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Tyson Foods, Inc. (TSN)

Q4 2014 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to the Tyson's Quarterly Investors Conference Call. All line will be on listen-only mode until the question-and-answer session. [Operator Instructions] Today's call is being recorded. If you have any objections, disconnect.

I'd now like to introduce Jon Kathol, Vice President, Investor Relations.

Jon Kathol
VP-Investor Relations & Assistant Secretary

Good morning, and thank you for joining us today for Tyson Foods' conference call for the fourth quarter and 2014 fiscal year. On today's call are Donnie Smith, President and Chief Executive Officer, and Dennis Leatherby, Executive Vice President and Chief Financial Officer.

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 provide a framework for our commentary, fiscal 2014 included one month of Hillshire results, but for the purposes of looking back on the year, we will speak to adjusted results that exclude Hillshire. For GAAP results

and adjustment reconciliations, please refer to this morning's press release. I'd also like to point out that our accounting cycle will result in a 53-week year in 2015. To make comparisons easier, the projections in our outlook have been adjusted to a 52-week year unless otherwise noted.

Following our prepared remarks, we'll go to Q&A. 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.

I'll now turn the call over to Donnie Smith.

Donald J. Smith

President & Chief Executive Officer

Thanks, Jon. Good morning, everyone, and thanks for joining us today. Well, Q4 was a record third quarter with adjusted earnings of \$0.87 a share, which is a 24% year-over-year improvement. 2014 was an outstanding year. So let's look at some of the highlights.

We had recorded adjusted EPS of \$2.94, a 30% improvement over last year. Sales were a record \$37.6 billion. Adjusted operating income was also a record at \$1.65 billion, a 20% increase over last year. Our overall adjusted operating margin was 4.4%. And most important in 2014, we completed the acquisition of Hillshire Brands, a watershed event that will take Tyson to a new level as a branded food company. It was a great year. One in which we structurally improved the earnings power and reduced the volatility of the business. But I don't want to spend a lot of time looking back because we have so much more to be excited about in 2015 and 2016 and for years to come. So let's take a look at the segments and see how the events of Q4 lead us into 2015.

In Q4 the Chicken segment reported, on an adjusted basis, a 7.4% return on sales with volume up 2.3% and average pricing down 4%. You'll remember on our last call that I told you about temporary disruptions in two plants that would affect our return on sales in the third quarter and fourth quarters. We have corrected those issues and began bringing production back online in Q1.

We'll be adding much needed value added capacity in the spring for fully cooked and tray-packed chicken. Demand for tray-pack is growing as retail consumers see fresh healthy options. It's important to understand that we're not increasing supply, but rather shifting capacity to a more value added product mix. Also to support growth in fresh chicken, we very efficiently used a small amount of MAP spending to generate over \$800 million consumer impressions and it's helped widen the gap over our competitors as the number one brand in the country.

We're also experiencing double-digit growth in our Nature Raised Farms brand of no-antibiotics-ever chicken. Although it's only a small piece of our branded chicken business, we're pleased with the demand for these products and the premium consumers are willing to pay for them.

As you probably saw in our press release this morning, we have raised the normalized operating margin range for the Chicken segment to 7% to 9%, but we expect to exceed that in fiscal 2015 with more than 10% return on sales. With consumption shifting away from high priced beef, we expect chicken demand to increase by at least 3% in 2015, which should support our pricing expectations given that chicken supplies are projected to be up about 3% for the year.

Additionally, our domestic feed costs should be down by about \$350 million and an important point to remember about our chicken business is that we have a diversified value-added portfolio and we don't require record chicken prices and cheap corn to do well. We use our buy versus grow strategy to take advantage of pricing when there's

more chicken on the market and we do expect more supply in 2016, but we'll need it to meet demand. Our strategy is steady growth not a commodity rollercoaster ride. With our business model, we don't view increased supply as a problem.

I'll move onto the Beef segment which had a 3.5% return on sales for the quarter. Volume was down only 2.6% and I say only because pricing was up 21.5%. Our team did a great job of managing the spread in times of record high cattle costs. We anticipate per cattle supplies to be down about 4% in 2015, but that should be the worst of it. There are indications of heifer retention to rebuild the herd. Supplies are expected to be flat to down – to be flat to down about 1% in 2016 and as a positive for Tyson, the cattle population continues to move closer to our plant in the Midwest. With good export demand, domestic pricing in 2015 will test how much people really want beef, but it's clear that demand for beef is very strong and will provide support for chicken and pork pricing.

One of the things that's really impressed me over the past few years is our ability to manage through a low volume environment. We continue to find ways to become the high revenue, low cost player in the regions we compete. How we run a commodity business is more important than the commodity volatility. A good example of our margin mentality is our continuing success in producing more case-ready beef, which drives incremental sales, margins and consumer occasions.

Turning to the Pork segment, which had a 6.1% return on sales in the fourth quarter, volume was about flat to Q4 last year on a 16.5% increase in pricing. The PED virus reduced hog availability and our pork team did a good job of hog procurement in a time of tight supplies, which kept our capacity utilization well above industry averages. As the supply of hogs tightened this past year, it demonstrated the relative inelasticity of certain cuts like pork bellies for bacon.

From an end to an end perspective, we find ways to reduce volatility and improve our margins. While I expect global beef and pork supplies to remain tight and to keep pricing at higher levels, the structural shift towards increased global protein consumption will continue driving incremental demand for our products.

Looking at fiscal 2015, we expect 2% to 3% expansion in hog supplies and it appears there will be fewer instances of PEDv. Coming off of reduced numbers last year in addition to constrained beef production, we think consumer demand will support 2% to 3% pork supply increase. So 2015 should be another good year for Pork segment margins.

In our International segment, as previously announced, we'll use proceeds from the sale of our Latin American businesses, one of which is expected to close by the end of this month, to pay down debt. We made these decisions to generate better long-term ROIC. I want to emphasize that we're committed to doing business in Mexico, and supporting our customers' growth there. China remains in somewhat of a holding pattern. We are in position to take advantage when demand improves and we'll continue to assess the situation with an eye towards the best long-term shareholder return. In fiscal 2015, we expect to cut operational losses to \$50 million for the International segment.

And finally, in the Prepared Foods segment, our legacy Tyson business reported an adjusted 1.8% return on sales for the fourth quarter. Volume was basically flat with average pricing up 5.5%. We've taken measures to right size our operations by closing three plants and we're getting our SG&A in line.

We continue to be ROIC focused in our decision-making and good allocators of capital for our shareholders. Looking forward, the new Prepared Foods segment including Hillshire starting 2015 in a good position. With the plant closures our capacity utilization is improving to the desired levels and our operations are becoming more efficient.

We recovered pork and beef input pricing, but we'll have to stay on top of it as we anticipate \$140 million of incremental raw material costs in 2015, primarily from increased beef trim and turkey pricing. With the price increases we've implemented so far, pro forma volume has been about flat to a year ago.

Investing in brand building and innovation are vitally important to our branded CPG business, and I can assure that we're not slowing down the Hillshire innovation pipeline. They're speeding us up. We're not only launching on trend consumer driven innovation this year, we're supporting our past innovation launches, a critical part of ensuring long-term success.

In the last quarter of fiscal 2014, Hillshire launched the line of Jimmy Dean frozen sandwiches and bowls for lunch and dinner, taking the brand beyond breakfast. This expansion into a new daypart has achieved very good incremental distribution of 16 premium priced items, thanks to our retail partners. We have a strong integrated marketing program for this launch including television, digital and shopper marketing support.

Another big platform carrying over from 2014 is Hillshire Farm Natural Lunchmeat. It provides the cleaner label consumers are looking for without sacrificing taste and quality. While we're early into the launch, the results are extremely positive, it's drawing incremental purchases and 80% of consumers who bought the product, reported it's even better than they expected.

In addition to those two big platforms, we're extending and supporting our innovation launches from early in fiscal 2014. In retail, we're launching new extensions to expand Ball Park Park's Finest franks. These premium hot dogs deliver a flavor adventure and nothing artificial, and they're a growing category.

We're also extending our Hillshire Farm American Craft line of hand crafted small batch smoked sausage with new products featuring authentic ingredients in bold flavors and in foodservice, we're extending our Chef Pierre Luxe Layer pies. We'll invest MAP spending to continue growth in the second year of these successful new platforms.

In the back half of the year, our focus will be around two new snacking platforms. We know the shift to snacking is here to stay and believe that we have the right to win with our brands in protein snacking. One of those launches Hillshire Snacking has been in test market since Q4 and looks to have a lot of potential delivering incremental sales and growing the category. You'll hear a lot more about innovation at Investor Day on December 10, where you'll get to try some of these products.

To wrap-up my thoughts on the Prepared Foods segment, although it's going to take three years to fully realize all of the synergies, we expect the segment to earn a 10% to 12% return on sales on a normalized basis. After a couple of months of working together and really drilling down on the synergy target, we're more confident than ever that we'll capture more than \$225 million in the first year and more than \$500 million by the end of year three.

I need to clarify, that not all the synergies will fall within the Prepared Foods segment. Synergies within shared services for example, would be allocated across all of the segments, but the majority will be in Prepared Foods. So now that I've given you our outlook for each of the segments, let's take a broader look at some reasons we're so optimistic.

First, we're disciplined in our approach towards managing our business. The understanding of the consumer centric demand and overall supply fundamentals allows us to make decisions that are ROIC based and provide the least volatility and best prospects for long-term growth. When we assess the demand picture, we're uniquely positioned to deliver against changing consumer needs with a portfolio that delivers against every meal occasion

throughout the store and across the menu. It's not just the breadth of our portfolio that's exciting, it's the depth along with our innovation that delivers against increasing consumer demand for naturally occurring high quality protein snacks and meals.

Consumer behavior at both retail and foodservice reflect this change. At retail, growth is occurring at the perimeter of the store and in a few frozen categories with two of the biggest being chicken and protein breakfast, which favor our portfolio. We're also entrenched with the leading quick service, full-service, and fast casual restaurants addressing this year. If past consumer behavior remains the same, and we believe it will, the recent drop in gas prices will put more money back into consumer wallet, which will result in increased meals away from home.

So in the macro sense, Tyson has the right brands and the right products in the right places for today's consumers. But let's take a look at some more specifics for fiscal 2015 and why we feel so good about it. With six weeks under our belt, it's already off to a great start. We expect adjusted earnings in the range of \$3.30 to \$3.40 a share that's more than 12% growth over fiscal 2014. We'll gain momentum throughout the year as we integrate Hillshire and capture synergies. High beef and pork prices will be supportive of pricing throughout all of our segments. We'll grow our value-added chicken, much needed fresh tray pack and fully-cooked chicken capacity will be coming online in the spring. We have a series of new product launches in the pipeline. We're investing in brand building and innovation and we're investing disproportionately over depreciation throughout our business as part of our culture of continuous improvement.

And let's keep looking ahead into 2016. It's unusual for us to talk about our business more than a year out, but we feel a lot to be confident about. We'll be in our second year of capturing synergies and improvements as we maximize the benefits of combining Tyson and Hillshire. If chicken supply allows, we'll buy more on the open market, add value to it and sell it at a higher margin. Elevated beef and pork prices should continue to provide an umbrella for chicken pricing and consumption. We'll have a full year of the new tray pack and fully-cooked capacity in our results. There should be adequate supply of cattle and hogs with growth coming in the regions where our plants are located. We'll be generating a lot of cash which we'll use to pay down debt thereby reducing interest expense.

We'll continue to spend CapEx well above maintenance levels with high value return projects that will continue to set us up well for the future. The share count of the tangible equity units will drop as the stock price goes up. We should also be in a position to buy back stock in 2016. We have leading brands and market share that will allow us to grow faster than our peers, and we're not finished growing. There's more to come. So, yeah, we feel really good about 2015 and 2016. It's Tyson 2.0 and we're a different company.

And finally, I'd just like to say how pleased I am with the progress of the integration. Tyson has integrated a lot of companies in its history and I've been involved in many of them, and this has been the smoothest I've ever experienced. We love having an office in Chicago, and we're keeping key members of the team there, and in many cases, expanding their roles. We have two like-minded groups, coming together to unlock the value that we know exists. There aren't any egos in way, people aren't being territorial, they're just getting it done.

We've been using the expression one plus one equals three a lot because we see Tyson and Hillshire together as more than the some other parts. So thank you to the team for working so well together.

And now let's go to Dennis, for the financial updates.

Dennis Leatherby

Chief Financial Officer & Executive Vice President

Thanks, Donnie, and good morning, everyone. Fiscal 2014 was another record year. We delivered strong overall operating results, and used our cash flow and balance sheet to make a significant acquisition in Hillshire Brands, to further deliver and execute our value-added strategy for years to come. As a reminder, we acquired Hillshire Brands in our final month of fiscal 2014.

This morning it's important for us to demonstrate that legacy Tyson delivered on results we have previously described over the last several earnings calls, to give you a good baseline. As a result, I will be referring to our fiscal 2014 adjusted operating income and EPS for legacy Tyson only, which exclude one month of Hillshire Brands' results, the equity and debt financing impacts, as well as a few other unrelated items. Please refer to our press release issued earlier this morning for a full reconciliation of our GAAP to adjusted results.

We had a record-setting fourth quarter and fiscal 2014. Fiscal 2014 revenues were \$37.6 billion, representing over 9% growth compared to prior year as we continue to execute on our gross strategy as evidenced by increased sales in Chicken, Pork, and Prepared Foods. Total company return on sales for 2014 was 4.4% and adjusted operating income was more than \$1.6 billion representing a 20% increase over fiscal 2013.

Our adjusted earnings of \$2.94 per share represents a 30% increase over our previous record of \$2.26 last year. We achieved an adjusted pre-tax return on invested capital of just over 21% compared to 18.5% for the prior year. Operating cash flow for 2014 was \$1.2 billion which is consistent with our five year average.

We have shown the ability to sustain high levels of cash generation while still funding significant investments in working capital as we grow our business and absorb higher input costs. We spent \$195 million on capital expenditures for the fourth quarter and \$632 million for the full fiscal year. This outpaced our depreciation by \$138 million in fiscal 2014 as we continue to invest in projects with a focus on delivering high ROIC.

Our effective tax rate in fiscal 2014 was 31.6%. On an adjusted basis, this rate was 33.4%. Net debt to EBITDA for the past 12 months was 4.1 times and on a gross debt to EBITDA basis this measure was 4.3 times. On a pro forma basis, including Hillshire's results of the past 12 months, net debt to EBITDA was approximately three times.

Including cash of \$438 million, net debt was \$7.7 billion. Total liquidity was just over \$1.6 billion remaining above our goal of \$1.2 billion. Year-to-date net interest expense was \$125 million, down 9% from a year ago. Adjusted net interest expense was \$98 million representing a 29% decrease from fiscal 2013.

Our adjusted EPS reflects diluted shares outstanding of \$356 million similar to last quarter, which exclude the impact of the issuance in August of common stock intangible equity units.

As Donnie pointed out, we will close on the sale of our Brazil chicken operations later this quarter and we expect to close the sale of our Mexico chicken operations in the second quarter of fiscal 2015. The sale of both of these operations will result in more than \$500 million of additional cash we plan to use to de-lever. We moved the assets for these operations to assets held for sale in our fiscal 2014 balance sheet.

Now looking forward, here are some additional thoughts on 2015. Please note our accounting cycle results in a 53 week year in fiscal 2015 as compared to a 52 week year in fiscal 2014. Accordingly, this outlook is based on a 52 week year for comparative purposes. We expect revenues of approximately \$42 billion for fiscal 2015, which is 12% growth over fiscal 2014. This was driven primarily by a full year Hillshire brands offset by reduction from the sale of our Brazil and Mexico chicken operations.

We expect to capture more than \$225 million in synergies in fiscal 2015 from the integration of Hillshire brands and improvements in our Prepared Foods segment. Net interest expense should approximate \$285 million for fiscal 2015. We currently estimate our adjusted effective tax rate to be around 35.75%.

CapEx is expected to be \$900 million, which represents approximately \$300 million or 50% more than our depreciation expense as we continue to focus on projects that will create long-term shareholder value. Based on our share price at the start of fiscal 2015, we expect diluted shares in Q1 2015 to be around \$416 million. This includes the August 2014 issuance of common stock intangible equity units.

This morning we reported our Board of Directors increased our regular quarterly dividend from \$0.075 to \$0.10 per share on our Class A common stock payable on December 15.

We expect adjusted EPS in the range of \$3.30 to \$3.40 representing an increase of over 12% versus fiscal 2014. FY 2015 is already setting up to be another phenomenal year for sales, operating income and EPS. As we look beyond 2015, we expect to realize annual synergies of more than \$500 million by fiscal 2017. We're excited about the tremendous value we will realize from our collection of iconic brands and look forward to growing them even further.

We believe returned focused capital allocation and our diversified and balance portfolio will be the engine to deliver constant growth year-over-year. And we're raising the long-term profitability expectations for our Chicken segment to 7% to 9% and for our Prepared Food segment to 10% to 12%.

Our priorities for the significant cash flows that our operations will continue to generate are for rapid deleveraging and strengthening our balance sheet, a continued return focus on capital allocation to drive long-term shareholder value, funding acquisitions to fulfill our growth strategies and returning cash to shareholders through share repurchases and dividends, all while ensuring we maintain plenty of liquidity.

And finally, I want to remind you that on this call in 2012, after coming off two years of more than \$1 billion in incremental feed costs and facing another incremental \$600 million in fiscal 2013, we surprised some by saying we would at least hold EPS flat in 2013 and grow EPS by around 10% or more in 2014 and 2015. This was based on our belief that continued improvements in operating performance in many areas of our company was accelerating and would enable these results to be achieved. Two years later, we're pleased to look back and note that we're delivering with 15% EPS growth in 2013, and 30% EPS growth in 2014.

But we're not finished. Our new EPS range calls for at least 12% growth in 2015 amidst the game changing acquisition of Hillshire Brands. When achieved, this means our three-year compounded annual growth rate since the 2012 call would be almost 19% reflecting the efforts of a great team, that just keeps getting better. As we continue the integration process, we see the tremendous opportunity that Hillshire business and team brings to the combined company.

As we execute our Prepared Foods strategy, we're even more excited about our future as we look to create strong shareholder value along with this acquisition, that will be accretive in the fiscal 2015 and highly accretive in future years.

That concludes our prepared remarks. Robin, we're ready to begin

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from Ken Goldman with JPMorgan. Your line is open.

Ken B. Goldman
JPMorgan Securities LLC

Q

Hey, thanks for the question. I have one and then a follow-up. The first one is, Donnie, I'm hoping you can detail for us some of the synergy targets? Maybe if you can fill in the blanks, how much is expected in COGS versus SG&A, some of the pacing of savings, anything you think is important for us to know as we model numbers out here?

Donald J. Smith
President & Chief Executive Officer

A

Okay. Sure, Ken. So let me start with the types, and then we'll fill in the gap a little bit around maybe some of the amounts of when they'll come, and I also want to clear-up a little bit about what's not in the synergies that we've been talking about so far. So there's early days, there's some low hanging fruit, things like procurement. Some of the redundant functions that are eliminated, some of the service contracts, those kind of things. Now, longer-term, things like how we optimize and improve the operational efficiencies in the manufacturing plants, how we continue to optimize the network, some of the logistic savings. There'll also be some savings, we think in trade spend. So there are several broad categories that we think will find more and as you know kind of increasing savings in over time.

Let me give you a quick example. An early example that we'll see this year is freight management. So we've been able to reduce the rate structure by lowering the rates on some of the Hillshire legacy business and then capturing additional discounts from having a much larger freight base. We expect that alone to be somewhere in the \$15 million to \$25 million this fiscal year. So at this point, I feel really good about the \$225 million number this year at least that number and at least \$500 million as we go forward over the three-year target.

So I also want to add that this is pertaining by and large to the Prepared Foods segment. So if you look at our Prepared Foods segment this next year, it's roughly an \$8 billion business. And if you look at that out over the three-year synergy number, that's about \$500 million which is about 6% or so of that. Now, it's a little more front-end loaded than you would typically see with just a straight M&A deal, but you'll remember we were able to see significant synergy capture in the legacy business because of this acquisition by closing three plants and then moving that product mix around into more efficient locations.

Now, Ken, what's not in these synergy numbers so far is any growth synergy that might come. We've not included any raw material synergies. And what we want to do is to add a bit of clarity about that as we get a bit more deeply into having those discussions. We've been about two months now working together as the team, we've built very detailed business cases that we can monitor to deliver these synergies and of course we'll be reporting those out to our investors quarterly.

So [ph] looking (27:54) back to one thing just for clarity, some of the things like shared service synergies that type of things will be seen across all of our segments, but the majority of the synergies will reside in the Prepared Foods segment.

Ken B. Goldman
JPMorgan Securities LLC

Q

That's helpful. If I can be very quick here in the follow-up. You mentioned even though next year has an extra week, items in your outlook are based on a 52 week year, but just to be clear, when you talk about that at \$3.30 to \$3.40 in EPS, is it fair to assume that range as 53 weeks or is that also 52 week, with upside of that number from the extra week?

Donald J. Smith
President & Chief Executive Officer

A

Ken, that's for 52 weeks.

Ken B. Goldman
JPMorgan Securities LLC

Q

Okay. Thank you.

Operator: Thank you. Our next question is from Brett Hundley with BB&T Capital Markets.

Brett M. Hundley
BB&T Capital Markets

Q

Hi, good morning. Can you hear me gentlemen?

Dennis Leatherby
Chief Financial Officer & Executive Vice President

A

Yeah.

Donald J. Smith
President & Chief Executive Officer

A

Hi, Brett.

Brett M. Hundley
BB&T Capital Markets

Q

Thank you for taking the questions. My first question is on the Chicken segment, you guys have – first of all, you've upped your normalized range, you continue to talk to 10% plus for next year, and the theme seems to be as of late ways that companies can insulate themselves in 2015 and beyond. You touched on that a little bit in your prepared remarks, but I'm wondering if we can delve back into it. One other thing that we're hearing in particular is that small bird operators are signing very favorable contracts with QSR guys, foodservice guys for multiple years out. I'm wondering if you guys are seeing that in your own business and again going back to the original question, the insulation you see in your chicken business going forward?

Donald J. Smith
President & Chief Executive Officer

A

Yes, certainly we are. We have seen good price increases in our small bird category as customers look to ensure supply there, but as importantly, there're several things that we've been able to do to insulate our business a bit. Number one, we're certainly a much more fundamentally sound company than we have been in the past and we continue to improve there.

We continue to invest in our business. We've improved our revenue by pricing and mix by the way. So what I mean by that is we've reduced our risk to grain market fluctuations and we've gotten a much better understanding of how the consumer is changing. Our fresh chicken business is doing very well. That's a very good business for us and we can see continued growth there. As you know our business model tends to better against the whole bird model than it does against just the UB parts. And so as the small bird business improves and the tray pack grows and you can't forget the additional value-added that we have, those are certainly things that insulate our business in the future.

Brett M. Hundley
BB&T Capital Markets

Q

Thank you much for that. And then, Dennis, just I had a follow-up question. As it relates to the way that you or rather the balance that you try to strike between looking at further M&A targets out there and then debt pay down. And I guess I'm just curious is there a certain level of debt pay down and then a switch gets flipped and you can say all right we can start looking at M&A again. Can you look at M&A right now? And as a follow on to that question, if there was a foodservice focus target out there in packaged meat, do you think there would be any trust issues for you guys going ahead and acquiring something like that?

Dennis Leatherby
Chief Financial Officer & Executive Vice President

A

Okay. Great series of questions. The way we look at M&A in our capital structure is that we put together this financing and capital arrays in a manner to assure that we've investment grade ratings. Right now net debt -to- EBITDA is around three times. We're going to throw off better part of \$1 billion of free cash flow. We're going to raise another \$500 million through the sale of Mexico and Brazil. So that will be used to de-lever and we would see net debt-to-EBITDA trending toward two times by the end of this fiscal year. That puts us in a pretty good place to re-leverage if we so choose.

We think that that we're in a much better position from a stability standpoint from an earnings and cash flow standpoint. So we're in really good position and we're certainly ready and willing to look at M&A to the extent it makes sense for us and it fulfills our growth strategies. As far as foodservice goes, I'm not sure that I know how to comment on that.

Brett M. Hundley
BB&T Capital Markets

Q

Thank you.

Operator: Thank you. Our next question is come from Farha Aslam with Stephens. Your line is open. Farha Aslam with Stephens. Your line is open. You may want to check your mute button, your line is open for your questions Farha. I'll move on to the next question, Adam Samuelson, Goldman Sachs. Your line is open.

Adam Samuelson
Goldman Sachs & Co.

Q

Yes, thank you. Good morning, everyone. Maybe a little more detail on the Chicken outlook. And as you think about the 7% and 9% normalized range, how should we think about the further processing percent of the mix on a normalized basis going forward? Clearly, that's something that's changed in how you're running that business and as a driver to normalize profitability to dampen the cyclicity. But as we think about the further process, how big of that is -- is that of your earnings mix at this point?

Donald J. Smith
President & Chief Executive Officer

A

Adam, let me add a little bit of color to that too. I mean, we feel that over the next two years, three years, four years, something like that, how beef and pork prices relatively speaking are going to continue to drive demand towards chicken. Also as the millennials enter the workforce they index very heavy towards chicken. So we feel like that's a meaningful consumer shift that will allow us to continue to grow our business well into the future. So we predict over the next couple of years at least a 3% increase in demand for chicken. And if you'll go back, it's been a long time, probably since 2006 or 2007, since we've been able to talk about a structural shift in consumption that would drive that demand.

So then if you look at foundationally a 3% or so demand increase driven both by high competing prices as well as preference to chicken from the millennials then how do we go to market against that? Well, for us chicken is certainly a great component and that adds incremental margin to anything we would do on just pure commodity basis.

By the way, about the only commodity part, just pure commodity part that we would sell would be a frozen leg order internationally. And so, which by the way favors us in times of an increased supply because we can then buy parts that we need on the outside market, add value to those through our further process capabilities.

So let me get to that part of the question. Last year, I noted on a couple of our calls that we were completely tapped out on FP capacity. Well, our two plants that we've been having issues with are completely back up into speed and we have incremental FP capacity there plus we have two more lines that will be coming on stream in the spring. And so some of our foodservice customers would have probably inserted more chicken promotions had there been industry capacity to actually produce the product where we're supplying that industry capacity this year. So we feel like that will give us an incremental improvement.

Another thing that I can add is that even though through the years, our leg quarter volume is down, the reason it's down is because we've been able to take advantage of a bit of an incremental shift to more boneless dark meat in our business. So if you look at the price comparison to boneless dark meat versus a boneless skinless breast meat. There are times when boneless dark meat is almost at parity in the marketplace with boneless skinless breast meat, so we're chasing that new demographic shift too. So that may have been a much more detailed option. But we are – answer than you were looking for, we are very optimistic about the demand in our Chicken segment.

Adam Samuelson
Goldman Sachs & Co.

Q

I appreciate the color. And then just as a follow-up, I guess you've got good detail on the demand side, on the supply side you do kind of own one of the main primary breeders in the industry. Can you talk about what the Cobb-Vantress order book looks like as you evaluate the outlook for supply growth in particularly 2016?

Donald J. Smith
President & Chief Executive Officer

A

I'll tell you this. Over the last couple of years or so most of the primary breeders have experienced some production issues. It appears that most of those production issues are now correcting themselves and that there will be some incremental supply capability.

Now, if you look at the bullet placements, it's going to be at least June, July, or something like that of next year before there is significant supply. And you got to remember the structural issues affecting the supply growth. Chicken house is getting built, hatchery is needing to be built. Those types of things, our hatchery capacity is about

as high as an industry our percent capacity is about as high as I've seen it in a long, long time. So we think that you'll probably see somewhere in order of magnitude of about a 3% or so percent growth in supply. And I'll tell you the demand for chicken needs that type of supply come into the market and we're looking forward to our buy versus grow strategy, we're buying the parts we need and add value to them through our further processing capabilities and continuing to drive our margins.

Adam Samuelson

Goldman Sachs & Co.

Q

All right. Thanks very much. I'll pass along.

Operator: Thank you. Our next question is from Diane Geissler with CLSA. Your line is open.

Diane R. Geissler

CLSA Americas LLC

Q

Good morning.

Donald J. Smith

President & Chief Executive Officer

A

Good morning.

Diane R. Geissler

CLSA Americas LLC

Q

So you had called out in your press release that there was a negative impact from purchasing product, I guess in the open market which I think is obviously part of our buy versus grow strategy, but could you – is that a surprise to you that it just rose more rapidly than you expected it to? And is there any way you can sort of quantify how much that was above your expectations?

Donald J. Smith

President & Chief Executive Officer

A

Yeah. Sure Diane. I sure will. As you know in the back half of the year, we had some fairly significant production issues in our fully-cooked value-added retail business. And obviously, we were disappointing customers with our fill rate and frankly we wanted to make sure that that was the only area of our business where we were disappointing customers. And so, we made the choice in our tray-pack business, and I think, you've seen the growth in fresh tray-pack with these really high beef [indiscernible] (40:15), ground beef prices at retail really high beef price. There's been a shift into fresh tray-pack. And we just didn't want to disappoint our customers in that part of our business too, so we made the conscious choice to be out on the market buying breast meat and then using internal breast meat to put it in a tray and make sure that we did not disappoint our customers particularly around the holidays.

And I'll tell you, we did a great job of order fill, it cost us a little bit of money, we were out there probably buying. I think, for the quarter we bought about a 100 loads of breast meat a week on average and you know what the market prices were. And typically we would have been closer to the 50 load, 55 load a week type range, but that was a conscious decision, I'm going to guess maybe it cost us, I don't know \$1.5 million, \$2 million a week, something like that for that quarter. And you know what it was right thing to do because we kept those valuable customer relationships. And as we bring this new tray pack capacity and this new further processing capacity on stream, we'll be able to capture that market share back. So we're positive we did the right thing although it did cost us a little bit of money in the quarter.

Diane R. Geissler
CLSA Americas LLC

Q

Okay. So it sounds like it was more of a production issue rather than you misjudging the market, is that a fair statement?

Donald J. Smith
President & Chief Executive Officer

A

By and large, I believe, that's correct, yes.

Diane R. Geissler
CLSA Americas LLC

Q

Okay. And then I wanted to ask about China where, obviously, the hopes are that that business will get some traction and really start pulling in some earnings, especially with what we've seen in terms of growth of the QSR channel, but it's been such a rocky road for those companies the re with sort of quality issues one after another. I guess could you talk a little bit about what you're seeing in China, what your customer base is telling you, I would think that with what happened over the summer with one of the large suppliers there that some of these companies would be knocking wildly on your door looking for supply, but that doesn't seem to be the case. So just talk a little bit about what your customer base is saying there about their proclivity to use you as a supplier?

Donald J. Smith
President & Chief Executive Officer

A

Without being too specific, about any individual customer, the issue is with these back-to-back food scarce, demand for poultry is down. Now, I mentioned in our prepared remarks that we remain in a bit of holding pattern and what that means is that we have acquired land use rights and we have the capabilities to be able to build on those parcels of land whenever we start getting some demand signals that would indicate it's time to do so. We saw a little bit of light in the day-old chick market and then we saw a little bit of light in the market bird pricing, but then this last market scare, it once again decreased the demand for the product.

So I do think it validates our model that with this safety from the farm all the way to the retailer or to the foodservice customer that we're on the right track. As you could well imagine it's a big frustrating when demand drops like it has and certainly, I think our customers understand what we have to deliver in our model and what that can do to help their business, and we feel if we get any light at all in the demand for poultry that we'll start seeing some improvement.

Diane R. Geissler
CLSA Americas LLC

Q

Have your customers given you any indication of when they expect to see demand snap back?

Donald J. Smith
President & Chief Executive Officer

A

We really haven't.

Diane R. Geissler
CLSA Americas LLC

Q

Haven't. Okay. All right. Great. Thank you.

Operator: Thank you. Our next question is from Tim Tiberio with Miller Tabak. Your line is open.

Tim J. Tiberio
Miller Tabak + Co. LLC

Q

Good morning. Thanks for taking my question. Obviously, your Prepared Food long-term operating margin guidance is well above your – what you've ever realized in legacy Tyson business and obviously is also a bit higher than even with Hillshire has seen in recent years. I would assume that most of this step-up is coming from synergies that you've outlined, but can you provide us maybe with a little bit more detailed frame up of the sensitivity of getting to that 10% to 12% operating profit margin range? How much is coming from synergies versus the potential for improved input costs as the hog herd expands? And then finally, how much sensitivity is coming from some of these new products that you've launched, particularly in the lunch category and also in the snack categories?

Donald J. Smith
President & Chief Executive Officer

A

Okay, Tim so, a couple of things. Number one, if you remember, when we closed the three facilities in our Prepared Foods business, that began our ability to take our product mix and put it into the most efficient plant from a production standpoint and from a network optimization standpoint. So we'll continue to see that develop. So if you look out over time, and the synergy capture, if you take the traditional, call it, legacy Tyson business, and put it in its normalized range, and then you bring the Hillshire business into that, and then take the preponderance of the \$500 million in synergy and do that math forward, you're pretty easy in that 10% to 12% return on sales.

Plus then with efficient MAP spending and new innovation capabilities across the business, we've been able to take foodservice innovation, and have that cross into the retail channel then you're able to see some good growth synergies that will happen over time, and we've not quantified that specifically yet, but we will over time. And so I think that's kind of the growth algorithm forward to be able to see how we're going to get to that 10% to 12%.

Tim J. Tiberio
Miller Tabak + Co. LLC

Q

Great. And just one last follow-up question, looking at some of the overlaps in the legacy and Hillshire brands, has there been any final decisions of which brands are staying particularly in the breakfast category? How should we be thinking about that as we model out that division going forward?

Donald J. Smith
President & Chief Executive Officer

A

Yeah. Well, I can tell you that we discontinued any investment at all in day starts or any of the Wright Brand sausage [indiscernible] (47:33) – any of the Wright Brand sausage that we were doing all of that obviously will go into Jimmy Dean. We have been a fairly successful though about not losing those slots, and we've been able to work with our retailers to be able to slot Jimmy Dean branded products into the slots that previously day starts had we – and we appreciate our retailers working with us on that.

So we do have a great portfolio of iconic brands and we'll continue the growth trajectory that they've been on. We haven't had a chance yet to grow through a detail of every brand or every label that we have. That work will be done. We've really spent the last three months making sure through the integration that we've got our teams in place, that we got the organizational structure like we want it going forward that every team member knows what their role is and that type thing, and we intend just in the next few weeks to be transitioning into the new work

structure that we talked about which – by the way that is very rapid. So that's been our overall focus at the beginning. And now that we've – once we get transitioned into the new organization, we'll certainly have our brand teams and we've got great capabilities there to look across our business, at are brands and understand how to maximize the portfolio.

Tim J. Tiberio

Miller Tabak + Co. LLC

Q

Great. Thanks for your time.

Operator: Thank you. Our next question is from Michael Piken. Your line is open, with Cleveland Research.

Michael L. Piken

Cleveland Research Co. LLC

Q

Yeah. Hi, good morning. I just want to get a little bit more of an update for your expectations for how big of an issue PEDv might be this winter and kind of where the industry is from about biosecurity standpoint as well as the efficacy of some of the vaccines that are being worked on? Thanks.

Donald J. Smith

President & Chief Executive Officer

A

Sure. We spend a lot of time talking to our producers. We're sort of in a transition period here, typically accessions, if there are going to be a higher number of accession will begin occurring a little bit later in the fall and winter. But what we can see so far in talking to our producers who, I think, have done a tremendous job about increasing biosecurity in their locations.

I feel confident through our conversations with them that accessions won't be as high in 2015 as they were in 2014. Now, what kind of spread, I think it's a little early for us to be able to call the kind of spread versus a year ago. But I will say that the reason I feel so confident about that is this has been one of our better years in parts and so with the biosecurity that we've put in place or that our producers have put in place to help handle PEDv, they've also given themselves the benefit in parts. So we're confident that next year shouldn't be as bad. It's a little too early to call what we think it will be. As we've rounded out, when you consider hog waste and our projection around sort of our first guess is around the PED and the head count, we're looking for about a 2%, maybe 3% increase in overall production, and certainly beef prices will be able to sustain that in the marketplace, and we think whole together pretty good cut outs. We're looking forward to a good year in our Pork segment.

Michael L. Piken

Cleveland Research Co. LLC

Q

Okay. Great. And then just sort of as a follow-up, just thinking about pork and really your overall business, I mean with the acquisition of Hillshire, what should we be thinking about as exports in the future as a percentage of your overall sales for both pork and beef, and chicken as well? Thanks.

Donald J. Smith

President & Chief Executive Officer

A

Michael, roughly the same. I don't see a significant shift one way or the other. The individual part may change, but I don't see a significant shift in exports.

Michael L. Piken
Cleveland Research Co. LLC

Q

Okay. Thank you.

Operator: Thank you. Our next question is from Farha Aslam, with Stephens Incorporated. Your line is open.

Farha Aslam
Stephens, Inc.

Q

Hi. Thanks for taking the follow-up.

Donald J. Smith
President & Chief Executive Officer

A

Hi, Farha.

Farha Aslam
Stephens, Inc.

Q

My question goes to consumer demand. Throughout your call, you've been very, very confident about the outlook for demand in your businesses. Could you talk about just how the consumer is approaching protein and how perhaps retailers are managing inventory differently because we're hearing the largest retailer in the U.S. has been expanding meat inventories, particularly in their frozen area because they've been seeing very strong demand?

Donald J. Smith
President & Chief Executive Officer

A

Farha, I can't comment about what individual retailers would do, but I will tell you about our business. So as you know with really high beef prices, beef volume is down. And as we look forward, both at retail and at foodservice, we continue to see that favoring chicken. We think chicken demand will be up at least 3% next year, and I would think, again, in 2016 because we already know that the beef supply, the beef herds are going to be down another 4%, which portends pretty high beef prices again into the future. So we think that is a strong demand signal for chicken. And also there's the generational issue that we're beginning to see in the marketplace with the millennials entering the marketplace and they index quite high versus chicken. And so we think that is also going to be driving consumer demand for chicken out front. That helps?

Farha Aslam
Stephens, Inc.

Q

Yeah, that's helpful. And then just as a follow-up, as we you see the combined Tyson, Hillshire business. Could you just comment on, going to market as a combined company? Have you identified yet any advantages that you can point to about that combined entity versus each company individually going to the market?

Donald J. Smith
President & Chief Executive Officer

A

Absolutely. I mean, bringing together these great iconic brands that have very strong meaningful positions in their categories, and our ability to take this innovative and insights driven innovation and brand building capabilities that are coming into the business with the Hillshire team, and being able to work with our customers to be able to drive the categories that drive their growth, that's a very meaningful change going forward.

Mow, a you look at the categories, particularly at retail that are growing, say just for example in frozen, of course breakfast is growing across refrigerated and frozen, but frozen breakfast, particularly frozen handheld breakfast is a great category. Frozen fully cooked chicken is a great category, and we certainly have leading positions in both of those categories and great insights about how to continue to drive growth forward.

I mentioned in my prepared remarks, the snacking platform. And we look forward to the growth that we'll see in that snacking platform. We also have great brand building capabilities now around our NatureRaised Farms no-antibiotics-ever. We've seen double-digit growth and we're just putting together a phenomenal team of insights driven innovators and brand builders, who can continue to take this portfolio of products and grow our customers' businesses and meet this consumer needs as they change. So we're very optimistic about how that will drive our future.

Farha Aslam

Stephens, Inc.

Q

Fantastic. And just one last question. About Mexico, we continue to hear disease issues impacting Mexican chicken supplies, is that impacting U.S. chicken availability or have you been able to – or the industry been able to work around that in terms of supply available in the U.S.?

Donald J. Smith

President & Chief Executive Officer

A

I don't see it impacting the supply available in the U.S. It does at times impact the demand for export leg quarters. There are times when demand for export leg quarters from the U.S. into Mexico is rather strong and then maybe in response to some of the disease issues, the market down there becomes saturated as more people bring birds to the market and it changes a little bit the demand for the exports, leg quarters going down there, but that's really about the only impact we see to the U.S. market from Mexico.

Farha Aslam

Stephens, Inc.

Q

Great. Thank you very much.

Donald J. Smith

President & Chief Executive Officer

A

Sure.

Operator: Thank you. Our next question is from Ken Zaslow with Bank of Montreal. Your line is open.

Kenneth B. Zaslow

BMO Capital Markets (United States)

Q

Hey, good morning, everyone.

Donald J. Smith

President & Chief Executive Officer

A

Hey, Ken.

Dennis Leatherby

Chief Financial Officer & Executive Vice President

A

Good morning.

Kenneth B. Zaslow

BMO Capital Markets (United States)

Q

So a couple questions. How much of the synergies would have been from legacy Tyson of that \$225 million in the \$500 million?

Donald J. Smith

President & Chief Executive Officer

A

A bit over a \$100 million. Somewhere probably between a \$100 million and a \$150 million, something like that. Most of those would have been in the year one, so call it \$100 million to \$150 million of the \$225 million and then going forward, it's more the incremental value of the Hillshire Tyson combination.

Kenneth B. Zaslow

BMO Capital Markets (United States)

Q

Great. And my second question is what is the underlying growth outlook for Hillshire. It seems like from your synergies and ex obviously legacy type business, because it seems like you're just using the \$400 million of EBIT from last year and just kind of rolling that forward. I'd be surprised if you'd buying a business and you'd expect to have flat growth in the year.

Donald J. Smith

President & Chief Executive Officer

A

Yeah, we're optimistic about the growth of the business going forward as we – so, Ken, remember our comments around the incremental \$140 million or so of raw material pricing coming and that's primarily around beef raw material and turkey, which frankly the Hillshire legacy business over-indexes towards the beef raw material increases versus what the legacy Tyson business would have done, think the beef and sausage and hot dogs and that kind of things. So we're pricing to recover that and we will, particularly as we, the earnings cadence will be back half driven. And so in year one, we're pricing to recover those raw materials. Certainly, as we move forward and we get beyond that then we'll be able to drive, I think, fairly significant incremental growth with some effective MAP spending. So we're very confident in the growth of those brands.

Kenneth B. Zaslow

BMO Capital Markets (United States)

Q

But when your turkey, – I thought, turkey expansion is happening, I'd expect the turkey prices to start to rollover over the next six months to nine months, is that not [ph] we should (59:11) expect?

Donald J. Smith

President & Chief Executive Officer

A

Our projection for turkey raw materials impacting our business will be up in 2015 versus 2014.

Dennis Leatherby

Chief Financial Officer & Executive Vice President

A

I think, Ken, it's fair repeating that, this is going to be a big front-half, back-half story as we overcome the raw material input prices, so you'll see quite a bit of lift in Prepared Foods both in overcoming the raw material price increases, and the synergies as they build on and the growth in legacy Hillshire.

Kenneth B. Zaslou
BMO Capital Markets (United States)

Q

And my final question is when you talk about the outlook for pork, and we didn't really touch on it that much, but it seems to me that pork supply is going to be up anywhere from 3% to 6% or so, and yet you're expecting pork packer margins to be roughly within the normalized range. What would make you feel more comfortable that the pork packer margins would be above the normalized range given we're going to see an expansion of hog? I would have thought that would have been a good thing for you.

Donald J. Smith
President & Chief Executive Officer

A

So perhaps, exports would increase our confidence if we see some movement along that line. We're pretty comfortable with a 3% or so increase in supply, and we think the market will easily absorb that type of supply increase, particularly with this really high halo that beef prices are providing. But we'll have to keep watching the dollar, but we feel comfortable with the export demand for our pork in China, Russia et cetera. And so I really don't view – I feel very comfortable in our range, might see above it depending on if that develops and we hope it would.

Kenneth B. Zaslou
BMO Capital Markets (United States)

Q

Great. I appreciate it.

Operator: Thank you. Our next question is from Robert Moskow with Credit Suisse. Your line is open.

Rachel N. Nabatian
Credit Suisse Securities (USA) LLC (Broker)

Q

Good morning. It's Rachel Nabatian in for Robert Moskow.

Donald J. Smith
President & Chief Executive Officer

A

Hi, Rachel.

Rachel N. Nabatian
Credit Suisse Securities (USA) LLC (Broker)

Q

Hey. So my question is on chicken productivity. We like to look at the ratio of chicks [ph] placed to ex-set (01:01:27) and in the last month this increased over last year's level. So I wanted to know if there's something sustainable driving this perhaps an increase in the supply of the hatching flock is driving a younger average age, which is more productive. And then as a second part from what I recall last year, a good number of eggs are destroyed during transportation because of the colder than usual winter weather. So I wanted to know if there are any learnings from this and how your company is prepared if the weather this year is as bad as it was last year?

Donald J. Smith
President & Chief Executive Officer

A

Okay. Let me, obviously, I'll start with your first one. Actually, our hen age is – so I'll talk about the physiological productivity first. The hen age and the hatchability. The hen age is probably still around 63 weeks to 65 weeks, hatchability is probably down about 1% from what we've seen over the last quarter or so. So I don't really see the actual productivity of the flock very differently. Here's what I see. We've seen that the industry has not taken the

production cuts. The cuts in [ph] sets in (01:02:45) placement that it normally would in previous years, and so the reason you're seeing [ph] sets in (01:02:53) placements above a year ago is because you can, because this quarter integrators could choose not to take the cut that they took last year, and so there is an ability to increase this quarter.

I think what you'll see once we get into the late December, early January is we get back to about 1% or so change versus a year ago because you don't have this ability to grow versus a year ago due to the holiday cuts.

Remind me on the second question again, I'm sorry.

Rachel N. Nabatian

Credit Suisse Securities (USA) LLC (Broker)

Q

I just wanted to know if the colder than usual winter last year, do you think is there any – I feel like a lot of the supply was kind of cut because a lot of the eggs were destroyed during transportation...

Donald J. Smith

President & Chief Executive Officer

A

Yeah.

Rachel N. Nabatian

Credit Suisse Securities (USA) LLC (Broker)

Q

Because of the colder weather, so I just wanted to know, if there are any learnings from that, and what you expect for this year from that end?

Donald J. Smith

President & Chief Executive Officer

A

Got it. I could tell you, we're in better shape on propane than we were a year ago. You'll remember, we actually created a kind of a small propane delivery company to keep a lot of growers in propane. We're much better prepared for that. We have looked forward and we do think we have adequate transportation capacity to be able to hold the loads. The big thing last year was just the weather and road closures and those types of things. We can position inventory a little bit differently, but if the road is closed, the road is closed. So those type of events are very hard to predict. I think we're in great shape going into FY 2015, and feel very good about demand and how we've prepared ourselves to be able to deliver to the [indiscernible] (01:04:42).

Rachel N. Nabatian

Credit Suisse Securities (USA) LLC (Broker)

Q

Got it. Very helpful. Thank you.

Operator: Thank you. Our last question is from Akshay Jagdale with Key Banc Capital Markets.

Akshay S. Jagdale

KeyBanc Capital Markets, Inc.

Q

Good morning.

Dennis Leatherby

Chief Financial Officer & Executive Vice President

A

Good morning.

Donald J. Smith

President & Chief Executive Officer

Hi, Akshay.

A

Akshay S. Jagdale

KeyBanc Capital Markets, Inc.

Q

Hi, congratulations on the good results. So my first – I just wanted to talk a little bit about the Chicken segment and then ask you a questions on Hillshire. So on Chicken, clearly two parts. One, you haven't really delivered a 10% or above margin even on a quarterly basis, just to push back. So can you tell me how we should think of next year being above 10% and why we should feel confident about that. And perhaps you could talk about how the quarter is trending right now? I mean, obviously you have the lower grain costs which will help you by about \$0.03 a pound, but your pricing performance the last couple of quarters hasn't been really that great or price realization, so if supply is potentially increasing, I'm guessing you're going to give back some on pricing, your volume is going to be up a little bit, but I just – I want to see why you have the comfort level to say you're going to earn above a 10% margin on Chicken? So that's my first question.

And then a second one is, you raised your normalized margin range and what we've seen is in the bottom of the cycle when the industry is losing money, you tend to do a lot better and at the top of the cycle, clearly companies like Pilgrim's are doing much better than you. So can you talk about the bottom end of your range and the comfort level you have with that if and when chicken supply, the chicken industry sort of oversupplies the market?

Donald J. Smith

President & Chief Executive Officer

A

Okay. So to your first part, our pricing has not going down. We feel very good about our pricing so far. If you'll remember, we have a much more whole bird equivalent exposure plus a lot more FP capacity built into the portfolio.

Now, remember in the last couple of quarters, we've had some production issues that have cost us some money, so kind of erase that that picks up at least [ph] 50 bps (01:07:08) plus a quarter. If you'll remember over the last couple of quarters, I mentioned on a call or on a question earlier that we spent some incremental money, call it a couple of million or so a week in tray pack, to be able to make sure we didn't disappoint our customers. So kind of scratch that and then you can get to about 10% on the last quarter there.

Now, let's move forward. Demand up about 3%. We feel very good about that, where is the demand shifting. The demand is shifting towards tray pack which is a great business for us and we're very, very good at it, and it wants to shift towards FP, there's just not been enough capacity to fill the orders. We're changing that dynamic this quarter, we now have full productive capability of all of our existing lines, and we're going to be bringing two more lines on stream in the spring.

So on top of all of that, if you include the \$350 million that we'll see in incremental grain cost or grain savings then that will help us. So I think that gives us a lot of confidence going forward, we'll continue to see some operational improvement throughout the year as we continue to advance ourselves in our lean and lean Six Sigma. So we feel good. And as I mentioned in the prepared remarks, we're off to a great start, so feel really good about it.

Now, as to the range, you're absolutely correct, our goal is to have consistent, stable growth and earnings growth. And so in the summer time when the commodity prices reach their peak, you're right, we typically don't do as well

as some of our competitors, but obviously in times when other parts of the year we do much better. What we want to provide is stable earnings growth for our investors and that's what our model is geared to do.

So as we look forward with an increase in demand, which we've not seen now for several years. If you take the market fluctuations and our buy versus grow strategy, if commodity prices get fairly, let's call it cheap, if you will then we're able to buy that raw material and put it into this further processing value added production model and create incremental margin on that, which gives us the confidence in the lower end of our range.

Akshay S. Jagdale

KeyBanc Capital Markets, Inc.

Q

And is the lower end of your range, I mean, do you expect to hit that when the market is oversupplied, meaning when commodity companies are losing money, would you expect to be at the lower end or could you be below the lower end?

Donald J. Smith

President & Chief Executive Officer

A

Akshay, that obviously, you're getting into individual scenarios, how much money are they losing and that type of thing and I don't know that that is as productive. So what we can say is we feel very comfortable with the range moving up and we'll continue to look at the range and if we need to take it higher in the future, we will, but we feel very confident about our ability to deliver. And we think, there's – there are structural changes in our business that give us the opportunity to continue to deliver against that.

Akshay S. Jagdale

KeyBanc Capital Markets, Inc.

Q

Okay. And just one last one, on your Prepared Foods business and the commodity outlook. You've been behind the eight ball on your legacy business, it seems like for almost two years or something. It's been a long time you always catching up on the cost and you're saying, Hillshire is also going to be catching up the first-half of the year. Can you just give us some little bit more color as to the type of increases you're expecting in fiscal 2015 for that cost basket for your Prepared Foods business?

Donald J. Smith

President & Chief Executive Officer

A

Well, the incremental costs year-over-year will be \$140 million. Now, if you remember in my prepared remarks I said that in the legacy Tyson business, we've recovered that, but we got to stay diligent to keep working on our pricing as we move forward to get on top of the incremental raw material inputs that are coming.

Again, pretty heavily driven by beef and by turkey pricing. So we know what we have to do and we know what parts of the business we have to continue to drive that pricing in and feel comfortable that this will be a significant – this year will be a significant improvement to our previous years. And might I note too that the legacy Tyson business was not just plagued by the pricing lag, it was also plagued by an inefficient supply chain. And we made corrections at the end of last year to correct those inefficiencies because we had this new Hillshire production network that we can move a lot of those products in and optimize that network. So that will bring incremental benefit. We'll see a lot of that in fiscal 2015.

Akshay S. Jagdale

KeyBanc Capital Markets, Inc.

Q

Okay. Thank you.

Donald J. Smith
President & Chief Executive Officer

A

You bet.

Donald J. Smith
President & Chief Executive Officer

So thank you all for joining us on the call today. We always appreciate your interest in our business. Follow-up with Jon throughout the rest of the day and I want to wish you all a very happy Thanksgiving. Thank you.

Operator: Thank you. This does conclude today's call. You may disconnect your lines and have a great day.

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