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TSN - Q1 2014 Tyson Foods Earnings Conference Call

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OVERVIEW:

TSN reported 1Q14 sales of \$8.8b and EPS from continuing operations of \$0.72. Expects FY14 revenue to be approx. \$36b.



CORPORATE PARTICIPANTS

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Dennis Leatherby *Tyson Foods - CFO*

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Ken Goldman *JPMorgan - Analyst*

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PRESENTATION

Operator

Welcome to the Tyson quarterly investor earnings call.

(Operator Instructions)

Today's call is being recorded. At this time I'll turn the call over to Jon Kathol, Vice President of Investor Relations. You may begin sir.

Jon Kathol - *Tyson Foods - VP, IR*

Good morning, and thank you for joining us today for Tyson Foods conference call for the first quarter of the 2014 fiscal year. On today's call is Donnie Smith, President and Chief Executive Officer, Dennis Leatherby, Chief Financial Officer, and Jim Lochner, Chief Operating Officer.

I need to remind you, our remarks today include forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. These statements are subject to risks and uncertainties that could cause actual results to differ materially from our expectations and projections. I encourage you to read today's press release and our filings with the Securities and Exchange Commission for a discussion of the risks that can affect our business.

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 for any additional questions. As you are probably aware our annual meeting of shareholders is this morning and we will need to stay on schedule. I hope we get to all of your questions but we will have to put a hard stop on this call to get over to the shareholders' meeting on time. I'll now turn the call over to Donnie Smith.



Donnie Smith - *Tyson Foods - President and CEO*

Thanks John. Good morning everyone and thanks for joining us today. FY14 is off to a strong start with earnings of \$0.72 a share in the first quarter, which is a 47% improvement over Q1 of last year.

Operating income grew 36% quarter-over-quarter and our overall operating margin was 4.7%. Sales were \$8.8 billion, the highest Q1 sales we've ever reported, up 4.7% over Q1 of FY13. Chicken, beef and prepared foods all have record Q1 sales and pork had its second largest Q1 sales.

I'm really pleased with those results but I'm even more pleased with what I'm seeing from the team to manage for the long term and invest in future growth. As an example, last week we acquired Bosco's in Michigan, which was our third prepared foods acquisition of less than a year and another step in our effort to grow sales in our prepared foods segment. Bosco's is a great fit with our pizza toppings and crusts, and it aligns nicely with our K-12 school food service business.

We have to look at a variety of options and avenues for growth. It goes back to being nimble and responsive to consumers and their changing needs. One of the first places consumers adjust their spending is on food purchases. Not just what they buy, but where they buy it.

As you know our business model is to offer a broad portfolio of products spread over multiple distribution channels so we were able to ship with the consumer and give them what they want where they want it. Consumers today are expanding their food purchases beyond the traditional food service and retail channels creating opportunities for us in dollar, convenience, drugstores, and even online.

In spite of historical high prices Nielsen data from the 52 week period ended December 28 indicates the total fresh meat volume at retail was up 1.3%. Pork, chicken and ground beef pounds sold increased while all muscle beef held steady. Fresh chicken was the leader with dollar sales up 8% versus the previous year, and once again Tyson was the number one brand of fresh chicken in the country.

Record high beef prices should continue through 2014 meaning fewer beef promotions and retail and food service. Pork prices will also remain high due to lower supply. Chicken should continue to be the winner.

As consumer confidence rebounds people are becoming less defensive in their spending but I don't know of anyone who thinks that consumers will go back to their pre-2008 spending habits anytime soon. Expectations are different. The definition of value is different and it isn't limited to price.

The consumer is asking: What am I getting for my dollar? What are the ingredients? Is it fresh? Is it good for me? All of those factors are part of the consumers' new value equation.

They're willing to pay for convenience but the product must legitimately fill an unmet need or solve a problem in a unique way. Our insights driven approach to new product development is focused on those unmet needs.

Better for you foods are becoming mainstream. People want clean labels and transparency in ingredients. They want to know where their food comes from and that we're being responsible in how we produce it.

They are uncompromising about food safety, and rightly so. But they also want only a few ingredients on the label, so that's our challenge and an area of focus for our R&D and innovation.

Another challenge is the cut to the government's supplemental nutritional assistance program. This could reduce total food sales growth by 1%. Shopper card data shows that SNAP shopper spending has dropped four points more than other shoppers since their benefits were cut.

We are developing consumer insights into those shoppers to retain them as consumers even though they have less money to spend. So that's our thinking about the market dynamics domestically, and now let's turn to our international business.



It was a disappointing quarter with a \$28 million loss. While China certainly wasn't the only source of the negative returns, it was the largest, and we've been making significant investments to build a fully integrated poultry business. I said on our Q4 call that I thought our China operations would reach breakeven by the end of the fiscal year. But I don't think -- I think it will take longer.

There's been a change in the market dynamics in China over the past year following widespread food safety concerns, an avian influenza outbreak, and the economic slowdown. Previously I told you that demand would return about three months after the initial AI problem was over, but I was wrong. Demand hasn't recovered which has led to a substantial oversupply of chicken. And now there are new concerns about avian influenza.

Because of these factors we've decided to slow down on building more chicken farms beyond those currently planned for this fiscal year until the market conditions improve. I want to be clear. We are not changing our path, just our pace.

We are not backing off our long-term commitment to produce quality chicken from a controlled supply in China. We simply slowing down until the supply and demand dynamics get back in balance in order to protect our margins. We will move forward with our planning processes and when the markets improve we will be able to resume construction of company-owned chicken housing.

I think one of the characteristics that makes Tyson Foods a great company is our ability to be flexible and to reassess and that's we're doing to grow our business and optimize shareholder returns. I remain confident about 2014. I think it's going to be another great year for us.

There's still a certain amount of seasonality to our business and Q2 is typically our softest quarter and the hardest to predict. It was last year and it certainly appears that this quarter won't be an exception. We still feel confident that the back half of our year will be strong and that this will be a very good year for us.

Overall, we've got a lot of momentum and we're anticipating healthy growth this year, next year and beyond. We feel really good about where we are as a company. There are always challenges in this business but we don't see anything on the horizon that we can't overcome.

And now I'll hand it off to Dennis for the financial update and then Jim will talk about the segments.

Dennis Leatherby - *Tyson Foods - CFO*

Thank you Donnie, and good morning everyone. As Donnie mentioned, this morning we reported first quarter earnings from continuing operations of \$0.72 per share. This represents a 47% increase over the \$0.49 we reported a year ago. I would also like to note that on an adjusted basis our rolling four quarter continuing EPS is \$2.49 as compared to \$2.26 for FY13.

Pretax return on invested capital for the past 12 months was just under 20%. Operating cash flow was strong in the first quarter at \$361 million. Capital expenditures were \$140 million for the quarter as we continue to invest in projects for both our domestic and foreign operations that resulted in improved productive capabilities, labor efficiencies, yields, and sales mix.

During the first quarter we acquired 4.6 million shares for \$150 million under our share repurchase program. Since May 2011 we have repurchased 47.9 million shares for \$1.1 billion. I'm also pleased to announce yesterday our Board of Directors increased the authorized shares under this program by 25 million and we now have 34.6 million shares available for repurchase.

Our effective tax rate for continuing operations in Q1 was 34.3%. Net debt to EBITDA for the last 12 months was 0.6 times and on a gross debt to EBITDA basis this measure was one times. Including cash of \$825 million net debt was \$1.1 billion. Total liquidity was \$1.8 billion, remaining well above the targeted range of \$1.2 billion to \$1.5 billion. Gross debt was nearly -- was down nearly \$0.5 billion from Q4 2013, coming in at \$1.9 billion.

As we reported in the last call we paid off our \$458 million convertible notes in October with cash on hand. Additionally, we issued 12 million shares at maturity for the conversion feature and at the same time we received 12 million shares under our bond hedge. This had the impact of finally canceling out the negative dilution impact we have been experiencing the last few years associated with convertible notes.

However, we still have warrants outstanding related to this transaction that will exercise from January through April, which are ready included in our diluted share count. For the quarter our diluted shares outstanding were 354 million, which included dilution from warrants of 8 million shares and stock options of 5 million shares.

Now here are some thoughts on the remainder of FY14. We expect revenues of approximately \$36 billion for FY14, up 5% over FY13. Net interest expense should be about \$100 million, down \$37 million from FY13. The effective tax rate for continuing operations should be around 35.5%. And our CapEx plan remains at \$700 million, up \$140 million from FY13 and \$180 million greater than our depreciation and amortization expense.

Based on our average share price in Q1 we expect our diluted shares in Q2 to remain around 354 million. Prior to considering changes in our stock price which would impact the dilution from warrants and stock options. This also does not reflect the impact of any additional stock buybacks.

Our priorities for excess cash remain the same, which include additional capital spending to improve and grow our existing businesses, acquisitions to fulfill our growth strategies around value-added products in our international footprint, and returning cash to shareholders through share repurchases and dividends, all while ensuring we maintain plenty of liquidity at our disposal.

As Donnie mentioned earlier we have a lot of momentum going and we feel great about where we are as a company. FY14 is off to a fabulous start with a 47% EPS improvement over prior year in Q1. And Q2, while softer and seasonally more challenging should beat last year and the fourth quarter should be really strong.

Although we don't normally provide guidance, the last couple of quarters we referenced the back half of FY13 times two, which implied about \$2.78 earnings per share for FY14. While it is still early in the year we are confident we can deliver at least that number which would be an excess of 23% EPS growth for the year and we are poised for at least 10% EPS growth in 2015 and beyond. I'll now turn it over to Jim for a closer look into our operating segments.

Jim Lochner - *Tyson Foods - COO*

Thank you Dennis and good morning. Starting with the pork segment, in the first quarter we reported \$121 million in operating income and an 8.5% return on sales. Volume decreased 2.1% compared to Q1 2013.

The available supplies of hogs were lower year-over-year and we adjusted our weekly volumes accordingly. Sales prices are up 6.7% due to mix changes and price increases associated with the lower total pork supplies. This helped to offset the lower US total exports.

We are now a third of the way into our second fiscal quarter and we are about where we thought we'd be, meaning we are performing well and on track managing revenue drivers such as mix, yields, and pricing. This fiscal year we expect the PED virus to impact domestic hog supplies by 2% to 4%. In our plant locations we will see the effects in the summer months.

Heavier weights will offset some of the headcount reductions, but we do expect to see wholesale price increases. We do not anticipate any issues running our plants.

In the chicken segment we generated a record \$225 million in operating income with 7.5% return on sales for the first quarter. Excluding international losses, chicken margins were 9.5%. Volume was up 3.6% compared to the first quarter of FY13 due to increased international production, outside buy, and rendered product sales.

In aggregate, pricing was down 1.4% year-over-year, predominantly from export sales, rendered products, and international operations. Q2 is off to a good start but this is typically our most challenging quarter.

Looking further out chicken supplies for the last three quarters of our fiscal year are projected to increase around 2% over last year reflecting the production cuts in 2013. We will continue our buy versus grow strategy in chicken to make opportunistic open market purchases and value up those sales. Currently, we project lower feed costs for the fiscal year to be around \$600 million.

As we discussed in previous calls, less than 10% of our contracts are annual fixed-price, and our focus is on helping our customers drive their businesses and generate category growth. So our pricing conversations lean more toward what our portfolio products are worth to the customer and to the consumer.

Turning to the beef segment, in Q1 we generated \$58 million in operating income and a 1.6% return on sales. Volume was up 4.1% over Q1 2013. Price was up 2.9% reflecting higher beef wholesale cut pricing from reduced supplies and stronger overall exports. So far in Q2 we've seen historically high wholesale beef prices and the cut out has set records each week.

Low production volumes relative to demand, particularly in ground beef, trim and the chuck and round cuts have driven the rapid rise in the overall cut out and beef revenue. As a result, consumers will see higher retail beef prices. And as Donnie mentioned, will likely see fewer beef features at retail and food service the summer. We expect have adequate supplies for our beef operations as our plants are located close to the fed cattle supplies.

In the prepared foods segment operating income for the first quarter was \$16 million with a 1.8% return on sales. Sales volume increased 3.5% versus the same quarter last year due to improved demand and the additional volume associated with the Don Julio and Circle Foods acquisitions.

Sales prices were up 4.2% as a result of mix improvements and price increases associated with higher input costs. Pricing gains however were not sufficient to fully offset increased inputs and additional costs associated with the investment in our lunch meat business and the other prepared foods growth platforms in the quarter.

In our Q4 earnings call we talked about a couple of those growth opportunities, including Tyson Day Starts in the frozen breakfast category and Wright brand breakfast sausage. Although they started shipping only a few weeks ago, we are already pleased with the customer acceptance and the volumes for both product lines. We will continue to put MAP spending behind them and other prepared foods as we look for growth in the long term from this segment.

In closing, I'd like to say a thank you to our team members for their commitment to continuous improvement. Tyson Foods has made tremendous strides in recent years and I still see a lot of runway ahead.

As we announced in November I've begun transitioning into retirement and as a result this will be my last earnings call. It's been a great experience getting to interact with investors and analysts over the years and I've appreciated your willingness to learn about our business.

That's the end of our prepared remarks. Shirley, we're ready to begin Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Brett Hundley with BB&T Capital Markets.

Brett Hundley - *BB&T Capital Markets - Analyst*

Donnie, just have a question for you. I'd love for you to give some further overall color on the balance of FY14 and then the outlook into FY15. I think you made some, or you guys made some interesting comments on both years.

Donnie I think one of the things that has really helped to kind of re-rate your stock and support your stock is you guys coming out on the last call and on this call and reiterating segment guidance in the face of a number of challenges. And certainly there's a lot of factors impacting you guys,

PED, tight cattle supplies, cold weather, propane issues, oncoming chicken supply, and now we have a resurgent bird flu in China, and your slowdown there. So I'm just kind wondering how all this plays out and affects earnings potential going forward, particularly as you guys mentioned at least 10% earnings growth in 2015. Thank you.

Donnie Smith - *Tyson Foods - President and CEO*

Sure Brett, so let me start with kind of reiterating what Dennis said in his comments. We're off to a very solid start in this year, great Q1. Our Q2 is typically softer and it's certainly harder to predict. But it looks like to us that the back half of the year ought to be really strong and so we are going to have a really good year and take a lot of momentum, by the way, into FY15. So from where we sit today we are confident in our ability to deliver at least that \$2.78 or so.

Let me talk about each segment just a little bit. Obviously the chicken segment is off to a strong start. We are headed into a lower cost environment with a little higher supply, 2% to 3%, but we are also going to see I think a halo effect from high priced beef and pork. So it feels like to me that the chicken segment is just going to have a really super year. Most of the issues in international for the year are behind us and we will be getting continually better there. And taking more positive momentum into FY15 there.

Beef and pork look to be very similar to last year. So be thinking of that equal to, and if either one, maybe a little better. In prepared foods, obviously we are investing in our growth platforms and it looks like that, we're going to be about like we were a year ago and could possibly do better there as well. So feel good there.

When you look at the overall balance sheet, debt is low, we're at -- our net debt is 0.6 times EBITDA, so we've got a lot of dry powder, we're going to throw off a lot of cash this year. Plenty to do the CapEx we need to do. We will be well above depreciation and amortization again this year, so we've got opportunity for more value-added acquisitions that fit. And we will continue to return cash to shareholders.

If you take the new acquisitions that we've made in prepared foods, they'll start contributing in, well, they are contributing now, and good opportunities for growth in those businesses and they'll be contributing in FY15 and beyond. Like I said, we're taking our foot off the gas a little bit in China, but we're still on the road and when the market dynamics give us an opportunity we will certainly continue to press forward there and we will gain more momentum in our international business in 2015.

Feels real solid. We got a great future. Obviously with that laundry list of stuff you mentioned we always have challenges to our business but we really don't see anything that we're not going to be able to overcome now.

Brett Hundley - *BB&T Capital Markets - Analyst*

All right thank you. That's very helpful. And then I just have a follow-up on chicken. You guys did very well during the quarter and I would expect given your business make up there for you guys to continue to do well.

I just wanted to ask you about this polar vortex that's gripping the nation, and predominantly the Midwest and Southeast, and as it relates to your chicken business. A, do you guys hedge forward on natural gas? And then B, if your growers are having, and of course that natural gas is at the plant level, but B, if your growers are having issues with propane would the company step in or be able to step in, and would that affect margins at all? Thanks guys.

Donnie Smith - *Tyson Foods - President and CEO*

Yes, sure, great question. We stay fairly close in natural gas. We might have natural gas purchased a couple months out in front of us, that kind of thing. As we do in grain, we take a fairly conservative but sensible approach to how we manage our commodity purchases.

On the propane issue for the growers, I'll tell you, we had a great team of people that came together and we've actually been buying propane down in Houston and transporting it into the areas where our growers had needs. So I'm not aware of any grower that's growing for Tyson Foods that doesn't have the propane they need to be able to take care of those chickens. And I'll tell you it's just been a heroic effort by a large group of people. I'm really proud of them for jumping in there and frankly, coming to the rescue for some of our growers. And yes, we will be making some adjustments in our grower pay to make sure that we take care of our growers during all this.

So we've got a great live production team. And by the way, we have great growers. So they have worked together to make sure we mitigated the risk of this to our business.

Operator

Ken Goldman with JPMorgan.

Ken Goldman - JPMorgan - Analyst

Can you talk a little bit about what you're seeing in PEDv right now? I assume it's not very constructive since you just took your expectation down for hog availability so dramatically. And also, you did take your estimate for chicken supply for the industry down this year as well. If I'm not mistaken, it was 3% to 4% last quarter, and now it is officially 3%, and on the call you're talking a little more like 2%. Can you just add a little color what you're seeing there to maybe drive that decline in your forecast?

Donnie Smith - Tyson Foods - President and CEO

Sure, Jim you take that.

Jim Lochner - Tyson Foods - COO

When I referenced that chicken supplies I said the last three quarters, annualized would be the same and I just took the first quarter, which was behind us. So I said going forward all the analysts I looked at and the data we look at implies around that 2% for the last three quarters.

Now referencing the PED, that's a very fluid situation. It seems like either at least weekly, but some times even daily new evidence comes out. And we do expect it might be influencing up to 30% of the sow herd with 10% or so impact on the available pigs impacted, so there is where the 3% comes from. Now, if that increases to 40% or decreases, because a lot of the data is still flowing in, that will have some influence.

So that offset -- that would offset any of the productivity gains or the balance of let's say it is 30%, the 70% would have some productivity gains, and we probably are likely to see some increase in carcass weight to offset at least some of the pounds lost from the head loss. But I do want to emphasize information does come out fairly regularly, and it's being assimilated and we're just saying on top of it region-to-region, producer-to-producer.

Ken Goldman - JPMorgan - Analyst

Best guest Jim, is PED better in terms of less spread or worse than what most media reports have come out with?

Jim Lochner - Tyson Foods - COO

Not sure -- is it spread to a greater degree or lesser degree?



Ken Goldman - *JPMorgan - Analyst*

Yes, I didn't ask that very deftly, but I guess is it spread to a greater degree or a lesser degree than what most people think?

Jim Lochner - *Tyson Foods - COO*

I don't know what most people think. So I'm hearing it is spreading in states and what we're really tracking is how many sows are impacted when, because it impacts the baby pig mortality, so then five to six months out there would be fewer pigs available. So that is how we are tracking it. Some people believe it -- well it has spread into more states, so it's the extent and the number of sows impacted that we're really monitoring.

Ken Goldman - *JPMorgan - Analyst*

Thank you.

Jim Lochner - *Tyson Foods - COO*

Thank you.

Operator

Farha Aslam with Stephens.

Farha Aslam - *Stephens Inc. - Analyst*

National Beef announced the closure of the Brawley, California plant this morning. How do you anticipate that impacts supply/demand in the beef market? And will that impact or benefit Tyson's facilities in particular?

Jim Lochner - *Tyson Foods - COO*

Well, we just found that out this morning and we're familiar with their daily head capacity. That plant is in California and there is generally a feed lot supply around so it will take daily capacity out, our best guess is around 2,000 head per day. So that obviously means those cattle will have to be marketed somewhere else, so they will flow I guess east and potentially north to different packers.

And it is consistent I guess with what we've been saying all along as the calf crop declines and the noncompetitive feed lot areas or noncompetitive plants or the combination thereof will probably have to curtail production. We were a bit surprised to see it this morning but I guess to some extent we would -- we have always felt and anticipated something like that would happen.

Farha Aslam - *Stephens Inc. - Analyst*

Okay. And just as a follow-up on prepared foods. You've done three sort of tack-on acquisitions in that space. Could you just share with us combined what the sales of those three acquisitions are? And kind of your vision for prepared foods longer-term into 2015 because clearly you are taking hits in terms of the plant et cetera. What is the potential and outlook in 2015 for that division?



Donnie Smith - *Tyson Foods - President and CEO*

So no particular specifics on the three acquisitions but our prepared foods business is really a broad mix of different types of businesses that are frankly at different stages of maturity. We've got some businesses that are mature and generate great results and then we've got some that we are building and we've talked about lunch meat before, and continuing to fix that business. And we're investing a lot in those businesses, as Jim referenced a couple of new product rollouts.

If we just -- I don't want to get too specific here, but if we took off the MAP spending, which we won't, but if we just adjusted back the MAP spending, our prepared foods segment would be above 4%. So we're spending a lot. We're investing a lot in this business. I view prepared foods a lot like where we were in chicken four or five years ago where we just had to get in the basics and build a strong foundation under that business. You can see kind of the results, two, three or four years later about doing all of that work. We are working on our footprint.

If you just look forward into our vision in prepared foods, continue to think about a broad portfolio of items that meet changing consumer requirements. We've got very broad capabilities. We've got access to raw materials. Obviously, we've got a great sound capital structure and the ability to invest in those businesses and we will continue to do that. And you should expect to see strong growth in prepared foods.

Farha Aslam - *Stephens Inc. - Analyst*

In 2015?

Donnie Smith - *Tyson Foods - President and CEO*

Right. And again think of this year at least equal to last year, but maybe a tad better. But as we go forward that segment should continue to improve as we see the benefit from the investments that we're making today.

Farha Aslam - *Stephens Inc. - Analyst*

Great. Thank you so much.

Donnie Smith - *Tyson Foods - President and CEO*

Thank you.

Operator

Robert Moskow with Credit Suisse.

Rachel Nabatian - *Credit Suisse - Analyst*

Hi, this is Rachel Nabatian in for Rob. Congratulations on the quarter.

Donnie Smith - *Tyson Foods - President and CEO*

Thank you. Hi, Rachel.

Rachel Nabatian - *Credit Suisse - Analyst*

I just wanted to get an update on the annual negotiations with food service customers that you recently had in pricing. With the benefit of lower grain at \$600 million now do you think that you would be able to maybe hang onto half of that benefit in pricing and then pass the rest of it onto your customers?

Donnie Smith - *Tyson Foods - President and CEO*

So very pleased with how, let's call it, contracting season went. Our customers recognize that we grow their categories and we grow their businesses and we spur their demand. So we are being recognized for the quality and the service and the insights driven innovation. And as Jim mentioned in his comments that keeps our conversations with customers much more focused on what our products and our offering and our service to their business is worth, than rather just what it costs.

Again, let me remind you, our fixed annual price exposure is less than 10%. Now getting to the how much of the grain question we will hang on to. I don't want to answer that specifically, but let me answer it this way. Remember that we've talked about our pricing profile is today is much more reflective of the inputs and we've made that change over the last two or three years. Over half of our pricing contracts today either adjust for grain costs or market values. So that helps us protect our dollar margins and gives us a lot more stability in up or down grain markets. Remember, chicken is still the best valued protein relative to all the other competing proteins.

I guess third thing is, again, our quality, our service, our innovative capabilities make us a go to supplier for our customers, and we're getting paid for the value that we add to their business. Again, we mentioned this too, our buy versus growth strategy we continue to keep our supply short of demand, and we will capitalize on buying less expensive raw materials as we continue to supply more breast meat per capita. So we will continue to buy those cheaper raw materials.

And then the last thing I'd say is we're going to continue to grow our value-added mix. And of course that provides us some protection from the underlying commodity markets. If you tie all those things together that gives us a great opportunity to hold on, if you want to call it that, to the grain benefit.

Rachel Nabatian - *Credit Suisse - Analyst*

Okay, great. I'll pass it on. Thank you.

Donnie Smith - *Tyson Foods - President and CEO*

Thank you.

Operator

Michael Piken with Cleveland Research.

Michael Piken - *Cleveland Research Company - Analyst*

Congratulations on a good quarter. Just wanted to circle back to a couple things, with respect to your outlook for exports from the upcoming year, if you could kind of break it down protein by protein what your expectations are for US exports are for beef, chicken, and pork.



Jim Lochner - *Tyson Foods - COO*

Let me start with beef. I think we'll continue to see an increase, probably not at the same rate that we saw last year because Japan's entrance in expanded to 30 month and down certainly was a boost. We continue -- we think will see US beef exports continue to grow probably in that 2% to 3%, and that's aligned with most people's expectations.

Pork this year is down, 2013 versus 2012 was down about I think around 7% or 8%. But I don't think we'll see that same decline this year. In fact I'm one who thinks it will probably increase although I can tell you there's a big divergence of opinions on most analysts to what they think pork exports are going to do this year.

And then chicken exports I'd consider -- I expect will continue to grow at the 2% to 3% year-over-year. So, and overall, again, domestic availability of protein is probably is going to come down which should be supportive of wholesale pricing as a whole. Obviously we will see less beef. Right now the way PED is going to impact pork we should see less pork than anticipated, prior to that most people were thinking it would be up. So I think that will be down.

And if chicken exports continue to improve and we don't -- and we think we're beyond the year-over-year major increase, so again, I think we're going to see very supportive prices for all the wholesale meat cuts and poultry cuts this year.

Michael Piken - *Cleveland Research Company - Analyst*

Okay, great, and just as a follow-up on the chicken side, if you could break it down a little bit more in terms of which markets you see growing because obviously last year we had the Mexico AI outbreak in the second quarter. Just if you could break it out market by market, and is it your belief that commodity quarter prices could start to rebound off of declines we saw in the [fourth] quarter? Thanks.

Jim Lochner - *Tyson Foods - COO*

Actually we would say that there won't be any market that's probably going to go down. We don't see any softness in Mexico. We see Russia having to come back in, Angola, Canada, et cetera. We don't really see any market that is acutely going to go down. In fact, some of them we don't see where that supply is going to come from so that's where the modest increase, and I think potentially it could be stronger than what I just said. But really we don't see any country at this point as a threat.

Operator

Akshay Jagdale with KeyBanc.

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

Congratulations on a good quarter.

Donnie Smith - *Tyson Foods - President and CEO*

Thank you.



Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

So my first question is on chicken, and Donnie you mentioned it's shaping up to be a good year, and thanks for breaking out the US margin. So my question is really how good can it get? The way I'm thinking about it, so help me if I'm thinking about it correctly, your costs came down sequentially, it seems like \$0.07 or \$0.08 a pound.

I would expect those to be sort of stable sequentially for the rest of the year unless grain prices change, and I would expect revenue per pound to continue to increase as the fiscal year progresses. So I would think that your US margin at 9.5% is biased upwards sequentially, unless I'm thinking about that incorrectly.

And then you mentioned on the international side things should continue to get better. Am I thinking about that generally correctly where your margins should improve from where we've seen them in 1Q?

Donnie Smith - *Tyson Foods - President and CEO*

I think you are a tad strong on your revenue growth for the balance of the year. We don't see it -- I guess the right way to put it, we don't see it deteriorating markedly, but I think continued growth in price per pound through the rest of the year is probably a little bit unrealistic. But still, don't let that mean that we don't think this is going to be a really great year in chicken. And I think you're right on the -- on our international business. The worst seems to be behind us, and it's getting better and it will continue to improve some through the year.

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

The price per pound, my comment was sequentially. Did you mean that sequentially as well or you meant year-over-year?

Donnie Smith - *Tyson Foods - President and CEO*

Oh, got it. Yes. Sequentially, we will be better. I thought you meant from Q1 getting better into Q2 getting better into Q3 getting better into Q4. Sequentially, yes, you are correct.

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

Okay. And then just a follow-up would be on the comment you made about 2Q being the most unpredictable. I would think that relates more to pork and beef, and less so to chicken. It just seems -- can you give us a little bit more on what you meant by that? Should it be higher or lower than \$0.70 and what were you really trying to indicate by the comment on Q2 being a little bit difficult to anticipate? Thank you.

Donnie Smith - *Tyson Foods - President and CEO*

Well so I'm not going to give quarterly guidance. We struggle enough on annual. But our Q2 is not generally as strong as our Q1. That's what we mean by that, and in our beef and pork markets coming out of the holidays there's just typically a bit more volatility. It's a little harder to predict how things are going to turn out and when you get into high demand seasons post Memorial Day, right? So it's just a difficult quarter. I guess it's a more difficult quarter to predict.

I'd say our guys are on top of it. They are doing a great job managing our supply. They are doing a great job on our pricing. I feel really good about where we are.

It didn't mean to over imply anything scary about our Q2 comments. It's just Q2 is generally a little softer than Q1 and it will be this year, and it's a little harder to predict. But still going to have a great back half of the year and this will be a good year for us. Jim, you want to add anything about beef and pork?

Jim Lochner - *Tyson Foods - COO*

Yes, beef is, the Jan, Feb, March periods are always very difficult, and this year is really extreme with record cut outs and they topped out at the choice cut out at \$240, but in two weeks it gave \$10 of it back up. So it tends to be extremely volatile and I feel really good about how we're navigating through this January period, particularly in beef and pork. But the general statement is, historically this is usually our most challenging quarter and typically less than Q1 and Q3. But I personally have a lot of optimism at four weeks into it.

Akshay Jagdale - *KeyBanc Capital Markets - Analyst*

I'll pass it on, congrats again.

Donnie Smith - *Tyson Foods - President and CEO*

Thank you.

Operator

Tim Tiberio with Miller Tabak.

Tim Tiberio - *Miller Tabak & Co - Analyst*

Just a very brief question around some of the trends that we're seeing other the natural organic side. We've been seeing some of the national food service companies talking about sourcing more non-GMO ingredients. I know that you have launched a line in the last two years. But looking forward, wanted to get a sense of whether you think that your current investment level is sufficient there or whether this is a segment that we should expect you investing in going forward over the next year or two.

Donnie Smith - *Tyson Foods - President and CEO*

So last summer, or late spring we launched our no antibiotic ever line, Nature Raised Farms. As a total -- as a percent of the total meat sold, let's lump things into natural. I'm going to call it that. It's a pretty small percentage versus our traditional lines, but it's growing at a pretty healthy pace, and so it's something that we can't ignore. The category is big enough that a national player can make some difference in. We will continue to focus on the category.

In terms of our investments we've got a lot of things that we can invest in in our business to continue to grow. That would be one of them. Feel good about our opportunity in that category. And so expect to hear more of us in the future. But I don't look for any disproportional investment over the next year or two I would say in our no antibiotic ever line.

Tim Tiberio - *Miller Tabak & Co - Analyst*

Great, and just one follow-up question for Jim. With some of the supply constraints with the Australian drought how are you thinking as far as imports of 90 or 50 CL trim and how is Tyson positioning for potentially lower trim imports during 2014?



Jim Lochner - *Tyson Foods - COO*

Lower trim imports are generally favorable to wholesale to domestic prices. But as always the market likes to do its job and we've seen very low cow kills, so therefore low 90 beef manufacturing supplies in October, in particularly October, November and December, more acute in December which is extremely supportive to the trim and ground beef and chuck and round pricing coming into January. So the question will be how fast can they get it in the pipeline and will it neutralize some of this rapid price increase we've seen.

Generally speaking if you have lower imports it's favorable to wholesale prices, and I think as we've seen these record high ground beef prices et cetera as part of that whole complex. That's part of the big contributor to the beef cut out right there. It's a nice number. You can watch when it's coming in and look at it and its contribution to total domestic availability.

Tim Tiberio - *Miller Tabak & Co - Analyst*

Great. Thanks for your time.

Jim Lochner - *Tyson Foods - COO*

Thank you.

Operator

Adam Samuelson with Goldman Sachs.

Adam Samuelson - *Goldman Sachs - Analyst*

Question on chicken, clearly the performance this quarter was a record. The outlook for the rest of the fiscal year is good. Supply is pretty contained in the pricing environment pretty healthy.

I guess thinking about 2015 as you start to see maybe some more pressure on supplies, the breeder flock gets rebuilt and one of your competitors has a new plant coming on stream. How confident are you in the 10% EPS growth in 2015 if you start to see some cyclical pressures in chicken?

Donnie Smith - *Tyson Foods - President and CEO*

Very. We manage the supply and the commodity risks through a variety of approaches. One is growing our value-added -- our value-added sales in Q1 grew by 6%. I think the total sales for the company was close to right at 5%, right? So we are going to make sure that we focus on growing our value-added sales in that 6% to 8% range.

And then when you combine some of the other pricing things that we talked about a little bit earlier, plus our buy versus grow strategy, we have the opportunity to continue to grow our sales at a very good pace whether we increase our production or not. So I feel great about our continued opportunities in 2015 to expand really our prepared foods business, our chicken business, getting better in exports. So yes, I feel very good about that.



Adam Samuelson - *Goldman Sachs - Analyst*

Okay, thanks. That's very helpful. And then maybe just one more from me. In the quarter SG&A up about 15% year-on-year, it's the highest level both on an absolute basis and as a percent of sales since 2010. Is that just really accelerated MAP spending in prepared foods or anything else there that you could comment on?

Donnie Smith - *Tyson Foods - President and CEO*

No, it's predominantly MAP spending in our growth categories, so we are intent on growing that business and we needed to increase our MAP spending to get to the category growth levels that we have to have to meet our objectives, so that's what it is.

Adam Samuelson - *Goldman Sachs - Analyst*

Okay. Thank you.

Donnie Smith - *Tyson Foods - President and CEO*

Thank you.

Operator

Jeremy Scott with CLSA.

Jeremy Scott - *CLSA - Analyst*

Just a follow-up on China. When you say that you will continue to plan for expansion, do you mean that you will continue to get permits from the China government and just not build the chicken houses? Or do you mean that you are going to hold off on everything?

Donnie Smith - *Tyson Foods - President and CEO*

No, you are exactly right. We intend to continue to get our land-use permits and to have all of that in place so that when we get the demand signal that we're looking for that we can begin construction on our houses. We will be, at the end of this year we will have both of our processing plants in China one shift full of company controlled birds.

Now we were planning on being, on in the last half of this fiscal year continuing the house build to be able to grow past that early in the first half of the year on company controlled birds. We are going to back off buying market birds and be at a single shift full at both plants with company controlled birds at the end of this year. And our planning and everything we're doing is focused on that with continuing to acquire the land to grow in the future. And if we get a demand signal that something is changing, we will be able to put our foot back on the accelerator and go again, because we fully intend to fill those plants out with company controlled birds.

Jeremy Scott - *CLSA - Analyst*

Helpful. Thank you.

Donnie Smith - *Tyson Foods - President and CEO*

You bet.

Operator

Ken Zaslow with Bank of Montreal.

Ken Zaslow - *BMO Capital Markets - Analyst*

I have a couple questions. Your 2014 outlook was always back half of 2000 run rate -- back half of 2013 run rate for this quarter, and then also that it was going to be more back end loaded this year as well. But this quarter you obviously kept the run rate actually a little bit above the run rate, so my question is what exceeded your expectations? Is there any change to the back half outlook for 2014?

Donnie Smith - *Tyson Foods - President and CEO*

I think for me, beef probably outperformed a little more than what I was expecting it to. Prepared foods was right where we thought it would be. Chicken is right where we thought it would be. Pork was pretty close so it was probably -- beef is what surprised a little bit. Well, maybe not surprised us, but we are pleased with the performance.

I tell you Ken, I would've never predicted a \$240 cut out in beef. This is just an unpredictable quarter that we're in today. But yes, we feel very good about the rest of our year and carrying a lot of good momentum into 2015.

Ken Zaslow - *BMO Capital Markets - Analyst*

So just going back, so you don't have a change to your back half look because you basically said, all you said was we are going to be at least what we thought, but you, I'll use your own words, it was a fabulous start, so I'm assuming that that fabulous start should be incremental to the full year when we think about the full year.

Donnie Smith - *Tyson Foods - President and CEO*

It could be. The door is open for us to do better. I'll tell you what, if we -- we will not miss an opportunity if one presents itself to increase our earnings. I promise (laughter). But hey, it's January and there's a few things that make it a little hard for us to predict, but I feel very comfortable about where we have been with the opportunity to get better, and we're certainly looking for every chance we get to do that.

Jim Lochner - *Tyson Foods - COO*

I apologize for laughing but we never miss an opportunity to do better.

Ken Zaslow - *BMO Capital Markets - Analyst*

And also, these beef packer margins, the Jan to March period of time is usually a pretty rough period for beef packer margins. Obviously you have the closure, and then on top of that you've had beef packer margins that -- look, in 25 years of history we've never seen a \$200 change per head in beef packer margins. Again, granted it's what we see, but again, beef packer margins seem pretty solid.

So this quarter you keep on saying, hey, look where it is, obviously we don't know the predictability, but it's clearly the beef packer environment seems better, can you talk to why it's better? And the duration to which that should stay better?

Jim Lochner - *Tyson Foods - COO*

I'll always remind everybody that it's the relationship of revenue to cattle costs that's where we make our money. So I always go back and say we do make our money in the slope of change. And prior to that run-up to the cut out, cattle ran up. And then the cut out, clearly there was insufficient supply relative to demand, the pipeline or the cupboard was bare and to replenish the pipeline prices really inflated very rapidly.

So we've had more volatility and we've navigated through that slope of change very well, and we're coming through January much better than we did a year ago. What we really watch is our, again, try to make sure we manage our mix, our price relative to the fair market value. And keep our costs in line, work on saving everything we can.

The only thing I know we have no influence over is what the live cattle are going to do. If they're tight, they're going to go up and beef will follow it up or precede it up depending upon what the circumstances are doing, and that's the nature of the market. Again a very volatile January, unprecedented both in incline and probably will be in decline. So it's an interesting time, but you can probably tell we feel pretty good about how we came through it.

Ken Zaslow - *BMO Capital Markets - Analyst*

And my final question is, you are slowing down, probably more for Dennis, is you are slowing down the CapEx spending on China but you maintained your CapEx spend at \$700 million. What are you spending more on?

Dennis Leatherby - *Tyson Foods - CFO*

That's a great question and we have still many great opportunities, both in prepared foods, and even in our chicken segment, so we are just moving it to a domestic bucket, high return projects that we feel really good about.

Ken Zaslow - *BMO Capital Markets - Analyst*

So your pipeline of CapEx projects, obviously China being a big one to slow down, the pipeline must be pretty substantial, is that a fair statement?

Dennis Leatherby - *Tyson Foods - CFO*

It sure is.

Ken Zaslow - *BMO Capital Markets - Analyst*

Great, I appreciate it. Thank you guys.

Donnie Smith - *Tyson Foods - President and CEO*

Well thanks for your time everyone and certainly your interest in our company. I'm sorry to wrap this up so quickly, but we really do need to head off to our shareholders' meeting. So I want to ask you all to have a great weekend. Thanks.

Operator

Thank you. This does conclude today's conference. We thank you for your participation. At this time you may disconnect your lines.

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