

Tyson Foods

Second Quarter 2022 Earnings

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CORPORATE PARTICIPANTS

Megan Britt - *Vice President of Investor Relations*

Donnie King - *President and Chief Executive Officer*

Stewart Glendinning - *EVP and Chief Financial Officer*

David Bray - *Group President, Poultry*

Noelle O'Mara - *Group President, Prepared Foods*

Shane Miller - *Group President, Fresh Meats*

PRESENTATION

Operator

Good morning and welcome to the Tyson Foods Second Quarter 2022 Earnings conference call. All participants will be in listen-only mode. Should you need assistance, please signal a conference specialist by pressing the star key followed by zero. After today's presentation, there will be an opportunity to ask questions. To ask a question you may press star then one on your touchtone phone. To withdraw your question, please press star then two. Please note, this event is being recorded.

I would now like to turn the conference over to Megan Britt, Vice President of Investor Relations. Please go ahead.

Megan Britt

Hello, and welcome to the second quarter fiscal 2022 earnings conference call for Tyson Foods. Prepared remarks today will be provided by Donnie King, President and Chief Executive Officer; and Stewart Glendinning, EVP and Chief Financial Officer. Additionally, David Bray, Group President, Poultry; Noelle O'Mara, Group President, Prepared Foods; Shane Miller, Group President, Fresh Meats; and Chris Langholz, Group President, International, will join the live Q&A session. We have prepared presentation slides to supplement our comments, which are available on the Investor Relations section of the Tyson website and through the link to our webcast.

During this call, we'll make forward-looking statements regarding our expectations for the future. These statements are subject to risks, uncertainties and assumptions, which may cause actual results to differ materially from our current projections. Please refer to our forward-looking statement disclaimers on slide 2 as well as our SEC filings for additional information concerning risk factors that could cause our actual results to differ materially from our projections. Please note that references to our earnings per share, operating income and operating margin in our remarks are on an adjusted basis unless otherwise noted. For a reconciliation of these non-GAAP measures to their corresponding GAAP measures, please refer to our earnings press release.

I'll now turn the call over to Donnie.

Donnie King

Thank you, Megan, and thank you to everyone for joining us for the call. Earlier today, we reported strong second quarter and first half fiscal year '22 results. Our results would not have been possible without the work of our team members. I'm grateful for their dedication and diligent efforts this quarter as we continue to manage a complex and dynamic operating environment. We delivered double-digit sales and earnings growth driven by strong market fundamentals, acceleration of our productivity actions and improving operational execution across our segments.

Our diverse protein portfolio, omnichannel capabilities, leading brands and value-added products all contributed to our results. Strong performance in our Beef segment, continued recovery in Prepared Foods and an improvement in Chicken supported improved sales and earnings. Our retail core business lines, which include our iconic brands, Tyson, Jimmy Dean, Hillshire Farm and Ball Park, have driven strong share performance in the retail channel since the onset of the pandemic. This quarter, we delivered share gains in bacon, hot dogs and snacking. We also continue to see recovery in the foodservice channel with our relative strength in QSRs and K-12, supporting continued share gains in branded value-added chicken.

Overall, consumer demand for protein has remained strong, and we are taking deliberate actions by segment to improve our volumes to better meet customer needs, including investing in new capacity,

brands, product innovation and our team member experience. We are seeing our investments in team members making an impact. Despite continued labor challenge during the Omicron surge this quarter, we're seeing lower turnover and absenteeism. We have invested in higher wages, benefits and other workplace enhancements, such as flexible schedules, child care and transportation. The construction of new plants continues to progress. This additional capacity will enable our team to address capacity constraints and better serve growing demand for protein across all segments.

Along with ramping up utilization of our newest plant in Humboldt, Eagle Mountain and Thailand, we have four plants expected to commence operation in the fourth quarter of fiscal year '22. In addition to the new sites, we're continually upgrading capacity as needed, with approximately ten projects planned in the third quarter, representing 25 million pounds of volume in Prepared Foods alone. In addition, we are working closely with our customers to ensure that the fair value of our products incorporates the inflationary cost pressures impacting our business. For the first half, our cost of goods sold rose 15% relative to the same period last year.

Every part of our business has been impacted by inflation. We experienced higher costs across our supply chain for all inputs from feed ingredients, live animals and other raw materials to cooking oils and basic supplies. We're also managing higher cost of labor and transportation due to robust demand, higher fuel costs and limited availability. As part of our effort to combat inflation and increase profitability, I'm pleased by our accomplishments to drive costs lower by accelerating our productivity actions. Also, our balance sheet and liquidity position remain healthy, providing optionality to invest in growth across our portfolio and return cash to shareholders.

We have a disciplined approach to deploying capital, with a focus on total shareholder return. Our first half results clearly demonstrate that we are making progress on our growth objectives and that we remain focused on outpacing the overall market, improving operating margins and driving stronger returns for our shareholders.

Now turning to the financial results, let me give you some highlights. Sales improved 16% in the second quarter and 20% during the first half. Our sales gains were largely driven by higher average sales price and mix improvement. Average sales price trends reflect disciplined revenue management strategies in the context of a volatile, high-inflation environment. Like many other companies, we've seen varying levels of heightened inflation, notably in grains, labor, live animals, raw material and transportation costs. As I mentioned earlier, our teams have worked together with our customers to manage inflationary pressures. We delivered solid operating income performance, up 57% during the second quarter and 47% for the first half.

The performance in the first half was due to strength in Beef, Chicken and Prepared Foods. Overall, our operating income performance translated to \$2.29 in earnings per share for the second quarter, up 71%, and \$5.16 in earnings per share for the first half, up 57%.

Looking at our results on volume. We remain confident that our actions will improve our performance, but we are not where we expected to be by now, as we faced the Omicron surge in the quarter and other labor and supply chain challenges. Due to these factors, our total volume was down slightly for the first half versus last year.

Chicken remained a bright spot, where volume was up 2.1% through the first half compared to the same period last year. This improvement was driven by solid fundamental demand as well as operational improvements. There is much more work to be done as we focus on filling our existing capacity. We are pulling multiple levers to drive sequential improvement in our performance. And as a result, I'm confident that we will see continued volume performance in the second half.

In Prepared Foods, volumes were down 4% in the first half compared to the same period last year. Approximately one-third of this decline was related to the pet treats divestiture, with the remainder as a result of a challenging supply environment and uneven recovery of the foodservice channel. We are working to improve these results over the remainder of FY '22, as we continue to take actions to expand and improve capacity utilization.

In Beef, volumes were down 2.9% in the first half compared to the same period last year. However, beef volumes increased quarter-over-quarter due to higher harvest weights. We expect continued volume improvements for the remainder of our fiscal year '22, as new team member recruitment strategies support an improved labor position and higher throughput.

In Pork, the impacts associated with a challenging labor environment contributed to a 2.3% decline in volume in the first half compared to the same period last year. We expect tightness in live hog inventories to affect our second half volume. In International/Other, our investments in capacity, innovation and brands are supporting our market share growth objectives and volume improvement. Overall, we will continue to take actions across our business to optimize our existing footprint, add new capacity, adjust our product mix and align our portfolio with customer and consumer needs.

Although we have reduced our expectations for the full year, we still expect to grow our total company volumes in fiscal year '22. We continue to take meaningful action toward becoming the most sought-after place to work, and we're making significant investments to attract and retain team members. Our US-based workforce is comprised of team members from more than 160 countries. In April, we announced that we are investing over \$1 million in several non-profit groups to expand legal and citizenship support for the team members aspiring to become US citizens. This will allow us to scale a program from 7 Tyson facilities to serve 40 company locations in 14 states.

We recently announced an expansion of the Upward Academy program as our latest investment in our team members. Starting this summer, U.S. team members will have access to free education, including masters, undergraduate and associate degrees, career certificates as well as class in literacy and technology fundamentals. And Tyson will pay 100% of the cost of tuition, books and fees, with an estimated investment of \$60 million over the next four years.

Ensuring the health and safety of our global team is a top priority. We continue to challenge ourselves to be an organization that stays ahead of the unforeseen events and adjusting our protocols to keep our team members healthy and safe. We have educated and encouraged team members to get vaccine boosters and have offered over 100 clinics across our office and plant locations.

We are also investing to support team member well-being more proactively in our rural communities. We now have seven on or near-site Tyson health centers opened and operating. These clinics provide comprehensive healthcare services, including preventive screenings, chronic condition coaching, mental health counseling, lab services and sick visits at little to no cost to most of our team members or their spouses and dependents. Overall, we're confident that our actions will increase Tyson staffing levels and position us for future growth, and we will continue to explore innovative benefit offerings that make our team members' lives better.

We're making excellent progress on our productivity program, which will deliver more than \$1 billion in recurring productivity savings by the end of fiscal year '24. Based on current progress, we now expect to deliver more than \$400 million of savings in fiscal year '22, which is on the high end of our previously disclosed range for the year.

Last quarter, I highlighted our work in Prepared Foods to build a digital manufacturing platform that

utilizes data to simplify complexity and optimize processing. I also shared our work to enhance the mix and allocation of our trucking fleet resources to enable better on-time deliveries to customers. This quarter, deployment of our Tyson production system approach has improved our yield across all segments versus a year ago. Additionally, our procurement program is addressing total company spend, including direct material as well as plant and corporate indirect areas. This program continues to deliver savings in line with expectations.

Our digital solutions journey has also progressed. In our supply chain, we are leveraging new processes and digital tools to quickly identify gaps in fulfillment. Meeting the demands of our customers on time and in full is of the utmost priority, and we are continuing to maximize our service levels. The early results of our finance automation and digitization work also remain promising. For example, this program is providing more accurate billing and improved collections for Tyson while lowering our intensive labor.

We are also investing aggressively in automation and technology to help address some of our most difficult roles and repetitive tasks. This is a well-planned program of automation to use common designs and equipment across our plants to optimize cost, maintenance and asset utilization. The debone automation program is continuing to scale in plants, and our Tyson proprietary debone automation solution is also beginning to roll out in select facilities. Looking ahead, we're starting to scale new programs like pack-out robotics to continue automating highly manual processes and deliver savings. Chicken remains a top priority, and we continue to execute against our road map to restore top-quartile profitability for this segment. We've been committed to returning our operating margins to 5% to 7% level by the middle of FY '22. This quarter, we delivered a 5% adjusted operating margin, in line with our previously communicated plan.

Critical to improving our profitability is maximizing our fixed cost leverage by being staffed to standard and having enough workers to run our plants full. Since September, we have seen an improvement in our hatch rate that is consistent with the expectations that we shared at our December Investor Day. We are committed to growing our harvest capacity utilization, and we outpaced the industry in the second quarter. Achieving improved chicken harvest and higher capacity utilization will allow us to build on the volume growth delivered by Chicken in the first half.

In parallel to actions to improve volume, we have also worked with customers to manage inflationary pressures by adjusting pricing to achieve a fair value for our products. This will be important to ensuring we deliver sequential improvement in our operating margins in the second half of fiscal year '22, especially with continued increases in key input costs such as labor and feed ingredients. As I mentioned a moment ago, we are also making good progress on our automation objectives for the segment. This includes the rollout of debone automation and a range of other equipment, which will enhance our productivity and cost effectiveness. We have come a long way in a short period of time, and I'm pleased with the progress we are making in Chicken.

To recap, we have strong consumer demand, a powerful and diverse portfolio across geographies and channels and a team that is positioned to take advantage of the opportunities in front of us. The five imperatives on this slide show how we will achieve our commitments and drive value creation for our shareholders. This starts first with our commitment to our team members, with a focus on ensuring their health, safety and well-being as well as investing in improving our team member experience.

Second, we are working to enhance our portfolio and capacity to better address demand. This includes increasing the contribution of branded and value-added sales. As a result, we expect our volume to outpace overall market growth over the next several years.

Third, we are aggressively restoring competitiveness in our Chicken segment and continue to achieve key milestones on our road map to top-quartile profitability.

Fourth, we are driving operational and functional excellence and investing in digital and automation initiatives. This is at the heart of our productivity program, where we are accelerating our efforts and now expect to deliver more than \$400 million in savings this year.

Fifth, to address projected demand growth over the next decade, we're using our financial strength to invest in our business. We're on track to invest \$2 billion in fiscal year '22, with a disproportionate share focused on new capacity and automation objectives. We also continue to return cash to shareholders. Through the first half, we returned approximately \$850 million in dividends and share repurchases.

As a final comment before turning the call over to Stewart, I want to highlight that Tyson Foods understands we have a critical role to play in the global food system, to make it more resilient, more sustainable and more equitable for current and future generations. Just recently, we completed a materiality analysis that will inform our long-range strategy. These insights from key stakeholders shape our strategic framework and provide direction on the expectations of our company.

I will now turn the call over to Stewart to walk us through more detail on the financial results for the second quarter.

Stewart Glendinning

Thank you, Donnie. Let me turn first to a summary of our total company financial performance. We're pleased to report strong results in the second quarter and first half of this fiscal year. Sales were up in the second quarter and the first half, benefiting from our pricing initiatives to offset inflation as well as improved product and channel mix. Volumes were down slightly through the first half, impacted by continued labor challenges and a temporary disruption from the Omicron variant surge.

Looking at our sales results by channel, retail drove \$424 million of top line improvement in the second quarter relative to the same quarter last year. Through the first half, retail sales have improved \$773 million. In the second quarter, improvements in sales through the foodservice channel drove an increase of \$684 million, and domestic export sales to international markets were \$311 million stronger than the prior year period as we leveraged our global scale to grow our business. Second quarter adjusted operating income of \$1.2 billion was up 57% relative to the same quarter last year, led by increases in Chicken, Beef and Prepared Foods.

First half adjusted operating income of \$2.6 billion was up 47%, supported by increases in Beef and Chicken. Driven by the strong increase in operating income, second quarter adjusted EPS of \$2.29 grew 71% compared to the same period last year. Second quarter earnings per share also benefited from lower net interest expense and higher other income.

Slide 11 bridges year-to-date operating income for the second quarter, which was \$422 million higher than fiscal 2021. Volumes were down 1.5% in the second quarter. Volume improvement in Chicken, International/Other and Beef were offset by declines in Pork and Prepared Foods, where continued labor and supply chain challenges impacted throughput. Our pricing mix and portfolio efforts led to higher sales during the quarter, which offset the higher input costs. We saw continued inflation across the business, in some instances up 25% or more. Notable examples were labor, feed ingredients, live cattle, lean hogs and freight costs. SG&A was \$46 million unfavorable to the same period last year due to increased team member-related costs and investments in advertising and promotional spend in support of our brands. As a final note, both cost of goods sold and SG&A expenses in the quarter were partially offset by productivity savings.

Moving to the Beef segment on slide 12, segment sales were approximately \$5 billion for the second quarter, up 24% versus the same period last year. Sales growth in the quarter was driven by continued robust demand for Beef products, which supported higher average sales price and volume. The cutout and our average sales price remained relatively strong during the quarter despite some consumer demand shifting toward lower-cost beef cuts. Quarterly volume improved compared to the prior year despite the Omicron surge experienced by the business. We expect volume to continue to improve in the second half of this fiscal year as new team member recruitment strategies support improved staffing and higher throughput levels.

On expenses, we incurred greater costs during the second quarter versus the comparable period a year ago as live cattle costs increased approximately \$545 million in the quarter. We had sufficient livestock available in the quarter, driven by higher herd liquidation due to drought conditions. As of February, 54% of cattle inventory were in areas experiencing drought conditions, which may lead to additional herd liquidation through the remainder of the fiscal year.

We delivered segment operating income of \$638 million in the quarter, up 43% versus the comparable period. This improvement was driven by solid global demand for Beef products, supporting a higher cutout as well as higher specialty product values, which were partially offset by higher operating costs. Our operating margin of 12.7% was higher than the same quarter last year but was down on a sequential basis versus the last two quarters, as cost increases led to a narrowing of the spread.

Looking next at the Pork segment, sales were approximately \$1.6 billion for the quarter, up 6% versus the same period last year. Average sales price increased 10.8%, but volumes were 4.8% lower relative to the same period last year. Average sales price was up due to higher input costs, while volumes were lower due to labor challenges from the Omicron surge, which led to lower processing throughput. Segment operating income was \$59 million for the quarter, down 12% versus the comparable period. Overall, operating margins for the segment declined to 3.8%. The operating income deterioration was driven by softer exports, higher input costs and labor challenges.

Moving now to Prepared Foods. Sales were approximately \$2.4 billion for the quarter, up 11% relative to the same period last year. Total volume was down in the quarter given labor and supply chain challenges and uneven foodservice recovery and the sale of our pet treats business. Sales growth outpaced volume growth driven by higher average sales price. Consumer demand has remained durable even as we worked to manage inflation through price increase.

Overall, consumer response to higher price levels is below historical expectations, as our brand strength and category relevance has enabled continuing strong demand. Raw material costs, logistics, ingredients, packaging and labor all increased our cost of production. To offset higher costs, we have executed productivity, revenue management and commercial spend optimization initiatives while ensuring the continued development of brand equity through increased marketing and trade support. Operating margins for the segment were 11% or \$263 million for the quarter, up 21% versus the same quarter last year.

Moving on to the Chicken segment's results. Sales were \$4.1 billion for the quarter, up 15%. Volumes improved in the quarter due to strong consumer demand and operational improvements. Our teams have been focused on streamlining our plants to deliver higher volumes. We expect to deliver further volume improvements in the second half of fiscal 2022 as harvest numbers improve and we continue to optimize the operational efficiency of our plants. Average sales price improved 14.4% in the quarter compared to the same period last year. This increase was primarily due to price recovery offsetting inflationary costs.

On pricing, we made meaningful progress to shift our pricing mechanisms toward more variable structures and are now seeing those benefits. We restructured our pricing strategies given our experience in fiscal 2021 to be more agile in response to market and inflationary conditions. Chicken delivered adjusted operating income of \$203 million in the second quarter of fiscal '22, representing an operating margin of 5%. Operating income increased in the second quarter due to increased sales volume and higher average sales prices, partially offset by the impacts of inflationary market conditions, including increased supply chain costs and a challenging labor environment.

In the second quarter of fiscal '22, we experienced \$100 million of higher feed ingredient costs and \$101 million of net derivative gain as compared to \$10 million of net derivative gains in the second quarter of fiscal 2021. During the fiscal month of April, the beginning of our third quarter, we have achieved an approximate 5% operating margin, excluding mark-to-market derivative impacts. Restoring competitiveness in our Chicken business remains a top priority, and we are making progress on achieving our long-term targets for adjusted operating margin, but we still have work to do.

Turning to slide 16. Our healthy cash flows have continued to support a broad capital allocation approach. We are focused on building financial strength, investing in our team members, investing in our business and returning cash to shareholders. Consistent with our expectations, our operating cash flows were down slightly in the first half of the year due to planned investment in working capital. And consistent of our priority to build financial strength and flexibility, we used our existing liquidity to retire \$1 billion of debt in the second quarter. Since the start of the pandemic, which this quarter now marks as two years ago, we have reduced gross debt by approximately \$3.8 billion. We maintained our leverage ratio at 1.1x net debt to adjusted EBITDA, demonstrating our powerful balance sheet and our continued capital allocation optionality.

Investing in our business for both organic and inorganic growth will continue to be an important priority and will help Tyson increase production capacity and market capabilities. This will support strong return on capital generation for our shareholders.

Finally, as our track record has demonstrated, we are committed to returning cash to shareholders through both dividends and share buybacks. We bought back \$175 million of shares at an average price of \$88.50 per share during the second quarter. This is in addition to the \$348 million of shares repurchased during the first quarter.

Let's now discuss the fiscal '22 financial outlook. Based on the strong first half results, we're raising our total company sales guidance to a range of \$52 billion to \$54 billion. In support of our sales growth, we now expect 1% to 2% volume growth on a year-over-year basis as we work to optimize our existing footprint and run our plants full.

Looking at AOI margin target ranges for our segments. In Chicken, our operational turnaround is working, and we expect full year margins to be between 5% and 7%. Based on our first half performance, we now expect the full year margin in Prepared Foods to be in the range of 8% to 10%. In Beef, we are raising our AOI margin to 11% to 13%. We still expect the first half of the year to be meaningfully stronger than the back half as industry and labor conditions are expected to normalize in the second half. We expect that cattle price increases will reduce the overall margin in the back half. In Pork, we expect similar performance during fiscal '22 to what we accomplished during fiscal 2021, equating to a margin of between 5% and 7%.

As is normal seasonality for Pork, we expect the first quarter to be the strongest. In International/Other, we anticipate reduced results from our foreign operations in fiscal '22 due to supply chain disruptions and other impacts related to COVID-19. Our expectations for CapEx, net interest expense and tax rate

remain unchanged. Our net leverage is expected to remain well below 2x net debt to adjusted EBITDA, providing optionality, inorganic investment and additional return of cash to shareholders over the course of the year.

I'll now turn the call back over to Megan for Q&A instructions. Megan?

Megan Britt

Thanks, Stewart. We'll now move to your questions. Please recall that our cautions on forward-looking statements and non-GAAP measures apply to both our prepared remarks and the following Q&A. Operator, please provide the Q&A instructions.

QUESTIONS AND ANSWERS

Operator

We will now begin the question and answer session. To ask a question, you may press star then one on your touchtone phone. If you're using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press star then two. Please limit yourself to one question and one follow up. If you have further questions you may re-enter the question queue. At this time we will pause momentarily to assemble our roster.

And our first question will come from Ken Goldman of JPMorgan. Please go ahead.

Ken Goldman

Hi. Thanks and good morning. Donnie, I think you mentioned your expectation for sequential improvements in operating margins in the back half of the year. I just wanted to clarify, does this mean that you expect your operating margin in 3Q to be above 2Q, so above 8.9%, and then for 4Q to be above that once again? Or are you simply saying that the second half will be above the first half with, I guess, no comment on the cadence of 3Q versus 4Q? I know it's hard to measure these things. I just wanted to be sure what you were suggesting there.

Stewart Glendinning

Yes. Let me pick that up for Donnie. This is Stewart. I think you can take it as the first half is going to be not as strong as the second half. We haven't got obviously into giving you quarter-by-quarter. But we expect our business to strengthen over the back half. You'll recall from the prepared remarks that we expect our Beef to start to weaken in the second half, so some of that quarter-by-quarter timing will depend a little bit on the timing update.

Ken Goldman

Okay. Thank you, Stewart. That's helpful. And then, how are you thinking about the timing of the cattle cycle right now? What I mean by that is you mentioned that you expected the herd liquidation to continue the rest of the year. Again, no one has a crystal ball on these things, but do you have even a rough estimate for when you might expect the liquidation cycle to end next year?

Donnie King

Thanks, Ken. This is Donnie. We expect it to—in fact, we thought we would have already seen lower supply than what we are seeing right now. An interesting data point is that cattle and feed recorded over 12 million head, a record high for March 1. So there's a little bit of noise in that still. Drought conditions and grain costs are certainly impacting supply. But as we said, we think in the back half of the year we'll see the spread tighten in our Beef business. But I would also point out that we think it will be much higher. In fact, we call it 6% to 8% on a normalized range these days. But it's holding up pretty good right now. And while it's not going to be a record back half, we think it will be a very good one.

Ken Goldman

Thank you to both.

Donnie King

Thank you.

Operator

The next question comes from Adam Samuelson of Goldman Sachs. Please go ahead.

Adam Samuelson

Good morning, everyone.

Donnie King

Good morning, Adam.

Adam Samuelson

So I just wanted to dig a little bit more in Chicken and thinking through the margin expectations in the back half of the year specifically and then what that implies as you move into fiscal '23. I think in the prepared comments, you talked about April being at 5% even after any mark-to-market impact on grain. How do we think about the different levers to further margin improvement in Chicken through the back half of the year, whether it's volume in terms of the hatch and your throughput in the slaughter plants, mix, pricing actions versus some of the incremental inflation as we look at grain and some of your other purchasing puts?

Donnie King

Thanks, Adam. Let me say a few words, and I'll flip it to David Bray to add a few details. It was a year ago this quarter that I talked about the turnaround in Chicken, and in fact, talked about being at a 5% to 7% business. I will tell you, in this quarter, January, from an Omicron resurgence was painful across all of our businesses. But we've improved sequentially throughout the quarter. The back half of the year, in Chicken specifically, the thing that we need is greater volume, greater efficiency from the assets that we currently have. And we've announced a further processing plant that will come online next year that will add some incremental capacity. But our productivity program is working. We are becoming more efficient, and our volume is growing. And I would expect you to see that to continue to grow and develop over the balance of the year. I would tell you in short, we're on plan.

And let me flip it to David, and he can add a little texture.

David Bray

Adam, good morning, and thank you for the question. I think, first and foremost, what I do want you to hear is that we have made progress within the Chicken segment. But we also know that we have much, much more work to do, and we're focused against that. I would also tell you that we said that we would deliver sequential improvement throughout the fiscal year, and we have. We also shared that we would see improved volumes sequentially. And quarter-over-quarter we have seen improved volume. And we also said that we would outpace the market for growth, and within the Q2 time frame we did that as well. In Q2, our harvest head was up 2.9%, and our harvest volume was up 4.9%, which actually allowed Tyson to gain share in the Q2 time frame of about three-quarters of a point. We've also improved our adjusted operating income and our AOI margins sequentially quarter-over-quarter, and this was the case whether we include or exclude any impacts of derivatives against our business.

And so again I would tell you, we're making progress. We have more work to do. We are focused, and our goal has not changed: to be the best chicken company as we focus on the levers of our business.

We're continuing to work hard to staff our plants. And today, I would tell you the poultry segment is staffed to standard. We're continuing to work on servicing our customers, growing our business and to drive overall operational improvements.

Donnie King

If I could add one more thing, Adam. On Friday, we closed on April—by the way, it was a five-day close, which is a new record, thanks to Stewart and Philip Thomas and the team, but in Chicken specifically, April was a good month. And Stewart referenced in his prepared remarks around 5%. I can tell you from the close that it's better than 5%. So I'll leave it at that.

Adam Samuelson

All right. That's really helpful. And if I can maybe just follow up in Chicken. I'm just trying to think about the internal kind of actions you're taking and what you have under your control is very clear. And I'm trying to make sure we can calibrate how the external environment has evolved in terms of record breast meat prices, maybe some declines in wings, risk around avian influenza and what that could potentially do to exports relative to the grain markets and just trying to think about how changes in that external environment would or would not impact how you think about chicken moving forward.

Donnie King

Thanks, Adam. I will tell you, we started over a year ago with what we call our four pillars, which was staffing our plants, servicing our customers, growing our business, and restoring industry-leading operating performance. That's still our plan. As you well know, there are a number of variables going on right now in the poultry business. What I can tell you is volume is good, demand is strong. In fact, I would tell you that if you look at the price of boneless skinless breast meat, I think Friday it was somewhere around \$3.60. It's been a long time since I've seen that kind of strength in breast meat and for chicken overall. And so grain is higher, of course. We are seeing that. Dave and his team are responding with shorter-term contracts to try to protect Tyson and try to protect our customers as well.

And I'll flip it over to David to see if there's anything other things he'd like to add. David?

David Bray

Yes, I think just from the grain standpoint, despite what we're seeing from volatility in grain, the turnaround in Chicken is progressing as planned. And again, a large part of that is based off of our variable pricing structures. We're able to move much faster than we have in the past, and that's been a big benefit to us. Relative to avian influenza, yes, we are watching that closely, and it is always a risk within this business. But I would tell you that we mitigate that risk through the use of our biosecurity measures and that they are in place across all of our facilities right now. This includes testing every flock that we have for AI before it leaves the farm.

We are operating under heightened measures in some geographic areas of the country right now, and the heightened measures would basically be we're limiting the amount of people and trips that are taken to our farms as well as making sure that the people that do go to the farms are in clean vehicles, and we will continue to monitor that. To that, I would tell you that any bird loss related to disease impacts our growers and it impacts our plants as well, but these have been relatively minimal to our business to date.

Adam Samuelson

All right. That color is all really helpful. I'll pass it on. Thank you.

Donnie King

Thank you.

Operator

The next question comes from Ben Bienvenu of Stephens. Please go ahead.

Ben Bienvenu

Good morning, everybody.

Donnie King

Good morning, Ben.

Ben Bienvenu

I want to follow up on Adam's questions about the Chicken business. Obviously, your commentary on April is quite strong. Your guidance suggests continued strength in that business. If we could, I want to ask a little bit about the mechanics of what happened in the quarter and kind of mechanics of cost-plus. I think we have an understanding of what happens when you have derivative gains and why. But would you talk about when and why you hedge your grain? And to the extent that we look into the balance of the year and that reflects hedges that you have on and benefits that you might enjoy as a result of that, could you talk about that versus a cost-plus sort of mechanism that as grain prices go up allow you to take high prices? I'm just trying to understand the moving pieces around what we should be mindful of as we monitor the environment going forward.

Stewart Glendinning

Yes. This is Stewart. Let me go ahead the question on hedging. So we hedge primarily when we are obligated to fixed price, and particularly any kind of agreements that are longer term that makes sure that we're not exposed to a fixed price with a moving commodity base. This year, we've seen a shift. We've talked about that in a couple of our calls. We have shifted to more variable or commodity-driven pricing, which means that we don't have to hedge as much. Keep in mind also, though, that those pricing mechanisms will have various triggers, and therefore, they won't be re-pricing every day. And so you will see us, of course, hedging over the shorter term to make sure that during that kind of lag period where we are obligated to price, that we've got protection from movements in grains and other commodities. Is that helpful?

Ben Bienvenu

Perfect. Very helpful, thank you. Pivoting and thinking about the Prepared Foods business, really solid margin results in the quarter, I know there's this cost price dynamics that you and all of your peers are navigating. The back half of the year suggests maybe a little bit of margin pressure and then expansion thereafter. Can you talk about how you feel about your price elasticities in that business, how you feel about your ability to operate the business well and perhaps as we cycle through some of the volume losses from the pet treat business to improve and deliver on fixed cost absorption and your balance of the margin balance when we move through this year and into next year would be helpful.

Donnie King

Thank you, Ben. Let me hit a couple of points, and I'll flip it over to Noelle, and she can go into greater detail with you. And you saw in our statement, the first half was down. We had lower production throughput. Again, January was troubling, with the Omicron resurgence, challenging labor. And we did have the sale of pet treats in the first half. We expect the volume to improve. Retail demand remained strong, and we had some uneven recovery in our foodservice business, meaning there are some spots, and I'll call them out specifically, and then I'll flip it to Noelle. In our pizza topping business, for example, it was softer than expected. Our Philly business was softer than expected, and our tortilla business was softer than projected.

And with that, I'll flip it over to Noelle, and she can talk about the elasticities.

Noelle O'Mara

Thanks, Donnie. So as Donnie referenced, demand really does continue to be strong, driven by our strong brand equities and our diverse portfolio. And we do see that demand continues to exceed supply in a majority of our categories. We've made significant improvements in our labor vacancy rates. We expect to be back to pre-pandemic levels. In the second half, we also have investments coming online that we referenced in the prepared remarks on capacity. As Donnie referenced in foodservice, we are seeing a bit of uneven recovery. Overall, I would say it's showing momentum. Where we did see impacts is in January and February, where the Omicron variant surge had a brief negative impact as consumer mobility waned and foodservice traffic declined. This, along with some of the other dynamics from a labor perspective in the industry, slowed recovery at the beginning of the year. But as we look at March traffic, the data shows that we are returning to pre-Omicron recovery levels as COVID cases drop back to a bit more normative levels.

But broadly speaking, QSRs and stores continue to lead the recovery relative to other channels. We're also seeing great momentum in K-12 and continue to be optimistic in the overall recovery. And as referenced, we continue to make significant impacts in cost transformation. And so you'll continue to see a focus on that holistically for us across the business as we continue to improve labor, as we continue to expand our capacity, as we continue to invest in our portfolio and our leading brands and expect to deliver 8% to 10% ROS for the year.

Ben Bienvenu

Great. Thanks so much and best of luck with the rest of the year.

Donnie King

Thank you.

Noelle O'Mara

Thank you.

Operator

The next question comes from Peter Galbo of Bank of America. Please go ahead.

Peter Galbo

Hi. Good morning. Thank you for taking the questions.

Donnie King

Good morning, Peter.

Peter Galbo

Maybe we could start with Beef. You guys have obviously seen your business, I think, disaggregate a bit from some of the third-party sources. And I do think a lot of that probably comes from your export business and maybe some of the byproduct business. But can you talk about maybe those two specifically in the quarter and how we should think about them going forward as we monitor external data versus stronger results that you're reporting in Beef?

Donnie King

Peter, I'll make a couple of comments, and I'll flip it to Shane to make a couple. In our Q2, sales volume did increase. We had improved staffing and higher harvest weight. We talked a lot about the fact that we're buying a higher grade of animal to process. Grades have improved significantly through the last couple of decades, and that continues to be the case for us. But as you pointed out, we're seeing a lot of help from our specialty products group, particularly in the fat and tallow area, our relationship with

Jacobs Stearns that we've had there, we're able to take a lot of that product and with the price of diesel and fuels, we're able to now get some really great value out of those products, and that's providing some tailwinds for us in our Beef business.

But I'll flip it to Shane, and he can add a little bit more color to that.

Shane Miller

Yes. Thanks, Donnie, and thanks, Peter, for the question. Donnie, he hit on a couple of the categories. Obviously, specialty products, which is everything that's coming off of the drop or the harvest side of our operations, has improved. We continue to see better value coming from the fats and oil category. But also if you think about areas like proteins, you think about hides, you think about some of the variety meats that are typically sold into the export arena, we're seeing very strong demand globally from the product mix that we're supplying to the marketplace.

This is still a cyclical business. We believe over that continuum that beef demand will continue to be very strong from a global perspective. And on top of that, if you think about the value that we're bringing to the marketplace and also ultimately to the consumer, the meat quality and the cattle genetics that are being supplied to us today have never been better. So I think as we look forward here, strong quality, great product mix and diversification of customers and programs will lend to stronger support.

Peter Galbo

That's helpful. Thank you. And then, Donnie, I just wanted to reconcile some of your comments in Chicken around your hatch improvement plan being on track. I think for total company, though, you took the volume guide down and just wanted to understand what that implied around back half chicken volumes. I think previously, we had talked about them being up maybe double digits to kind of make the year. So just wanted to reconcile kind of those two aspects.

Donnie King

Sure. There's a number of things going on there. Our hatch has improved. We're better than the average of the industry, for example, today. A year ago, we could not say that. So we have seen improvement there. We have also reduced our outside purchase of meat, and that's had a pretty significant impact on our overall volume, in Chicken specifically. We also, if you'll recall, we had a fire in Huntsville, Alabama that impacted our volume, not only of the rendered product that we produce ourselves, but on the ability to go buy that on the outside. That had a pretty significant impact as well. So those are kind of the top line things relative to volume.

What I will tell you is we grew in the quarter, we grew in the first half. We didn't grow at the rate which we said, and if you'll recall, we wanted to grow faster than the market, which we did, but not where we want to be in terms of overall volume. And I'll let David touch on some of that.

David Bray

Yes. I think one other comment to that is we have seen several weeks, five weeks of continuous improvement within our live operations. And one big component of what's going to continue to improve for us is we are on track with the delivery of the new male into all of our farms. And so we feel very optimistic about that. It's a male that we know very well. With that, we will continue to see improved hatch rates within our facilities as well as improved weight gain across with the new male coming in.

Peter Galbo

Thanks very much, guys.

Donnie King

Thank you.

Operator

The next question comes from Ben Theurer of Barclays. Please go ahead.

Ben Theurer

Good morning, Donnie, Stewart, congrats on the results. First question, just if you could elaborate a little more about the productivity program and the savings realizations which you had, the roughly \$400 million you've mentioned. Can you give us a breakdown on like sector basis, how we should think about where our focus has been mainly put within more recently? And where do you think low-hanging fruits are for the back half to deliver here? That would be my first question. Thanks.

Donnie King

Sure. Thank you. So in terms of productivity, I'll just start out by reminding what we said in our Investor Day. We said that from an operational and functional excellence perspective between now and '24, we would save \$300-plus million, applying digital throughout our supply chain was worth another \$250 million, and automation was \$450 million. What I can tell you to date is that we will deliver near \$400 million in year one. And each and every day, we identify new things that we can put on our tracker that will deliver better results. What I would want you to take away from this is that there's unprecedented inflation, inflation we haven't seen in generations, really. And so this is not just pricing for inflation, we're also doing everything we know to do to become a more productive, a more efficient, a lower-cost producer. And as we say in our poultry business, we want to be top quartile or better in every place that we play, and we've still got room to do that.

So I'd tell you that we're on track. There are things like trucking fleet resources and optimization, our procurement program to address total company spend and then gas and fulfillment, the debone automation projects that we have in poultry, they're progressing as planned. In fact, they're a little ahead of that. And so we feel good about that. But our future is going to, one, we have a fair market value price in the marketplace; but two, we want to be among the very best in every place that we participate.

Ben Theurer

Okay. Perfect. And then my follow-up is actually just a quick one for Noelle, on one of her comments she made around the adjusted operating margin in Prepared Foods to get this to the 10% level. So obviously, if we look into, first half was very strong, roughly 9.5%. So that's already the higher end of the range. So how should we think about that 8% to 10%? Is it really achievable at a higher level? Because I think you said something like you want to be at 10%. So you want to be at 10%, but there might be some uncertainty which could bring it down for whatever reason, which we don't know today, but we should more plan on 10% than maybe 8%. Is that fair?

Noelle O'Mara

Well, what I'd start by saying is, to your point, and you've heard this in the prepared remarks and Stewart emphasized as well, is that we had a better-than-expected first half, really driven by the actions that we took on price to offset inflationary impacts, the improvements that we saw in labor, the cost transformation starting to come through as well as mix. As I referenced a few minutes ago, the demand expectations that we see continues to outpace supply. And with labor momentum and the capacity investments, we do expect volume improvements as we continue through the second half. We also anticipate continued foodservice recovery. As we look towards the back half on the inflationary side, we do continue to expect inflationary pressures through the back half, which is why it's sort of top of mind on the cost transformation efforts that Donnie just referenced. And so holistically, we're confident about

the 8% to 10% ROS range.

Ben Theurer

Okay, perfect. Thank you.

Operator

The next question comes from Alexia Howard of Bernstein. Please go ahead.

Alexia Howard

Good morning, everyone.

Donnie King

Good morning.

Alexia Howard

Can I dig into the labor cost issue? To begin with, maybe some numbers if you have them, the labor costs as a percentage of COGS, especially in Chicken, your vacancy rates and how they're trending over time? And specifically, just more philosophically, you've been improving pay and benefit for two years now since that summer of 2020, and it seems as though the pandemic is easing and yet these labor challenges are persisting. I think you alluded to the diversity of your team members. Is there a more structural problem that with the tightening of immigration policies that that sort of dried up the well of where you can recruit people into those types of roles?

And then secondly on the labor side, I'm just thinking from a cultural perspective, from a morale perspective, I think your automation processes are talking about a 3,000-person reduction in job counts over the next three years to fiscal '24. How do you recruit and retain people as you're going through that automation process? I'm trying to get a whether this labor issue is likely to be a persistent problem despite all the efforts that you're making to improve the working conditions. Thank you, and I'll pass it on.

Donnie King

Thank you for that question. And I'll hit on a few points. For example, we realize—fully realize—that we have to create a desirable place to work. In fact, we talked about it in terms of being the most sought-after place to work. We realize that those team members that we have can work wherever they choose to work and we want to give them a reason to work for us. I believe I said in the last call, it is not my objective to fix the labor problem in the United States. My objective is to fix the labor issues that we have at Tyson Foods, and we're doing that. And there's not one thing that fits all the needs. For example, child care, you can talk about child care, and there's a subset of the population that that is of value. But there's also other areas where it's not. Transportation is more desired and needed in other areas. We have, in some rural communities, for example, the need for healthcare. So we created on-site or near-site health clinics that our team members and their families have access to little or no cost. And that's one more opportunity for us to have a differentiated place to work.

It's true, we continue to invest in wages and benefits, in booster shots and booster clinics. We've done over 100 of those. And we think we're seeing a positive impact from those things. We're seeing improved absenteeism and turnover rates. We announced that we're going to support team members through non-profits for legal citizenship support. And then two weeks ago, I think it was, we announced Upward Academy program. And we're going to spend \$60 million over the next four years for education for our team members. That's master's degree, bachelor's degree, associate's degrees, live skills training, English, for example, whatever we can do to try to differentiate Tyson as a place to work. We are committed to that result. We, this past year, paid all of our team members at end of the year, thank-

you bonuses. And we were happy to do that. Those team members we have are the lifeblood of this company. We don't do anything without them. And so investing in them, taking care of them, keeping them safe is our highest priority.

Alexia Howard

Thank you very much. I'll pass it on.

Operator

The next question is from Ken Zaslow of BMO. Please go ahead.

Ken Zaslow

Good morning, guys.

Donnie King

Good morning, Ken.

Ken Zaslow

Talking about the Prepared Foods business, it sounds like there's a lot of internal improvement. How does this margin structure that you've created for this year kind of forecast how you're going to be going forward in 2023 and 2024? Does this give you more confidence? Or are you more tempered because of the inflation? I got a sense of both those sides throughout the conference so far. So I'm just trying to figure out. I would have thought it would have been more bullish longer term, but it sounds like you were tempering it a little bit on the inflation. I'll leave it there for now.

Donnie King

Thanks, Ken. I'll start off, and then I'll let Noelle, see if she wants to add anything. I think it's important that everyone here—that we're pricing and trying to get a fair market value for our product in the marketplace. That's one avenue. But secondly, the one that's absolutely in our control is to be able to do what we do better, as being best-in-class in operations. That's labor, that's yield, that's spend, productivity, running lines at rate. And then let's not forget the fact that a location—we all have 168 hours in a week, how do we run more hours in a week and get greater asset utilization off the assets that we currently have? And so we're looking at all those things. So think productivity, don't think of it as something to offset inflation. Think of it as a way of life and who we are as a company. And, pardon the expression, it's the gift that's going to keep on giving for us, and it will never go out of style for us.

So with that, let me pause, and I'll let Noelle add some color to that.

Noelle O'Mara

Thank you, Donnie, and thanks for the question, Ken. So what we've talked about through Investor Day and as we've come together on these calls, we continue to believe in our confidence that this portfolio is a double-digit ROS business. And the foundations of those building blocks continue to be the same. Demand continues to be strong across retail as well as the expected continued foodservice recovery. As we look holistically, the top line acceleration will come from actions that we're taking to increase capacity, both in our existing footprint as well as through expansion in our network, including step-change investments in automation that Donnie referenced. We're also taking significant actions to transform our cost base, and we'll continue navigating the increase of inputs with pricing to offset inflation as necessary.

And so you do recognize that there is inflationary dynamics that we're mindful of as well as continuing to keep a very close watch on the elasticities as we go throughout the second half. But as we look holistically in terms of the strength of this business, the demand outlook, coupled with investments

across our portfolio, mix opportunities within the business, which includes organic discriminating investments as well as inorganic portfolio shaping and aggressive cost transformation, we're confident in our path to deliver sustainable double-digit margins. And then for the year, as we referenced, we do expect to be in that 8% to 10% ROS range.

Ken Zaslow

Great. I appreciate that. And then my second question is, when you think about the cattle cycle longer term, there seems to be a fair bit of new capacity announcements over the last six-or-so months going out 2023, 2024. How do you think about that new capacity versus the cattle supply versus the demand? And how does that impact how you think about margins longer term, not just this year? And with that, I thank you very much.

Donnie King

Thank you, Ken. I will start off, and then I will flip it to Shane to add a little extra color. In terms of incremental capacity, competition makes us better. So we're not frightened by that. We welcome that. But in terms of cattle supply because of the drought and herd liquidation and a number of other things going on, it will have some impact on supply in the cattle out front. In terms of our business, so I think it's really important to understand that a cow is not a cow and the fact that we work with our ranchers and feeders and we buy premium cattle. And that premium cattle, we pay more for it, but we also get a better cutout for it. And then we talked earlier about specialty products, particularly fats and oils and hides and the like and how that helps that whole cutout value.

So we've had some really extraordinary margins over the last couple of years. We don't think that will maintain that level. It was a point in time and a shock to the system. However, we do believe that we will be in that 6% to 8% range on a go-forward basis because of some of those things that I talked about earlier.

And with that, Shane, anything I've missed if you'd like to—

Shane Miller

Yes. And thank you for the question. Donnie, you hit on most of it here. I would say a couple of things here, and I mentioned it earlier, that from a cattle genetics perspective and the quality that our feeding partners are bringing to the marketplace today, it's never been better. And the drought conditions that are plaguing, I'd say, over 50%, 55% of the country continue to persist. So you've seen heavy cow liquidation year-to-date that's impacting the forward curve because this is what's going to impact you two and three years out. And that's due to the lack of grass and forage that's in the country right now. So as Donnie mentioned, we expect to see more competition for livestock here as we go forward. We're laser-focused on staffing our plans, building our supply chain, enhancing our relationships, servicing customers and performing with the best.

And this is a very competitive industry, and it always has been. But at the end of the day, it's having a diversification of programs and customers. We feel we offer a solution to customers through our case-ready business with two new plants that have been added here this past year. They're going to lend to our overall success, too. So yes, we're seeing higher prices here from a cattle perspective, and we anticipated that here, and we continue to navigate that. But your point and your question is spot on, there's going to be more competition in the future.

Ken Zaslow

Great. I appreciate it, guys.

Stewart Glendinning

Ken, Stewart here. Just one thing to add. I think it's important to just think about how this impacts the shape of the year. Ken Goldman opened with a question on sequential improvement. That answer I gave him, just so all of you are really clear, related specifically to Chicken. That was Donnie's comment on Chicken, sequential improvement in Chicken and the guidance that supports that. But my comment on Beef, which ties into your question, is that you have to watch Beef in the back part of the year when you start thinking about Tyson as a whole because the first half of the year has been better. It's been a better half of the year, 16% in total. And that's been a great result for us. Of course, the back part of the year, we'll start to see that come off.

And in the coming quarters, we'll be able to give you the guidance on the future years. But be clear that we've been consistent in Investor Day and in recent calls in saying that we think that global demand for beef is strong and so long as the cattle are there to supply that. Over the long haul, Beef, we think, will be a better business than it has been historically.

Ken Zaslow

Great. Thank you very much.

Donnie King

Thank you, Ken.

CONCLUSION**Operator**

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

Donnie King

Thanks again for your interest in Tyson Foods. We look forward to speaking to you again soon.

Operator

The conference has now concluded. Thank you for attending today's presentation, and you may now disconnect.