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TSN - Q3 2012 Tyson Foods Inc Earnings Conference Call

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OVERVIEW:

TSN reported 3Q12 sales of $8.3b, operating income of $336m and EPS of $0.21. Expects FY12 revenue to approximate $33b and FY13 revenue to approximate $35b.

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PRESENTATION

Operator

Welcome to the Tyson quarterly investor earnings call. All participants are in a listen only mode until the question and answer session.

(Operator Instructions)

Today's conference is being recorded. If you have any objections please disconnect at this time. I would now turn the call over to Mr. Jon Kathol, Vice President Investor Relations. You may begin.

Jon Kathol - *Tyson Foods - VP, IR*

Good morning and thank you for joining us today for Tyson Foods conference call for the third quarter of our 2012 fiscal year. I need to remind you that some of the things we'll talk about today will include forward-looking statements. Those statements are based on our view of the world as we know it now, which could change. I encourage you to look at today's press release for a discussion of the risks that can affect our business.

On today's call is Donnie Smith, President and Chief Executive Officer; Jim Lochner, Chief Operating Officer; and Dennis Leatherby, Chief Financial Officer. To ensure we get to as many of you as possible, please limit yourself to one question and one follow-up and then get back in the queue if you have additional questions. I'll now turn the call over to Donnie Smith.

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Donnie Smith - *Tyson Foods - President and CEO*

Thanks, Jon. Good morning everyone and thanks for joining us today. Earnings for our fiscal third quarter were $0.21 a share, compared to $0.51 in Q3 of last year. And keep in mind, earnings were impacted by $167 million, or $0.29 a share, for the early extinguishment of the 2014 notes. Adjusted EPS was $0.50 for the quarter. I'm very pleased we were able to pay off that debt early which strengthened an already strong balance sheet, lowered our interest expense in upcoming quarters and helped us get back to an investment grade with all three rating agencies. This was an important milestone for our team and I'm proud of them for accomplishing this goal.

Sales rose slightly to $8.3 billion, compared to $8.2 billion in Q3 of '11. For the quarter, Chicken sales were up 3.6% in large part due to an 8% increase in pricing. Even though Beef pricing was up over 15% versus a year ago, sales dollars were down slightly due to a 14% decrease in volume. Both Pork and Prepared Foods sales were down by about 4.5% to 5%, driven largely by softer pricing. Although let me hasten on to add, that year-to-date our pricing is higher in all segments, driving sales growth of 4.4% across the entire portfolio.

Operating income for the quarter was $336 million, compared to $312 million in the same quarter last year. The Prepared Foods segment was above its normalized range with a 6.2% operating margin, the Chicken segment was within its range at 5.3%. Our international Chicken operations faced significant headwinds in Q3 including start up issues in China and Brazil. Excluding these start up related losses, our Chicken segment had a 6.7% return on sales. The Pork segment came in just below its range for the first time in 10 quarters with a 5.1% return on sales.

Beef was just under its range with a 2% return. Considering the challenges Beef and Pork faced in the third quarter, I'm pleased they were able to produce as well as they did. And due to those challenges, along with softer demand and economic conditions, earnings for the year will come in lower than we previously projected but I'll hurry on to say that 2012 will still be a strong year and fourth quarter earnings should be within the range of results reported in the first three quarters. That's why we have a strategy in the business model we have, to manage through volatility. We have a few businesses that are having record years and all of our businesses have plans in place to deal with the headwinds that we know are coming.

Looking into 2013 we believe it's prudent to enter the year with plans to pullback some on our CapEx and be a little conservative with our cash in order to keep a good supply of dry powder. That's not to say we won't buy back stock or we won't make an opportunistic acquisition. We just want to be prudent in how we handle our cash. We worked hard to get our balance sheet back in order and to get back to investment grade ratings and we don't want to jeopardize that. Our plans to grow Prepared Foods, value-added Poultry and international are the best hedge against volatility. Providing value and getting paid for the value we create for our customers by being their go to supplier is the key to stability it and long term growth.

Now moving on to the macro environment, after four months of moderate decline, consumer confidence was up in July according to the Conference Board Consumer Research Center. Unemployment, however, was virtually unchanged which weighs on the pace of economic recovery. In the retail channel, according to The Perishables Group, for the 13 week period ended June 30, overall fresh sales -- overall sales of fresh meat were down 3.3% in volume versus the same period a year ago, driven by a 0.6% increase in price.

Beef and Pork volume were down 7% and 1.7% respectively. Chicken was the only category that saw pounds sold increase versus a year ago, but the increase was very slight at 0.2% and demand feels sluggish to us. The USDA forecast food prices will continue to rise in 2013, led by meat, eggs, and dairy as a result of the drought. Beef prices are expected to be up 4% to 5%, Pork up 2.5% to 3.5% and Poultry up 3% to 4%.

In the food service channel, Technomic revised its 2012-2013 forecast upward to 1.7% real annual growth, up 1.1% from its previous forecast. The National Restaurant Associations performance index was stable for June. And while we still feel sluggish demand in food service and the outlook is far from robust, these indexes might indicate that perhaps the worst is over. The NPD Group's consensus of commercial restaurant locations finds that numbers of both independent and chain restaurants have risen, with independents finally showing a slight increase for the first time since 2009, another hopeful sign.

There are specific high growth opportunities in an overall low growth market. According to Mintel, chicken focused concepts have done well through the post-recession economy and despite the heavy presence of discounting, many chains have been focusing on premium menu items

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like bacon and steak and will most likely continue to do so. Premium meats on burgers, chicken sandwiches and salads and other items are helping operators increase menu prices with an enhanced value perception. That concludes my remarks and now Jim will give you the specifics around our segments followed by Dennis with the financial report, and after that we'll try to get into more detail with the questions.

Jim Lochner - *Tyson Foods - COO*

Thanks, Donnie and good morning, everyone. With $47 million in operating income and a 6.2% return on sales in the fiscal third quarter, the Prepared Foods segment performed above its normalized operating range of 4% to 6%. I'm pleased with the continued improvement, and I see real opportunity for this segment. Prepared Foods is a key part of our Company's overall growth strategy, and we are actively seeking ways to expand this business into other categories and grow existing categories in 2013 and beyond.

The Chicken segment posted $153 million in operating income and a 5.3% return on sales for the quarter, which is within the normalized range of 5% to 7%. We are able to offset the slightly higher grain costs in the quarter through price and mix improvement. In China, our Chicken operations were negatively impacted by start-up challenges and compounded by economic and market issues. While we were pleased with the performance of our new company owned farms, at this point they represent less than 20% of the birds we process weekly. We are building new bio security controlled grow to farms and plan to phase out the use of uncontrolled market birds over the next two years. This will allow us to value up into a premium mix of branded, fresh retail trade pack and food service sales, but in the interim we will have some dependency on market birds and wholesale market conditions.

In addition to normal start-up issues, our Brazilian Chicken operation saw significant market deterioration in the fiscal third quarter, stemming from a very soft market for boneless leg meat in Japan. We are in the process of bringing up second shifts at two of our plants, which should improve our cost structure. We will continue increasing value-added capabilities to move beyond dependency on commodity export and domestic wholesale markets.

To help you understand our expectations for the level and pace of our international expansion, I'll give you the numbers around our plants for growth over the next two years. In China, we currently produce about 2 million birds per week and plan to reach 3 million a week in 2014. In Brazil we're at 1.3 million birds with plans for 2 million, and India we grow from 280,000 to 450,000, and in Mexico, we intend to maintain production at around 2.7 million birds per week.

Turning back to domestic Chicken, obviously because of the drought, we expect grain costs, higher grain costs in 2013. Over the past couple of years we have substantially reduced a number of fixed price contracts we have with customers and currently have less than 15% of our Poultry volume and annual fixed price contracts. The vast majority of our contracts are tied to specific markets or allow for conversations about adjusting prices to move -- prices to offset higher input and we will continue to push for even more of these types of contracts. I believe supply will begin to rationalize as well, making it easier for us to have those pricing conversations. The capital investments and operational improvements we made in recent years have put us in good position to handle higher inputs through efficiencies. Based on current grain futures, we believe our Chicken segment will remain profitable in 2013.

In our Pork segment we produced $69 million in operating income and a 5.1% return on sales, which is below the normalized range of 6% to 8%. Unfortunately supply and demand got out of balance, but it wasn't due to a shortage of hogs as some may think. Increased domestic availability partially due to heavier hogs, along with pricing pressure, caused the industry to get out of balance and packer margins were compressed more than prior quarters. Our Pork margins are starting to come back to normalized levels now. Supply of hogs should be 1% to 2% higher the first three quarters of fiscal '13, and we do not see any material demand shifts on the horizon that would be detrimental to our Pork segment's performance next fiscal year.

Moving on to the Beef segment, we had $71 million in operating income and a 2% return on sales in the third quarter. This was just below our normalized range of 2.5% to 4.5%. Considering how difficult the month of April was for us, I'm pleased we are able to make up so much ground in May and June, and I'll go on to add that we focused on maximizing revenue through price and mix to enhance margins, not market share. Looking to cattle supplies, the 2012 calf crop was down as expected, which will impact the late calendar 2013 and calendar 2014 fed Beef supplies. Based on the last inventory report, we currently aren't seeing any definitive signs of heifer retention. Additionally, more feeder cattle were imported into

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the country than anticipated in the past six months to partially offset last year's reduced calf crop. We expect close to the same supplies for the rest of fiscal '12 and into the first half of fiscal 2013 that we experienced this year.

Similar to last year, feeder cattle are coming into feed lots earlier as a reaction to the drought. We do see a supply drop off in the back half of '13 as a result of the lower 2012 calf crop and slaughter capacity will likely adjust to lower volumes. I'll remind you that Tyson Beef plants are located in traditionally cost effective cattle feeding areas, and we expect to have adequate supplies to run our plants at a profitable level. We believe the Beef segment will remain profitable in fiscal 2013, but will have challenges similar to what we experienced in 2012.

In conclusion I'll say that we are proud of the operational and sales improvements our business units have delivered over the last couple of years. This has positioned us well to deal with increased Beef costs and the Chicken segment. We have a strong balance sheet, diversified protein product portfolio, and we've been investing in our plants to make them extremely efficient with mix improvements. So we're in very good shape to get through the near term challenges ahead and with that, Dennis?

Dennis Leatherby - *Tyson Foods - CFO*

Thank you, Jim and good morning everyone. As Donnie mentioned in his remarks, we reported Q3 earnings of $0.21 per share, or $0.50 per share after adjusting for a charge of $167 million, or $0.29 per share related to the extinguishment of our 2014 notes, which I will address in a moment. Return on invested capital for the last 12 months was 14.7%. Capital expenditures were $186 million for the quarter and totaled $530 million through three quarters of fiscal 2012. We continue to invest in numerous capital projects for both our domestic and foreign operations that will result in improved productive capabilities and drive labor efficiencies, improved yields and sales mix. Our operating cash flow through three quarters of fiscal 2012 remains strong at $719 million.

Including cash of more than $800 million, net debt was $1.6 billion. Total liquidity was $1.8 billion, well above our targeted range of $1.2 billion to $1.5 billion. Gross debt increased to $2.5 billion. The increase in gross debt was due to a successful 4.5%, $1 billion note offering, which we then used the note proceeds to extinguish our 10.5% 2014 notes. We were able to tender and purchase $790 million of the $810 million principal on the 2014 notes prior to June 30. Subsequent to the settlement of the tender offer, we called for redemption of the remaining $20 million, and we can now say the high yield 2014 notes are fully extinguished. As a result, we incurred a charge of $167 million during the third quarter related to this early extinguishment.

Going forward this refinancing will reduce our annualized interest expense approximately $55 million, which equates to about $0.09 per share. At the same time as we issued the new bonds, we also received an upgrade from Moody's, which means we are now back to investment grade with all three rating agencies. Personally it feels really good to have a debt maturity profile and interest costs that are reflective of being an investment grade company again. Gross debt to EBITDA for the last 12 months was 1.6 times. On a net debt to EBITDA basis this measure was 1 times.

During the third quarter we acquired 3.9 million shares for $75 million under our share repurchase program. Since reactivating this program in 2011, we have repurchased 19 million shares for $350 million, representing a reduction of about 5% of our outstanding shares. At this time we believe it is prudent for us to reduce our share repurchases under this program until we have better visibility into our working capital needs. Returning to investment grade was very important to us and we are going to be disciplined concerning our balance sheet, which we believe to be a source of competitive advantage.

Our average diluted shares outstanding for the third quarter was 369 million. This reflects the dilutive share effect totaling 5 million for options and 3 million for convertible bonds, which will fluctuate depending on our stock price performance. Our effective tax rate for Q3 was 42.4%, or 37.9% without the charge related to the early extinguishment of the 2014 notes.

Now here is an update on the outlook for the remainder of fiscal 2012 and a few items pertaining to fiscal 2013. Revenues for fiscal 2012 are expected to approximate $33 billion, down $1 billion as previously estimated due to weakened domestic protein demand. Revenues for fiscal 2013 are expected to approximate $35 billion, mostly resulting from price increases associated with increased raw material costs and expected decreases in overall domestic availability of protein. We expect 2012 net interest expense to be approximately $340 million, including the $167 million charge related to the early extinguishment of the 2014 notes. For fiscal 2013 we expect net interest expense to be in the $130 million to $140 million range.

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The effective tax rate for fiscal '12 should be around 37%. CapEx should be around $700 million. Although down from our previous estimate, the anticipated projects are moving along but will not be completed in fiscal 2012. This amount still well exceeds our depreciation and amortization levels. Our preliminary capital expenditures plan for fiscal 2013 is in the $500 million to $550 million range, down from fiscal 2012 until we have better visibility into our working capital needs. However, as with share repurchases, if forecasted conditions change we may increase our planned capital expenditures.

In closing, we are pleased with our Q3 results and are confident in our ability to end fiscal 2012 with another strong quarter despite the ongoing challenges with soft protein domestic demand and high grain prices that appear to be in place for the foreseeable future. The moves we have made to strengthen our balance sheet over the past few years and recent capital restructuring will allow us to face those challenges head on and continue executing our strategy as we head into fiscal 2013. This concludes our prepared remarks. Now I'll ask Wendy to begin Q&A.

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions) Heather Jones, BB&T Capital Markets.

Heather Jones - *BB&T Capital Markets - Analyst*

Good morning.

Donnie Smith - *Tyson Foods - President and CEO*

Good morning.

Heather Jones - *BB&T Capital Markets - Analyst*

First question is on your Poultry business. I was wondering if you could give us a sense of what your Poultry profitability looks like if you take today's spot grain and market prices, as well as what you think it will look like in the September/October time frame if we get the typical seasonal decline in Chicken prices.

Donnie Smith - *Tyson Foods - President and CEO*

Okay, so Heather let me make sure I've got the question right. So you're asking what -- if our cost of goods were to immediately reflect the cost of what spot ingredient purchases would cost and there was no impact on revenue, right?

Heather Jones - *BB&T Capital Markets - Analyst*

Yes.

Donnie Smith - *Tyson Foods - President and CEO*

Okay, so first of all let me say we don't have that scenario. Our grain group has done a good job and they've got us coverage out a couple months in front of us well below the market. So this scenario is purely hypothetical, but let's think about it. At current values, spot corn is probably going to deliver something like $9 a bushel. Meal you're probably going to be something like $550 delivered, so that's probably going to count to a live

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cost in the low 50s, let's call that say $0.52 a pound. So today, our live cost is probably just a tick under $0.45 a pound. So our live cost would go up immediately $0.07 a pound. Now yielded, that's probably going to be like $0.10 on the finished pound. So we're not making $0.10 a finished pound today in Chicken. So no, in that hypothetical scenario, and I'm really glad it is hypothetical, we would not make money.

Now, thinking back if I look at -- we participate in benchmarking services, a couple and so looking back at June, we were top quartile in one, top tertile in the other. So we're operating across all of our businesses fairly well. And if I think back to the top spots in those surveys, probably the number one, number two spots were around that $0.10 a pound mark. I'd say pricing has probably softened up a little bit now versus June. We've seen breast meat prices come down and such and obviously, the live cost is probably going to be a little higher. So in your scenario, no we wouldn't be profitable and I don't think anybody would be, just based on what we see in those benchmarking services. Now, going forward into the Fall, fortunately our cost of goods in Q4 is going to be fairly well contained. I do anticipate -- and we've seen a little bit of softness in the last couple weeks -- that with the current supply, pricing is likely to soften a little bit going into Q4 as it typically does. And then into the Q1 on into the Fall, that typically is not a very strong pricing period too, so that's kind of our view going forward.

Heather Jones - *BB&T Capital Markets - Analyst*

Okay, thanks, and on a follow-up, let's just -- you talk about probably being below your normalized range for beef in 2013, but if we put you at the 1% to 1.5% range for fiscal '13, most of the industry would be losing money. And further, even if without the drought, from a long term structural perspective, some of your peers are poorly positioned. So I'm just wondering, do you think that this drought will hasten what probably needed to happen anyway and have some of your competitors shutter some capacity? Just wanted to get your thoughts on that.

Jim Lochner - *Tyson Foods - COO*

This is Jim. The drought definitely will have a long term impact on the overall Beef supply because I do believe that it's done a little bit what it did last year, and obviously it starts to make cattle come to the feed lots earlier. It changes some of the geography of where they're fed. But more importantly this year, what it's doing as well is the price of corn going up caused a radical correction to the feeder cattle pricing with that revenue dropping as much as $200 a head over that time frame. So one short run, what that did is probably stopped any heifer retention that was going on or anticipated to go on. And you have to remember that those heifer calves now won't be probably staying in the herd, will go into the feed lot. So over the next six months to a year, they would be into the feed lot numbers.

But over the long run, we'll have to see capacity adjust likely either through plant closing or capacity utilization reductions. And we always got to remind everybody that our plants have always been situated where the cost competitive feed lots exist and the peripheral feed lots generally have a higher operating cost and then on top of that, they have a higher freight cost to get cattle to the plant when they get outside their region. So I think that's a key component, so I agree that we'll probably have to see and we'll likely see some capacity utilization reduction. Timing of that is difficult to look at and nail down, but in general that's correct. And then I think one other thing on cattle, we've seen dramatically a shift in the length and time cattle are fed, which has reduced those feed lot turns probably in combination of higher grain costs and the accelerated movement, particularly last year from the drought with cattle being in the feed lots longer. So it's a lot more difficult than it's been in prior years to predict exactly what we think is going to happen on a timing basis for availability. So that's a fairly long answer to that question, but that's what we see.

Heather Jones - *BB&T Capital Markets - Analyst*

No, it's very helpful. I appreciate it, thanks.

Operator

Akshay Jagdale, KeyBanc Capital Markets.

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Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

Good morning.

Donnie Smith - *Tyson Foods - President and CEO*

Good morning.

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

My first question is on Chicken, just to follow-up on the previous question, so you said the hypothetical is not what you're dealing with in '13 so I just wanted to be clear. Are you hedged through 2013? My guess is no, so at some point in 2013, fiscal '13, you are going to see higher grain costs if they stay where they are today so the fact that you're saying you still remain profitable tells me that 85% of your revenue base that's flexible you believe will adjust. Is that the right way to think about it?

Donnie Smith - *Tyson Foods - President and CEO*

Yes, you're reading it correctly. We're a couple months out in front on our grain cost, which pretty much covers us through Q4 and that's -- what we really wanted to do in our grain strategy was to get us into new crop, frankly, I would have liked to have seen a better new crop to get into but be that as it may, it is what it is. So we are covered through the end of September so as we get into new crop, our grain costs will likely go up looking at today's markets, but you're exactly right. A few things are giving us the optimism about being profitable.

Number one is the pricing and the opportunities there but also, we've spent a lot of money on our Chicken business in the last couple years. We still think there's some room for operating efficiency gains, probably in the order of about another $100 million. Jim mentioned and I think I did too about our international operations, having a really tough quarter and we think those will improve, the environment will improve there coming into 2013, that will help some. We are going to continue to sell more value-added and as we do, that will improve the revenue side of our business.

And two, our buy versus grow strategy has given us a cost advantage because we're not saddled with parts of the chicken that don't carry very high revenue and we're able to buy the parts we need at generally below our cost and convert those into value-added items. So you add all that stuff up and that's what gives us the optimism going into 2013. And by the way, going into 2013, our estimate as of about a week ago and this corn market is bouncing around like a yoyo. But as of a week ago, we were anticipating an incremental $700 million in grain costs in 2013 just to kind of --

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Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

That is impressive if you're able to achieve that. So the next question is what's the supply scenario that you're assuming as being probable for next year for the industry and what could change that. So most people expect a 2% to 3% cutback could get the commodity prices up 10% or more and offset these higher grain costs, but I'm assuming you'll be profitable even if there's no further cutback. Please correct me if I'm wrong there, and what do you think the industry is going to do, when will it happen and what might that do to your EBIT margins in Chicken?

Donnie Smith - *Tyson Foods - President and CEO*

Okay, I think I understood your question, so we are predicting or in our model for 2013, we do have current slaughter pounds in the forecast. Now let me talk about what we think is going to happen. Let's look back, well about a year ago this time or so we were talking about this. We looked back at a couple of periods now when our Chicken business has been in that 6% or so range, that April, May, June period of '09 and during that time, we had a 6% return on sales and slaughter pounds were running around 860 a week for the industry, and that gave us the environment we needed to be able to get the pricing we needed up on top of our cost structure. Now let me hasten on to say during that year, corn was around $5

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and meal was somewhere between $325 and $350ish. So then fast forward now, up into 2012, third quarter just ended 2012, you've got about $880 million-ish or so slaughter pounds and you've got probably $7 corn and $360 meal. So what made the difference there?

It was all those things we mentioned before, the operating efficiencies, more value-added, our buy versus grow strategy, all those things. And so if you look at now, the impact of this $0.07 a pound live production increase, it would just make sense to us that something South of that 860 million slaughter pounds, which by the way I think is pretty close to your math of 2% to 3%, is probably the minimum to provide the environment that we're going to need to be able to get our pricing structure up on top of this cost structure that's coming our way.

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

And when might that happen relative to historical norms because it usually takes six months of losses before the industry starts cutting back. Do you think it might happen sooner?

Donnie Smith - *Tyson Foods - President and CEO*

Yes, I can't comment on that, but I can tell you that the current situation is untenable.

Jim Lochner - *Tyson Foods - COO*

I think the key is we've had a rapid run up in grain and the drought and the overall supplies of grain worldwide don't look like we're going to see a radical correction downward. So the optimism waiting for a grain market to correct down isn't there, so that to me shortens the potential time frames.

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

One last one for Jim. On Beef, are you assuming -- you are I think around $50 a head in Beef and my guess is April was negative. I'm assuming you're above normal range today?

Jim Lochner - *Tyson Foods - COO*

Today meaning last week?

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

Yes, last week or in the month of June, I'm assuming you are above normal and that's continued?

Jim Lochner - *Tyson Foods - COO*

The month of May and June corrected. We got the relationship with the revenue increasing above the cattle cost, and our effort is always to run for gross margin as best we can, and that means maximizing the revenue at the beef, maximize the mix, watch our costs and really look at the forward supplies of cattle and the forward demand and try to keep those in harmony.

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

Okay, thank you. I'll pass that on.

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Operator

Farha Aslam, Stephens.

Farha Aslam - *Stephens Inc. - Analyst*

Hi, good morning.

Donnie Smith - *Tyson Foods - President and CEO*

Good morning.

Farha Aslam - *Stephens Inc. - Analyst*

Do you think that there would be chicken producers who would choose not to cut production and just because of a good balance sheet would keep their production flat and power through this current negative grain environment?

Donnie Smith - *Tyson Foods - President and CEO*

I just couldn't say. For us, we, last year we cut production 6% to 8% and we have held solid with those cuts all year long. That allows us to buy meat on the outside market. And I'll tell you, through Q3, we probably bought 60 loads of meat on the low side and over 100, maybe between 115 and 120 loads of meat a week on the upside. And then bought it below our cost in most cases and brought that into further process it, which meant we didn't have parts of the bird that would be an oversupply that would have hurt our sales revenue. So I can't speak for what somebody else may be thinking about with their balance sheet. I'm really proud of our team for doing a great job.

If I look at our Chicken business, Donnie King and his group have taken over $900 million out of our cost structure since, call it mid '08. That's significant. They've done a great job. They've been very, very prudent in how they spent their capital and they've got these plants running great. And so all those things put together, give us the optimism, but I can tell you we don't have any plans to increase our production at all, don't have any plans to cut anything further. If demand erodes, we might buy a few less loads on the outside, but we're continuing with our production cutbacks. I can talk about us. I can't speak for the rest of the industry.

Farha Aslam - *Stephens Inc. - Analyst*

That's helpful and just as a follow-up on Pork, could you share with us the timing of how you see animals coming to market? Do you expect a huge Fall rush of hogs, and we're hearing that potentially there might not be enough shackle space, and then do you expect it to tighten up going into next year as higher grain costs hit the hub producers?

Jim Lochner - *Tyson Foods - COO*

Typically you do start to see increased numbers coming off of the Summer heat and usually they come in the June time frame, as from prior year's Summer heat as it affects fertility rates. As we would expect that coming into the back half of August into September or October, we'll see what we used to call the normal Fall run and we would expect numbers at this point to be 1% to 2%. I don't think they will be anywhere close to pushing the maximum slaughter capacity of the industry and then you always have to, you just look at the whole cycle approach here and say that high priced grain will impact production, but you still have a pipeline of about 10 months in production that's coming at you. So I'd say that the impact of producer profitability we'll start to feel 10 months from now and then this Summer's heat also will have probably some issues as we get into next Summer's processing.

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Farha Aslam - *Stephens Inc. - Analyst*

Okay, thank you very much.

Operator

Vincent Andrews, Morgan Stanley.

Greg Van Winkle - *Morgan Stanley - Analyst*

Hi guys. This is Greg Van Winkle from Vincent's team. My question relates to Pork. Wondering if you've seen any increase recently in hog supplies as a result of breeder sales being sent to slaughter? And you addressed a little bit with the last question, but what do you expect in terms of hog reductions going forward after the run-off we've seen in feed costs?

Jim Lochner - *Tyson Foods - COO*

We're not in the sow processing end of the business, but I am hearing that there are more sows being offered and you would expect to see some early liquidation as a result of the run-up in grain prices, but that's what we're hearing. I'll just have to monitor it week over week and month over month to look at what the projected long range supplies are going to be.

Greg Van Winkle - *Morgan Stanley - Analyst*

Okay, and what assumptions go into your outlook for Pork margins? You seem to be pretty optimistic about fiscal 2013, even though it seems to me like we'll need higher hog prices to make producers profitable and it seems like maybe the domestic demand environment is still a little weak so I'm just wondering what's driving your optimism there despite what seems like a challenging environment?

Jim Lochner - *Tyson Foods - COO*

What drives my optimism is you've still seen really strong export demand, you've seen an industry that can flex on the live production side, it's also put down a lot of efficiencies. We'll have to just watch and see what will happen as overall protein prices increase, whether or not how much demand destruction there may be or won't be.

One interesting thing that's going on this year with the drought, there's been so much communication out in the popular press about affecting higher prices because of a reduced corn crop, so I do think that at least we'll start to see some acceptance and maybe a little less demand destruction, and we'll definitely have ample supplies to the majority of our fiscal '13. So the other key component that I think one always has to look at is that the high grain prices in the US are affecting worldwide grain prices, and we're still the most efficient producer of Pork and Chicken throughout the world. So again, the US should be favorably impacted from an overall efficiency in export. So those are a lot of different reasons why I don't see anything real detrimental on the horizon in Pork.

Greg Van Winkle - *Morgan Stanley - Analyst*

Okay, thanks, that's very helpful. I'll pass it on.

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Operator

Christine McCracken, Cleveland Research.

Christine McCracken - *Cleveland Research Company - Analyst*

Good morning.

Donnie Smith - *Tyson Foods - President and CEO*

Good morning.

Christine McCracken - *Cleveland Research Company - Analyst*

Jim, you talked a little bit about liquidation maybe not happening as quickly here, but we're seeing quite a bit of liquidation it seems in some of the other countries that we export into, specifically into Mexico and that's been mentioned by some of your peers. I'm wondering, could you see a slowdown in exports you think in the near term as some of that liquidates and then it's setting up for a really strong export outlook maybe into 2013?

Jim Lochner - *Tyson Foods - COO*

I'm not sure which species you're referencing.

Christine McCracken - *Cleveland Research Company - Analyst*

Really --

Jim Lochner - *Tyson Foods - COO*

The pork producing country --

Christine McCracken - *Cleveland Research Company - Analyst*

We've heard quite a bit about pork specifically. You've seen some liquidation in the cattle side in Oceania and in the pork side, it's primarily the hogs in Europe, which maybe create some export opportunities for us, Mexico, I think Canada is also bringing quite a bit to slaughter. So I'm just curious kind of universally on the red meat side, obviously the AI situation in Mexico is also perhaps creating a near term pull.

Jim Lochner - *Tyson Foods - COO*

Let me just -- my last answer, I do think that we'll continue to see demand for countries we export to, which hopefully will persist. If there are that degree of liquidation against the small base, I don't look at their liquidation putting extra pounds on the market that have to be -- that are going to materially impact their need to import product. Clearly the AI scenario in Mexico has some issue relative to overall chicken movement within the country, which appeared to strengthen pricing here in the last several weeks. And then in the EU, you continue to hear about big production being curtailed from a variety of different reasons. But, again, as I mentioned in the previous answer, worldwide grain prices are going up as well so the world's protein producers are going to feel this impact and the US is the most efficient place to grow pork and chicken. So I would expect that we'll see that long term ramification from that.

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Christine McCracken - *Cleveland Research Company - Analyst*

And then Donnie, you mentioned what sounded like an improving food service environment. Just curious, what your customer conversations are looking like in light of this increase in protein prices and possibly higher fuel on the back of lower ethanol production. And also with wing prices so high this year, how much higher can they go relatively in order to offset some of the feed. Might some of that increase have to come on the back of boneless?

Donnie Smith - *Tyson Foods - President and CEO*

The best way I would characterize food service demand is it's a little bit -- it's sluggish but finally, there's a little bit of optimism so maybe this thing has quit going down so that's not a very -- there's a little bit of optimism there but not a lot. So as far as the conversations are going, I think people understand there's nobody confused about the drought and its impact on the meat industry and meat producers. Also though, they're well aware of the current supply situation so there's not an immediate need to make a pricing adjustment. So the conversations are largely around we understand it's coming and when it gets here, we'll participate because you guys do a great job taking care of us in service and quality and you're the innovation leader and that kind of thing. So does that answer your question?

Christine McCracken - *Cleveland Research Company - Analyst*

Yes, just on the Wings. I'm a little bit worried given how high they got this year that they would be able to take on much more.

Donnie Smith - *Tyson Foods - President and CEO*

Yes, it's interesting. If you go back in just about every year regardless of where the Wing price starts, when you go into the winter Wing season, Wing prices escalate so we may test that this year but so far, every year Wing prices go up during Wing season.

Jim Lochner - *Tyson Foods - COO*

I want to add one other thing. We do spend a lot of time with customers showing them the supply demand fundamentals, what's out in front of them and what the moves are and that does help immensely. The dialogue gives them some anticipation of what they think the supply will be relative to demand and forward, and they are thinking about prices.

Christine McCracken - *Cleveland Research Company - Analyst*

Not the first time we have gone down this road in any case. Thanks.

Operator

Ken Goldman, JPMorgan.

Ken Goldman - *JPMorgan - Analyst*

Hi, good morning everyone.

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Donnie Smith - *Tyson Foods - President and CEO*

Good morning.

Ken Goldman - *JPMorgan - Analyst*

Can you elaborate a little bit -- and forgive me if you talked about this already -- on the soft domestic demand you highlighted, is it primarily in a certain species or across-the-board? To what degree are consumers trading down? Where are you seeing it? Just a little more color there would be appreciated if you can.

Donnie Smith - *Tyson Foods - President and CEO*

Let's talk about retail first. Overall fresh meat sales are down. As pricing increases, it does hurt volume. Sales dollars are there, but volume is down. Beef and Pork are down more than Chicken. Fresh Chicken sales are about flat, Beef is down and Pork is down. At food service, really Chicken has had a pretty good Summer at food service. Demand for the other items is fair at best.

Pork has actually been probably the softest between Beef and Pork. We tend to look at holiday seasons as an indicator for things to come and Memorial Day was just average at best, and then when we went into the 4th of July, Chicken demand was just fair. Pork was a little bit soft. Beef did okay. Beef got a lot of feature activity in retail during the 4th of July holiday.

As we look at it now, as prices edge higher, it's probably going to hurt demand. We haven't really seen -- well you might call 4% to 5% volume down in Beef and Pork and flat Chicken meaning some shift into Chicken. You might interpret that, but really we haven't seen what I would call wholesale movement between the proteins. They are trading down within the category from more expensive muscle cut, maybe down into grinds and that kind of thing, but really haven't seen wholesale movement between the proteins.

Jim Lochner - *Tyson Foods - COO*

I'd add one other thing and that is even with the Perishable data showing down 3% in 4 weeks and 13 weeks down 1%, and the volume is down 8%, the wholesale prices of Beef have been high. And they've been higher than a year ago, so the balance of the cutout has still been high.

Ken Goldman - *JPMorgan - Analyst*

Okay, thank you. And then just generally, as you think about approaching a year when input costs could be a headwind and obviously looks like it will be, I realize you're going to stay on target with your long term strategies but are there tactical moves you perhaps might make this time rather than at the time when inflation is a little bit less onerous. It looks like some of what you're doing with capital spending and share repurchase is that, but just trying to get a sense for what other adjustments you can make in running your business now versus what it looked like a few months ago.

Donnie Smith - *Tyson Foods - President and CEO*

Yes, you've mentioned the primary two. We want to keep more dry powder around us and just be cautionary. And as we get into the year and we get more visibility into what our working capital needs are going to be, I have absolutely no problem continuing to invest in the business. Obviously there are acquisitions that are out there that may interest us in the future, buying our stock back, I think we're a great value. So all those things are there.

Other than that, no, we really don't want to change our strategy. We're on point, growing our value-added businesses, doing those things we need to do to take care of our customers and lead with quality, our services, innovation is our guys have done a great job. Noel White and his group have

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done a super job with the premium programs in Beef and Pork and continue to operate their business better than the indexes that they compare themselves to. So no, that's the whole point was to weather the storm and get to a point like this to where we could continue down our path and have a balance sheet that would support that.

Ken Goldman - *JPMorgan - Analyst*

Thank you very much.

Donnie Smith - *Tyson Foods - President and CEO*

You bet.

Operator

Ken Zaslow, BMO.

Ken Zaslow - *BMO Capital Markets - Analyst*

Hi, good morning, everyone.

Donnie Smith - *Tyson Foods - President and CEO*

Good morning.

Ken Zaslow - *BMO Capital Markets - Analyst*

I know you touched on it but trying to get more hard core answers, is how much production cuts do you expect to the industry and what will your participation be?

Donnie Smith - *Tyson Foods - President and CEO*

Let me go to the latter. What we did was look back in the environments that happened before when we got into an environment where we could add pricing but in our business, we have remained cutbacks, the 6% or 8% we did back a year ago, and we're going to continue with our current production plans is the plan now. Now things may change depending on what grain does or something like that but currently we don't have any plans to change our production because we're producing well below our demand today, thus buying all the parts we're buying. So we like our production model being well short of our demand.

Ken Zaslow - *BMO Capital Markets - Analyst*

And because your comment in the Press Release is changing crop conditions and pricing could reduce or change the USDA outlook, so I'm assuming you guys think there's going to be some production cut. I'm just trying to figure out what extent do you think it is and how confident you are in that.

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Donnie Smith - *Tyson Foods - President and CEO*

Yes, go ahead.

Jim Lochner - *Tyson Foods - COO*

I think we look back a lot and do a lot of work looking at history, correlating live pounds and over production against demand, and the data that basically says to increase price, you've got to pull back production and the market will have to do its job. How fast that happens, under what environment is difficult for anybody to predict, and then I think as we look across-the-board, history tells us that will happen. Who, how fast and when is virtually impossible to tell. We have thoughts, but we are certainly not going to talk about anybody specifically. As Donnie keeps saying, we manage our own business and a lot of focus on demand forecast by part, what our production runs are going to have to be and manage it out 13-14 weeks in advance, and we do know what we have ahead of us with increased live production costs. So we have to work on pricing and all of the dialogue associated therein.

Ken Zaslow - *BMO Capital Markets - Analyst*

The other question is if you guys are projecting at least breakeven, if not positive, what would that be for the industry? I'm assuming you're outperforming the industry. Can you give us a metric to which you are outperforming the industry?

Donnie Smith - *Tyson Foods - President and CEO*

I mentioned in an earlier question that we're top quartile in one of our benchmarking services and top third in the other, so that's about as much as I could say about how we compare.

Ken Zaslow - *BMO Capital Markets - Analyst*

Okay. Great. Thank you.

Donnie Smith - *Tyson Foods - President and CEO*

Sure.

Operator

Ryan Oksenhendler, Bank of America Merrill Lynch.

Ryan Oksenhendler - *BofA Merrill Lynch - Analyst*

Good morning, guys.

Donnie Smith - *Tyson Foods - President and CEO*

Good morning.

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Ryan Oksenhendler - *BofA Merrill Lynch - Analyst*

Jim, I want to follow-up on Ken's question and your answer and some of the previous questions. In terms of -- is this time different where historically you said when you cut supply pricing will go up, but is demand weak such that you actually can't pass it through this time? And looking at getting back to Christine's question in terms of Wing prices at all -- really high levels, weighing our leg quarter and breast meat prices didn't really move that much higher this year in relation to where they are relative to their cold storage levels and where production levels were in general for the industry. So in terms of your optimism for pricing next year, leg quarter cold storage inventories are at the lowest level in three years since they've changed the data and breast meat is at the lowest level in several years, so could you comment about that in your ability to take pricing next year?

Donnie Smith - *Tyson Foods - President and CEO*

You're making a good point for us, Ryan, because inventories are low and that's certainly an advantage to us but think, we're facing today not knowing what's in front of us. $9 corn delivered and $550 soybean meal, which is going to have your live cost above $0.50 a pound. Somewhere in the neighborhood of $0.52 a pound, that frankly is just untenable. So we talked about earlier as we went back into earlier periods when there was 860 million slaughter pounds, and in those environments we had the pricing structure that we needed to get on top of our current cost. By the way, we've improved our business since then. But if you just look at that, it stands to reason to us that with this wave of feed costs coming at us you certainly would need to be below that level in order to have a favorable pricing environment. Now, our forecast for the year is to operate profitably in this environment so anything -- any time the environment improves, that should be additive to our business.

Jim Lochner - *Tyson Foods - COO*

The only thing I'd add is my comments previously that I'd add now would be you've seen different parts of the bird, particularly, carry a different percentage of the overall with breast meat being soft, Wings high, leg quarters running pretty strong prices all year, and again we really try to manage through a total revenue component and look at where the opportunity to maximize that be it in country, be it export. So I think the market, will there be demand restructuring with higher prices? Generally that's normal activity and the supply generally coming down, we'll have to offset it until equilibrium again occurs. So the timing of that is very difficult to call, but I do believe people will eat protein, the world will still have the same overall demand for protein, there will be adjustments on the parts, and we'll just have to see how fast it comes up to cover the increased live costs.

Ryan Oksenhendler - *BofA Merrill Lynch - Analyst*

Got it. And then can you just talk about have you guys been importing any corn from Brazil at all or contracted to do so?

Donnie Smith - *Tyson Foods - President and CEO*

No, not that we wouldn't if the math worked but we've got a lot of truck corn bought from local farmers close to our feed mills. And right now, the value, the imported values out of Brazil wouldn't compete with the costs that we've got, local truck grain bought for. But we run the math constantly and when it works, that's an avenue for us.

Ryan Oksenhendler - *BofA Merrill Lynch - Analyst*

Got it. Thanks and then just one last quick one, Jim, if you talk about volumes down 14% in Beef, how much of that -- you said lower cattle purchases, could you talk about what drove that or break down that 14% decline?

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Jim Lochner - *Tyson Foods - COO*

In that 14%, we did process fewer head, carcass weight was up and then or outside tallow purchases really related to the impact of the relationship we have with BPI with their volume down where we basically captured some of that tallow and sold it. So it was a combination of those three things on the line.

Ryan Oksenhendler - *BofA Merrill Lynch - Analyst*

Okay, thanks guys.

Donnie Smith - *Tyson Foods - President and CEO*

Thank you.

Operator

Tim Ramey, D.A. Davidson.

Tim Ramey - *D.A. Davidson & Co. - Analyst*

Good morning. First on the Brazil/China losses of $30 million, is there anymore color that you can give us on that and what did that relate to, what's the likelihood of that continuing and so on?

Donnie Smith - *Tyson Foods - President and CEO*

We're definitely seeing softness that you hear a little bit about in the China economy and that's affecting the wholesale values. What basically what the story is there, Tim, we have a young start up business that we run today largely dependent on market birds. The premiums we will get will come when we have these bio secured company owned houses, which that part makes up only about 20% of the 2 million head that we're slaughtering today. So when you combine -- now let me hasten on to say, the cost structure we see in those live production assets is great, the premiums that we see over the wholesale markets, both at retail and food service, is what we expected, so our business model looks right. It feels good. We're very optimistic about what we're doing there. It's just we're a young start up, fledgling business and today, we're way too dependent on wholesale markets and its been soft.

Pretty much the same story in Brazil as we move towards a more value-added mix. This boneless leg meat deal in Japan when that market closed, it kind of backed up through in effect the course and problems in economic problems in Europe have slowed down, breast meat prices there. So if you take the bone less leg meat market closing in Japan and the softness in the breast meat market in Europe, a lot of that had ripple effects into other markets and ended up backing up a lot of meat into the domestic business. And again, we don't have our value-added mix sold out like we want to yet, so we were very dependent on the wholesale markets and that was just not a good place to be in Q3.

We see some improvement now and we do predict steady improvement. It's liable to be a couple more quarters out though before we are feeling a whole lot better about that. And the story is, in Brazil, its plant's double shifted and get into that value-added mix like our business model says we have to do and in China, we can't build chicken houses fast enough. So the model is good. We'll get there. It's just we're too dependent on export and wholesale markets today.

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Tim Ramey - *D.A. Davidson & Co. - Analyst*

Got you and just a quick one for Dennis. If we were bridging to the $0.50, Dennis, what would we plug in for the tax component of the refunding of the bonds?

Dennis Leatherby - *Tyson Foods - CFO*

If we're going back to $0.50, if we didn't have the extinguishment of the bonds, it would have been 37.9%.

Tim Ramey - *D.A. Davidson & Co. - Analyst*

Okay, but do you know the dollar amount for the tax impact of the bond?

Dennis Leatherby - *Tyson Foods - CFO*

We can get you that, Tim.

Tim Ramey - *D.A. Davidson & Co. - Analyst*

Okay, awesome. Thanks so much.

Operator

Robert Moskow, Credit Suisse.

Robert Moskow - *Credit Suisse - Analyst*

Hi, thank you. I wanted to know what your capacity utilization levels are in Beef now, Jim. Your volume was down 14% in the quarter. Still had pretty decent margins, but you're going to be down double digits this year, you'll probably be down again next year. At what point does capacity utilization become an issue in Beef?

Jim Lochner - *Tyson Foods - COO*

The normal -- the issue really gets critical when you are going to average, I've got to get my math right here but I'll make it simple when you think you're going to average less than 36 hours it's critical. We were well north of that. We always do our capacity utilization on a six day week and I don't think we're not going to see volumes that are going to warrant much Saturday operation, but we were still in the high 70s on capacity utilization on a six day capacity. But you also got to look at that number because when you're adding value on your cut floors and going to more value-added mixes, you have to watch how you really run your plant. So sometimes you'll sacrifice throughput for revenue and that's part of the overall game of trying to maximize revenue against cost, against the supply. So sometimes you'll take a capacity reduction simply to maximize your revenue to get a higher mix. That's why it's a lot less dependent than a pure number of saying what is the capacity utilization and we're always making those adjustments. That's why I'm a bit vague with the answer.

Robert Moskow - *Credit Suisse - Analyst*

I remember years ago capacity utilization was the most important thing to follow. Has your business philosophy changed since then, it's more revenue management?

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Jim Lochner - *Tyson Foods - COO*

Yes, I apologize for jumping in there but it was not always the most important thing to follow. Maximizing revenue has always been a key driver, just that people like to look at that relative to the supply and the adjustments. So yes, the key is really maximizing the revenue through mix and sales, and then looking forward to what that type of cattle supplies are out in front and really trying to match those. And we're not hesitant to try to drop a little bit of the daily capacity or the daily run rates to try to maximize those revenues.

Robert Moskow - *Credit Suisse - Analyst*

And the follow-up for Donnie. Chicken pricing, looks like yours is going to be up about 9% this year. Your volume will be down pretty much in line with the industry, maybe in line. Is 9% pricing disappointing? Were you expecting a higher pick up in pricing?

Donnie Smith - *Tyson Foods - President and CEO*

Good question. No, I think at the cost level so far for the run rate feels okay and it's going to be woefully inadequate to cover the cost structure that's coming at us. So we will definitely need to take more, but I'm proud of our guys. We won some price based on the things we like to win a price increase on, which is having a great quality product in the box or in the tray. Our service on time and order fill has just been phenomenal. And two, we lead with innovative capabilities, which had a lot of our customers in the Discovery Center working on ways to grow their business and so for that, we get rewarded for adding that value to their business with the pricing structure that makes sense. So no, I wouldn't say we're disappointed in where we are. I think our folks have done a good job. They do know they have another hill to climb and we're headed that way.

Robert Moskow - *Credit Suisse - Analyst*

Okay, thank you very much.

Operator

Tim Tiberio, Miller Tabak.

Tim Tiberio - *Miller Tabak - Analyst*

Good morning. My question is on the Prepared Food segment. Can you just give us some highlights within the quarter, what actual product categories performed well versus the other categories? Thank you.

Donnie Smith - *Tyson Foods - President and CEO*

Yes, sure. Our lunchmeat business, we've talk about a little bit before, continues to make improvement prior to that, Tim, our Wright brand bacon has well out paced category growth there. We've extended the Wright brand beyond bacon now into dinner sausages and are very pleased with that. We are seeing some movement and pretty optimistic around Chicken lunchmeat. We've got some smoked meats offerings coming out. We've actually done very well in our franks business.

And two, we've got a new offering coming very soon into the marketplace in the next two or three months, which is back to a Chicken offering which will be gluten free strips and nuggets. So adding value to the red meat items, whether it's pizza topping, our tortilla business has done well, as well. So its really been a fairly broad based growth in all of those Prepared Food segments and we see a continued bright future and a lot of growth opportunities in that segment.

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Jim Lochner - *Tyson Foods - COO*

The only thing I'd add is we also had a plant startup, which actually hurt us in this, which we started our Council Bluffs Pepperoni plant which will be very efficient process there, much more competitive than some of our existing pepperoni. And we'll continue to really put a lot of focus in our overall Prepared Foods, particularly the sausage and pizza topping businesses, as well as the lunchmeat. So we're very encouraged with the activity and the project list that we have on the incremental improvements throughout the whole category we call prepared.

Tim Tiberio - *Miller Tabak - Analyst*

Thank you.

Operator

Diane Geissler, CLSA.

Diane Geissler - *Credit Agricole Securities - Analyst*

Good morning.

Donnie Smith - *Tyson Foods - President and CEO*

Good morning.

Diane Geissler - *Credit Agricole Securities - Analyst*

Donnie, it wasn't clear from your comments if you thought you would actually fall into a position of unprofitability in the Chicken segment. I think earlier in the call you talked about the incremental cost of grain and that pricing was actually coming down on a seasonal basis. We always see it and that suggested to me that maybe the December and March periods you would be negative, but then later you said we're managing our business however we can to remain profitable. So I'm just wondering for your commentary regarding fiscal '13, is it built on we know where we are to the extent that we know where grain is today and we think we'll be profitable or is there a little bit of sort of optimism built into your back half of your fiscal '13 because at some point the market will start pricing in presumably, that we'll have a crop in 2013?

Donnie Smith - *Tyson Foods - President and CEO*

The answer to both of those questions is yes. Our optimism is based around where grains are today because that's really the only visibility we have. And we do see improvements in the back end, not so much in our costing model but on the revenue side of the model, it's a little bit back half loaded. But to your question, we are using current grain prices, current soybean meal as however the spot market is plus the basis freight delivered to our feed meals in our cost structure.

Dennis Leatherby - *Tyson Foods - CFO*

And we're seeing more operating efficiencies coming.

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Donnie Smith - *Tyson Foods - President and CEO*

About $100 million.

Diane Geissler - *Credit Agricole Securities - Analyst*

Somebody touched on it earlier about the revenue side and the fact that, obviously, the industry is really sort of supply driven industry and the pricing follows how much for either short or in excess, but if you look at even the breeder flock today is down 10% below what it was in 2007 and yet pricing wasn't all that robust this year. So I'm just a little nervous that even if we get another cut next year, call it 2% to 3%, that the consumer environment is so difficult that you really won't see it. And when I talk to the restaurant companies that I follow and QSR, they're looking to maintain their pricing structure to their customers, which means they're going to pressure back on their supply chains. So is it the conversations you're having with your customers today that they are now giving you an idea that okay yes they are going to be willing to accept these price increases that you'll need to take to cover this, or what's making you so optimistic about pricing in 2013?

Donnie Smith - *Tyson Foods - President and CEO*

Number one, yes, we are, as we talk to customers today, they do see that this is an unprecedented movement in grain that is likely to have an impact on the supply of meat in all three proteins, maybe all four proteins including turkey, on the market as we move forward. The exact timing of when which segment will cut back and supply will decrease, we have our ideas but I won't speculate on that. But I think everyone that we talk to realizes that the meat situation in America is going to tighten up and that's going to have an impact on pricing. USDA has their figures, we kind of pencil in ours, but our Chicken business has done -- the domestic Chicken business did very well I think in Q3. We continue to add, not only operating efficiencies, but we continue to grow our value-added, and we're getting paid for the value that we're adding to our customers' businesses, and so that's what keeps us optimistic is the fact that this situation is untenable. It's going to change and we're in a position because we so dramatically reduced the amount of fixed price long term annual fixed price agreements that we have to be able to take advantage of helping a customer ensure supply by being in an arrangement with a great supplier.

Diane Geissler - *Credit Agricole Securities - Analyst*

Okay, and then just one follow-up question if I have a minute -- I realize you're over schedule here -- on the international business, you'd talked about pulling in all of that production internally and building out farms, et cetera, in China. Is that -- what's the timeline on that again? Is that two years?

Donnie Smith - *Tyson Foods - President and CEO*

A couple years, 2014, yes. We should grow steadily in company controlled bio secure houses between now and 2014.

Diane Geissler - *Credit Agricole Securities - Analyst*

And at that time you don't expect to take any meat from the outside market?

Donnie Smith - *Tyson Foods - President and CEO*

Correct.

Diane Geissler - *Credit Agricole Securities - Analyst*

And what will your run rate be in 2014 in terms of total production?

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Donnie Smith - *Tyson Foods - President and CEO*

In China, about 3 million heads per week.

Diane Geissler - *Credit Agricole Securities - Analyst*

Okay, thank you.

Operator

Colin Guheen, Cowen & Company.

Colin Guheen - *Cowen and Company - Analyst*

Hi, just real quickly bigger picture and playing off some of Diane's questions, there's been such demand destruction over the last couple years in beef. Are we getting to a level more late in demand here where people become more agnostic on price or do we see more species substitution if we continue to have above your forecasted pricing in Beef and continued demand destruction?

Jim Lochner - *Tyson Foods - COO*

When I hear that and I tend to think that until I go look at the numbers and then I see that the cutout has ran a very high level, and is currently running a much higher level relative to last year. When I look at the Perishable data, you see the volumes being down and the prices being down, but the reality is the market is absorbing, did absorb a Choice cut out in the 190s through the bulk of May. It came off after the 4th of July. It's a very difficult thing to answer other than looking at history, but we do know that the supplies will continue to come down. The prices probably will continue to rise and the export demand, I think even though it's down year-over-year January through May about 11%, we expect to see probably exports continue or will strengthen in the back half and potentially into '13. Again, that overall available worldwide supply keeps dropping, and so I think there are a number of consumers that are really price isn't the primary driver. So it's a long answer to say I'm not sure. I can't predict the future very well, but I can look at the supply dynamic going down and history tells me that as supplies come down, prices will continue to inflate.

Colin Guheen - *Cowen and Company - Analyst*

Great. Thanks a lot.

Donnie Smith - *Tyson Foods - President and CEO*

Okay, well that wraps up our call for today. We obviously have some challenging months ahead, but we've got the right team in place and the right plan to handle what comes our way. So thanks for joining us today and have a great day.

Operator

Thank you. This does conclude today's conference. Thank you for joining. You may disconnect at this time.

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