under our revolver of approximately $132 million of additional bond capacity. This affords us added flexibility to strategically invest and support our business.

In summary, we are executing our strategy and key initiatives in setting the foundation to continue to grow. Our teams are aligned across the segments once we focus on growing our core brands, innovating and finding new opportunities in snacking occasions, cross-selling across our portfolio and channel and improving how we operate.

This combination is helping us improve performance throughout the P&L and positions us well to grab strong returns and shareholder value. I would now like to open the call to questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) The first question comes from Connor Rattigan with Consumer Edge.

Connor Rattigan ***Consumer Edge Research, LLC - Research Analyst***

So I guess just first things first, just on the top line, so obviously, results came in a little lighter than I think we folks have expected. So I mean, I guess, maybe could you guys sort of maybe break out what you saw there, maybe if anything came in ahead below your expectations? If you saw any topic of weakness or softness ahead of expectations there?

Ken Allen Plunk ***J&J Snack Foods Corp. - Senior VP, CFO & Treasurer***

Yes. Connor, this is Ken. Good question. Yes, let me break that down a little bit. Take the Food Service segment, and you've got to kind of break it in because there some different things going on here. So if you look at soft pretzels, frozen novelties, excluding Dippin' Dots, churros, that combination of products was up over 14%.

So somewhat aligned with I think what you would expect and what we would expect and ties into what we talked about and emphasizing [drilling] those core products.

If you look at handhelds and bakery, in handhelds, there's around $3.5 million in there that is a cost past-due, based on an agreement we have with one of our club channel customers. So that's -- the units stay the same, but we passed on deflation that we got, we passed it on to the customer.

Also, when you think about bakery and handheld, the big part of our business is sold through retail. And as we talked about in the Retail segment, the retail industry saw a decline in traffic, saw softer baskets, and that's pretty much aligned with I think anything you need from some of the core retail grocery channels that have come out recently. So those behave similar to that. And then if you add in Dippin' Dots, Dippin' Dots was an incremental 29.2 million novelties.

Frozen Beverages, really excited about what we saw there. Beverage sales up 26%. The overall segment of 20% volume up over 9% in the quarter. We talked about the recovering the theater industry, so you start to see the consumer come back to theaters, the last few weeks having some of the biggest weekends they've had in a long, long time.

So all in all, we feel really good, but there's certainly some things going on with the consumer. There's probably a little bit, in the amusement area, of impact from some of the hot weather, and some of our amusement customers have talked about some impact on traffic in that category.

So kind of a quick overview, all in all, though, we feel like we're executing the plan we need to execute. And we're quite pleased, given all of that and where we ended up with sales.

Daniel Fachner ***J&J Snack Foods Corp. - President, CEO & Director***

Connor, I'd just add to that. We are confident in where we ended up. Much like what we've seen throughout this year, there has been some ups and downs throughout the year. And even this quarter, April, as it started, was off. There a consumer confidence issue, I think, going on a time with a lot of different things happening in our world, and it kind of grew again throughout the quarter.

So we've watched that really closely, but I don't think we had any big surprises, as you asked, in the quarter.

Connor Rattigan ***Consumer Edge Research, LLC - Research Analyst***

Okay. Great. That was really helpful, guys. And then I guess just looking at the gross margin, too, right, I mean as you guys called out pricing mix, stabilized inflation, right, I mean, I guess, could you maybe help us sort of, I guess, dimensionalize the extensive impact on each one of those, just kind of get a sense to that?

Ken Allen Plunk ***J&J Snack Foods Corp. - Senior VP, CFO & Treasurer***

Well, there's a lot in that, Connor, in terms of kind of parsing all that out. I mean the way I would answer your question is relative to mix, when you see us going in pretzels, churros, frozen novelties in our biggest segment Food Service, that mix will drive stronger margin, and it's a part of our strategy.

At the same time, some of the declines in bakery and handhelds are strategic. We're sharpening the pencil on SKUs, and some SKUs we got out of that weren't driving the margins we needed, and we're tweaking that, and we're investing in other products in those areas that we expect that things go down the road. But the combination of both dialing down in that area and then growing in those [highlands] helps mix, a little bit of that going on in Retail as well.

And then the other thing is when you mix in a record quarter for ICEE together with the biggest quarter to get the [], those are both very accretive to our top line margin, and so that mix in -- had a big role in our strong gross margin performance.

You then add on inflation coming down, I think, more than all of us expected. I think PPI was just shy of 3%. PPI, I think, was closer to 5%, that was about, I think, 200 to 300 basis points decline just from quarter-to-quarter, and we benefited then that cost in some of our key commodities, flour, oils, things of that nature came down, and certainly, that played a role on that.

And then the other thing we talked about is our initiatives to get better in how we operate, get better in how we produce product, is start to drop some efficiencies. So it all came together really nicely in this quarter. And I think it kind of sets the foundation, going forward. And we've -- somewhat, we guided that really crazy 12, 18 months of historic inflation.

Operator

The next question comes from Andrew Wolf with CL King.

Andrew Paul Wolf ***CL King & Associates, Inc., Research Division - Senior VP & Senior Research Analyst***

Congratulations on the quarter and the results. The results speak for themselves, but I just wanted to ask about -- sort of a prior question on the sales, and you guys kind of touched on, I guess, pass-through some deflation to a large customer. But in the past, you talked about SKU rationalization and lower margin lines, which I think bakery is and perhaps handhelds as well.

Is there any deliberate, if you will, kind of portfolio management of the lines in that way where you're not bidding up for contracts that just don't make sense when you have other lines of products you can produce and distribute that maybe have 2 or 3x the margin?

Daniel Fachner ***J&J Snack Foods Corp. - President, CEO & Director***

Yes. Andrew, you heard us talk a lot about kind of our strategy of pushing our core products, and we continue to use that, and we'll continue to do that. Also in the bakery is we're all fond with the bakery and what happens there. But what we do have a strategic initiative there to make sure what we're bidding on and what we make and who we sell to also complements our strategy as what we've been talking about getting to that 30% gross profit margin.

So absolutely has there been a strategy around it to reduce some SKUs that were operating there. And then the team that -- bakery team is really focused on new business and what they bring to the organization. And as I said in the opening, I'm proud of all of our teams in the way that they're executing the strategy.

Andrew Paul Wolf ***CL King & Associates, Inc., Research Division - Senior VP & Senior Research Analyst***

Is there any way to quantify beyond the pass-through on deflation of what the SKU rationalization might have been as a drag to see the sales growth?

Ken Allen Plunk ***J&J Snack Foods Corp. - Senior VP, CFO & Treasurer***

No, I'm not going to quantify what that is exactly and adds and flows with make month-to-month. I mean the bulk of it is going to be in bakery. So I think as you look at the bakery numbers, it's a combination of that SKU that together with the fact that a lot of that bakery is in retail and grocery bakery groups, where there has been some declines, softening of traffic in those venues.

Andrew Paul Wolf ***CL King & Associates, Inc., Research Division - Senior VP & Senior Research Analyst***

Okay. I understand. And Dan, if I could just get back to the way you're talking about your sales and just kind of -- I know you don't guide to us, but I just wanted to ask like how -- when you're thinking through your sales budget for the Board or however, how are you thinking about the current quarter and going into fiscal '24 for your budget about -- where the sales growth comes from in terms of price versus velocity gains on existing products? And it sounds like you're really bullish on new placements at new distribution.

So I'm not trying to fish a number out of you because I know you don't guide, but I am trying to get sort of a sense of where you see the growth, especially as economy is showing less inflation. So obviously, price is going to be less and less of a driver of sales growth, where would your volume -- I guess, to focus more on the volume growth, do you see it more in velocity in this kind of economy or more in your distribution gains?

Daniel Fachner ***J&J Snack Foods Corp. - President, CEO & Director***

Great question, Andrew. And to kind of highlight, I'd probably see it on both sides of it. right? I do think that we have the opportunity through some of the marketing activity that our team is doing to grow velocity in locations that we're already in. And then I love as we talked about some of the new innovation that we have and some of the new products that we're releasing and their abilities to complement and grow the business as well.

And the teams are working really hard and have what I consider a really strong pipeline to look at for this next year. And so -- as I talked about before, there is some volatility in the market. We'll watch that closely. Part of what I love about our company is that we have a really balanced portfolio, and you lived through this with us. There is a period of time when theaters were down, but retail was up, and now we're living in a period of time where theaters are up and retail has come back to more of a normal level.

I like the way that this business has been built with great products and great customers around a portfolio that allows us to ebb and flow that way. I think this quarter, we'll continue to see some growth, and then I look forward to seeing the budgets as they roll up over the next month or so for next year.

Andrew Paul Wolf ***CL King & Associates, Inc., Research Division - Senior VP & Senior Research Analyst***

Great. I appreciate that color. And if I can add just one kind of follow-up on your commentary on the marketing, budgeting being -- expenses being up, excuse me. When you talk about trade shows and sponsorships, is there some of the -- and I think in the past, you said to get some of the products like churros -- all the churros into retail, there would be slotting and things like that. Is that kind of what this is about? Or is this separate from that? And in the current quarter, we should look for the slotting fees as part of the marketing spend.

Ken Allen Plunk ***J&J Snack Foods Corp. - Senior VP, CFO & Treasurer***

Yes. It's really driven by kind of what we mentioned, is both timing and I would even say kind of the level of investment we're making in trade shows and sponsorship, particularly trade shows. I don't know if you've been to one recently that we were at, but kind of the level of kind of bringing together a good brand presence in an event, we will bring that out. I mean, it's really amazing what the marketing team has done to bring all our brands together and display it in a way.

So we're making investments there. We believe that's paying off. It's driving new channels, and it's driving new conversations. So it's really about that. I mean, full year, we may -- we want to be in the ballpark of where we typically are, maybe hear about that, Andrew. But it's money well spent. I think it started to tie in all the other strategies we're doing to drive interest in our brands.

Daniel Fachner ***J&J Snack Foods Corp. - President, CEO & Director***

I'll just add to that. Some of it is timing, Andrew, but we did make a really conscious decision at some of the major trade shows this year to really highlight all the great things that we do in our core products. And really proud of the team in the way that they put that together.

[You] let us talk about one of our core strategies being cross-selling our portfolio. By doing what we've done, we've had some really tremendous effort by the team, and some of our customers have just really seeing how well they can complement one of our products to the next. And and we think that's working. So we're proud of that.

Operator

The next question comes from Robert Dickerson with Jefferies.

Robert Frederick Dickerson ***Jefferies LLC, Research Division - MD & Senior Research Analyst***

Great. I guess just first question, just on Dippin' Dots. I say it's personal anecdote, but I don't know, past few months have been over kind of all in place and have seen certain formats in places like Wawas, few of my kids eat them in now kind of more handheld frozen novelty kind of on-the-go packaging.

So as you talk about all the distribution opportunities, whether it's in Food Service, Retail, what have you, I mean, is it fair to say at this point, kind of despite some of the innovation of the overall portfolio that -- I mean it seems like kind of more highly likely, more highly probable kind of revenue generation upside here, J&J is kind of primarily being driven by Dippin' Dots. And I don't mean that as a negative. It just sounds like the runway is pretty low.

Daniel Fachner ***J&J Snack Foods Corp. - President, CEO & Director***

We love that acquisition. You've heard us talk about that, Rob. Again, I'm proud of that team. And we've worked hard at integrating and then cross-selling and getting out and introducing them to some of the great relationships that we have out in the industry, it's really working. We see a really nice opportunity for that to continue to grow and are happy with what it's done to date.

And also, just thank you for your kids buying a product, too, all right. We appreciate that. But we really are happy with that acquisition. We're proud of the team and the way that they're managing it and the way that they have integrated with the whole J&J organization to find new growth, and have a lot of hopes for it in 2024.

Ken Allen Plunk ***J&J Snack Foods Corp. - Senior VP, CFO & Treasurer***

Just to quickly add to that. Everything Dan said, yes, optimistic and aggressive in the way we believe we can grow Dippin' Dots. But Dan [Indiscernable] the script, his focus on churros or Hola! as a brand, super pretzels as a brand, ICEE as a brand, all of those businesses have performed quite well in the quarter. Soft pretzels in Food Service, which is the biggest area that we sell pretzels in, was about 13.5%. Churros is up 19%. ICEE beverages by itself was up 26%.

So I certainly want to get credit to what we're doing, given that, but our focus areas are growing, and we feel really good about the opportunities down the road in those areas as well.

Robert Frederick Dickerson ***Jefferies LLC, Research Division - MD & Senior Research Analyst***

All right, super. And then I guess, just to jump to the margin side, clearly, gross margin is back strong as we think -- and then also Frozen Beverage, I think that's like may be the highest margin I've ever seen. So I'm just curious, as we think forward into kind of Q4, then clearly, we start thinking about next fiscal year, kind of where things sit today, is some of this kind of margin mix shift in the portfolio sticky?

Like is there anything that we saw in Q3 in Frozen Beverages maybe kind of like a one-off, so we don't want to get ahead of ourselves because you look at the gross margin in the quarter, it's great, but then you look at the op margins, too, and clearly, there are nice benefits flowing through? So I know that was the expectation kind of as we got into the back half. I'm just curious, at this point, kind of given normal seasonality as well as these improved margins now hopefully, kind of where we sit for some time?

Ken Allen Plunk ***J&J Snack Foods Corp. - Senior VP, CFO & Treasurer***

Yes. As we go into Q4, we feel very good about the position we're in, from a gross margin standpoint. I think if you look at Q4 and Q2 historically, given a little bit of slowdown as kids go back to school, that kind of thing, the margins will probably be a little bit south of what they were in Q3, but they should still be very good because we think we've passed the hurdle of some of those things that challenged us and most in the industry over the last several months.

And if theaters continue to the perform the way they are, it's going to be a big shot in the [arm] is both our ICEE business and as we penetrate theaters [and given to us], again, those high-margin parts of our portfolio.

So yes, I think we're pretty confident. I told you we're going to this make business to getting into the [higher] margin business year in, year out. And this is a really good start to that, and we expect to have good momentum going into Q4. Obviously, as you get into Q1 and Q2, the seasonality of that, those margins won't be at that level, but they will be much better than over the last year or so.

Daniel Fachner ***J&J Snack Foods Corp. - President, CEO & Director***

Rob, you heard us talk about kind of working all angles of the P&L, and that's exactly what we're doing. And we're really proud of each and everyone who's focused on that, right? We're certainly in the summer months where the mix helps us for sure.

But also, just the movement in the ICEE business, not only domestically but really strong quarter out of our Mexico operations, proud of what that team is doing. We think that we can have those margins up in that 30-plus area, like we've been talking about for a while. And it certainly gets a boost when you're in the summer months, but we're proud of what the teams are doing at all angles of the P&L.

Robert Frederick Dickerson ***Jefferies LLC, Research Division - MD & Senior Research Analyst***

All right. Great. And then maybe just lastly, I know, clearly, kind of overall basket and cost inflation side improved like you're saying, but also you're seeing some kind of material step-up in sugar and sweeteners, and anybody with decent exposure to those commodities have been saying the same thing, we all see it. .

So it sounds like overall, clearly, kind of pricing relative to your overall cost structure has really improved. But we've also heard some others that, "Look, if some of these inputs on the sweetener side remain elevated, the industry overall could potentially think about incremental pricing."

Is that anything -- is there anything in that that's kind of come up internally in terms of kind of those 2 core commodities? Or you're thinking about it more from an overall portfolio dynamic versus kind of, let's say, frozen novelties? That's it.

Daniel Fachner ***J&J Snack Foods Corp. - President, CEO & Director***

Yes, that's a great question, Rob. We do a monthly review with our different teams around the P&L. And our review in the [snack foods] side of our business this last month, we talked a little bit about the frozen novelties and what we may or may not do. And so we will look at it individually like that. We're going to watch it closely. And you're right, if that doesn't come down, then we may have to approach that in a different manner.

Operator

(Operator Instructions) The next question comes from Todd Brooks with Benchmark Company.

Todd Morrison Brooks ***The Benchmark Company, LLC, Research Division - Senior Equity Analyst***

Congrats on -- the results in the last quarter were surprising, margin improvement that you delivered, so congrats.

Two quick questions here, if I may. And this is just kind of getting this first year of Dippin' Dots correct. Can you talk about what the seasonality typically is for Dippin' Dots revenues in Q4 versus Q3? I'm just trying to triangulate, you've talked about a couple of annual goals for Dippin' Dots, and I think we'd be a little bit less than $30 million here in Q3. Would you expect that business to grow meaningfully in Q4? And if you look at overall company revenues, would you expect that Q4 will be our peak revenue quarter or Q3?

Ken Allen Plunk ***J&J Snack Foods Corp. - Senior VP, CFO & Treasurer***

Yes, Todd, we've talked about it, we're very clear about the seasonality in Dippin' Dots, particularly on the profit side, I talked about that. I would say, Q4 is going to probably perform similar to Q3, maybe a little bit better. Like you, we're still kind of running this business.

But we know, obviously, what they did last year, we know what some of the new initiatives and things we have in place in some of the areas of growth that you probably look at into Q4, that is somewhat similar to Q3 or given months.

Todd Morrison Brooks ***The Benchmark Company, LLC, Research Division - Senior Equity Analyst***

Okay. Great. And then based on Dippin' Dots similar to a little bit better in Q4, more core products, the SKU rationalization, just trying to think about what the headwinds are, if revenues are relatively similar between the quarters that would cause much of a gross profit margin moderation sequentially?

Ken Allen Plunk ***J&J Snack Foods Corp. - Senior VP, CFO & Treasurer***

Are you asking talking about the headwind on sales or gross margin?

Todd Morrison Brooks ***The Benchmark Company, LLC, Research Division - Senior Equity Analyst***

Well, if sales are relatively similar quarter-over-quarter and you're getting a little bit more Dippin' Dots revenue and you SKU-rationalize some lesser-margin products for core margin products. I'm just trying to figure out why gross profit should drop much from the 33% plus level that you did in Q3 when we get to Q4.

Ken Allen Plunk ***J&J Snack Foods Corp. - Senior VP, CFO & Treasurer***

Yes. It's really more about kind of historical seasonality. As you get into mid to late [August], it's certainly in the September, a lot of kids who are obviously, when [a lot of schools are] active and theaters and amusement parks and others, our business SKUs a bit heavier in Q3 and Q4 in those areas. So it's just more of the seasonal behavior of the consumer, which traditionally, we've seen a little bit lower gross margin in Q4 than Q3. But I wouldn't say it would be a dramatic time.

Todd Morrison Brooks ***The Benchmark Company, LLC, Research Division - Senior Equity Analyst***

Okay. That's fair. And then one final follow-up question on the gross margin. I look back historically, just to try to map that seasonal movement in gross margins. And you get back to '18, '19, and you were looking at maybe 200 to 300 basis points higher gross margins in the back half of the year than the front half of the year. .

Do you think that's where we normalize to? I know the difference as is a new piece of business that may drag a little bit more in the first half. But what would you expect that go-forward type of gross margin spend -- spread to be between the first half and second half of the year?

Ken Allen Plunk ***J&J Snack Foods Corp. - Senior VP, CFO & Treasurer***

Yes. I think the spread, certainly, I would say, the next year or so, will be similar. But I think all quarters relative to what it was particularly the 2 that we've already gone through, it should be better. So Q1 is coming up which should be better than Q1 of last year because we've gotten half some of the inflationary impacts and yes, and some of our initiatives are starting to be big dividends.

But if you just look quarter-to-quarter and think about the behavior of margin, it will continue to be strongest in Q3 and Q4 and then more relative to history in Q1 and Q2.

Now, what we're focused on, like we did the ICEE business years ago, is as we grow the penetration given that in the places like theaters, that provides a better seasonality for us and helps those on [Indiscernable] which we think would pay dividends for a sound road. But that will be kind of a gradual move to that, I think, as we build that business up.

Todd Morrison Brooks ***The Benchmark Company, LLC, Research Division - Senior Equity Analyst***

Okay. Great. And then, Dan, just a final one for you and I'll jump back in. You talked about the 6 new production lines that have been launched over the course of this year. As you start looking out to '24, how meaningful is that incremental capacity and throughput/productivity as a revenue driver for J&J because it's levered on those core categories where you're seeing the best growth around novelties, pretzels and churros?

Daniel Fachner ***J&J Snack Foods Corp. - President, CEO & Director***

Yes. Good question, Todd. We're really excited about those 6 new lines. We talked a little bit in the past about having capacity constraints in those core products that we think there's a lot of runway with. And so the teams are out there really actively being able to sell things like churros and different forms of pretzels and maybe even bringing some of that core into our bakery division as well, and that's being worked on right now.

So they become really meaningful for us. They kind of are at the heart of the strategy that we have in place right now. We're being able to grow pretzels, churros, frozen novelties and been able to broaden that like releasing a new pretzel bite or a pretzel stick that we have had some great early interest in.

So I think it becomes very meaningful for us. It allows the team to get out there and sell on the things that we do best and on the things that help us drive the margin mix that we've been talking about.

Operator

I am showing no further questions at this time. I would now like to turn the call back to Dan Fachner for closing remarks.

Daniel Fachner ***J&J Snack Foods Corp. - President, CEO & Director***

Well, thank you for your time today. In closing, we are excited about the opportunities to continue growing this great business of ours and confident that we have the right people, products, partners and strategy to maximize these opportunities. We look forward to sharing our fiscal 2023 full-year results later this year and updating you on the positive impact of various operational and strategic initiatives we are having on our business.

In the interim, should you have any questions or wish to speak to us, please contact our Investor Relations firm, JCIR at 212-835-8500. Thank you, and have a great rest of the summer.

Operator

This concludes today's conference call. Thank you for participating. You may now disconnect.