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Tyson Foods, Inc. (TSN)

Q3 2018 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning and welcome to the Tyson Foods Third Quarter Earnings Conference Call. All participants will be in listen-only mode. [Operator Instructions] Please note this event is being recorded.

I would now like to turn the conference over to Jon Kathol, Vice President of Investor Relations. Please go ahead, sir.

Jon Kathol

Vice President-Investor Relations, Tyson Foods, Inc.

Good morning and welcome to the Tyson Foods, Incorporated third quarter earnings conference call of the 2018 fiscal year. On today's call are Tom Hayes, President and Chief Executive Officer; and Stewart Glendinning, Chief Financial Officer.

Slides accompanying today's prepared remarks are available as a quarterly supplemental report on the Investor Relations website at ir.tyson.com. Tyson Foods issued an earnings release this morning, which has been furnished to the SEC on Form 8-K and is available on our website at ir.tyson.com.

Our remarks today include forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. These statements reflect current views with respect to future events, such as Tyson's outlook for future performance on sales, margin, earnings growth, and various other aspects of its business. 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 the release issued earlier this morning and our filings with the SEC for a discussion of the risks that can affect our business. I would like to remind everyone that this call is being recorded on Monday, August 6 at 9:00 a.m. Eastern Time. A replay of today's call will be available on Tyson's website approximately one hour after the conclusion of this call.

This broadcast is the property of Tyson Foods and any redistribution, retransmission, or rebroadcast of this call in any form, without the expressed written consent of Tyson Foods, is strictly prohibited. Please note that our references to earnings per share, operating income, and operating margin in today's remarks are on an adjusted basis, unless otherwise noted. For reconciliations to our GAAP results, please refer to this morning's press release.

I'll now turn the call over to Tom Hayes.

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

Okay. Thanks, Jon, and good morning, everybody. Thanks for joining us today. While our business continued to grow in the third quarter, we are clearly not satisfied with our results, particularly in our Chicken segment, intertwined with uncertainty in trade policies and tariffs are increasing supplies of relatively low priced beef and pork that are competing with chicken.

Typically, in Q3 and Q4 we expect strong chicken demand, driven by the grilling season and normal summer feature activity. Instead, cool Memorial Day weekend weather curbed demand, while competing proteins displaced chicken in retail and foodservice promotions. To recover, we are aggressively addressing costs and capturing new feature activity and by keeping our inventories low, we can quickly react to market changes.

Rising freight costs have been a challenge for all of our businesses. We now expect freight to be about \$270 million more this year compared to last year, with a net effect for FY 2018 estimated to be around \$0.33 per share. On a run rate basis, we recovered about 85% and we plan to reach 100% once our longer-term contracts expire and new pricing terms take effect. Our efforts to recover price are likely curbing short-term growth. We are growing, but not as fast as we could be and not as fast as we want to be.

Despite the current trade issues, global protein demand continues to grow. Our products are moving in the export markets, albeit at lower values. We're working to strengthen our existing relationships certain markets and build inroads into new markets.

In Q3 we demonstrated the value of playing across all proteins. We delivered strong results in our Beef and Prepared Foods segments, offsetting lower margins in Chicken and Pork. Sales volume of value added products was up 2.6% compared to third quarter last year.

We're managing costs tightly across the company. Ongoing Financial Fitness savings were \$66 million in the quarter and \$168 million year-to-date. We're on track to exceed our \$200 million target this year and an incremental \$400 million over the next two years. Having this cost program and the continuous improvement mindset already established is proving to be beneficial when facing the current challenges in the market.

While we're focused on costs, we're also making strategic investments in our people and our business. Our efforts to improve employee satisfaction are already proving results, with improved safety and retention in tight labor markets. Our CapEx investments are yielding real P&L benefits by driving innovation and improving supply chain capabilities and production flexibility.

Now I'm going to ask that Stewart take us through the financials as well as our segment results in Beef, Pork, Chicken, and Prepared Foods. Stewart?

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

Thanks, Tom, and good morning, everyone. Third quarter EPS of \$1.50 is up 2% compared to Q3 last year, excluding the \$0.20 tax benefit. As we announced last week, we revised our annual EPS guidance down to \$5.70 to \$6 per share. Our original forecast was underpinned by a strong fourth quarter, but we saw market weakness carryover from the end of Q3 into the first three weeks of Q4, when we had been expecting improvement.

While external factors continue to pressure our business, we believe in our ability to create long-term shareholder value. There are many positives to focus on; our business model, our diversified portfolio, and our ability to generate cash. Year-to-date operating cash flows are very strong at \$1.9 billion, which is up 33% compared to last year.

Third quarter revenues were up 2% to more than \$10 billion, with total company volume up 30 basis points. Operating income was \$816 million, up 8% versus Q3 last year, and total company return on sales was 8.1%. Our \$328 million in capital expenditure outpaced depreciation by \$144 million, as we continue to invest in projects with a focus on delivering returns well in excess of our cost of capital.

Through the third quarter, total share repurchases for the year were 5 million shares for \$367 million. Our adjusted effective tax rate for the third quarter was 25.2%. Net debt to adjusted EBITDA was 2.3 times. Excluding cash of \$170 million net debt was just under \$10 billion and total liquidity was \$894 million at the end of Q3.

Net interest expense was \$87 million in the third quarter and \$257 million for the first nine months of the year. We expect approximately \$275 million of incremental cash flow in fiscal 2018 as a result of tax reform. And now I'd like to review our performance and provide an initial outlook for our business segments.

The Beef segment performed very well in Q3, with operating income of \$319 million and an 8% operating margin. Compared to the third quarter last year, sales volume increased 2.7% and, while average price decreased 2.8%, revenue remained relatively flat. Beef results were driven by strong demand and increased availability of cattle near our plants.

Demand for our case-ready products continues to grow and we're also seeing sizable growth in our premium programs, including Certified Angus Beef, Open Prairie Natural and Chairman's Reserve Certified Premium. With the Beef segment strong performance, we believe it will finish fiscal 2018 with operating margin above 6% and similar results expected in fiscal 2019. The cattle supply appears to be set-up well for fiscal 2019 and supply should be adequate into 2021.

In the Pork segment, we generated operating income of \$67 million with a 5.6% margin. Revenue was down due to a 2.1% decline in volume and 7.4% lower average price. The supply/demand imbalance compressed our Pork margins, exacerbated by reduced export values. Pork prices are down by more than \$6 per head, but hog costs did not follow. We will continue upgrading our mix to more value added products and we're moving more pork into Prepared Foods whenever possible.

While this will lead to higher, more stable margins over time, currently the operating environment for Pork is difficult, leading us to believe our Pork segment operating margin will be around 6% for the year. We expect hog supplies to increase approximately 3% in fiscal 2019, providing a sufficient supply for our plants. Tariffs and trade concerns could continue to affect product pricing. Based on the current market environment, we expect an operating margin of around 6% for the Pork segment next fiscal year.

The Chicken segment generated operating income of \$196 million in the third quarter, with a 6.6% operating margin. Revenue increased on 3.7% average higher price, while volume remained relatively flat. The segment benefited from \$25 million in Financial Fitness savings in the quarter. Chicken segment results were challenged by soft demand due to relatively low priced competing proteins. Additionally, Chicken experienced export headwinds, increased freight, labor, and feed costs, and \$20 million in non-recurring charges.

We're focused on growth, innovation, value-added capabilities, and customer partnerships, which is why over the long term our Chicken segment has demonstrated higher margins and more stability. Currently, however, results will remain challenged, as customers shift from chicken to relatively lower priced beef and pork. As a result, we expect an operating margin of around 8% in fiscal 2018 and similar results in 2019.

Our Prepared Foods segment performed well in Q3 and is building momentum with \$249 million in operating income and an 11.7% margin. Revenue increased with average price up 6.8%, while acquisitions drove the 2.7% volume increase. We're growing sales dollars across nearly all major categories and leading in competitive categories. The strong top and bottom line improvement is attributed to acquisitions, investments to drive volume, positive net price recovery, and \$39 million in Financial Fitness savings.

Operating income was also affected by higher input and freight costs. With Prepared Foods momentum continuing into the fourth quarter and fiscal 2019, we expect the segment's operating margin to exceed 11% in fiscal 2018, with similar results next year.

Before we go back to Tom for his views on our distribution channels and M&A activity, I'd like to offer some thoughts on fiscal 2018 and 2019. Our capital allocation priorities will continue to focus on driving shareholder value and growing the business. We will be disciplined as we pay down debt and deploy cash to grow our business organically and through acquisitions. And we'll continue to return cash to shareholders through share buybacks and dividend growth.

In fiscal 2019, we expect top line sales of approximately \$42 billion, which would be around 3% growth over the \$40 billion to \$41 billion expected in fiscal 2018. Net interest expense should approximate \$345 million in fiscal 2018 and 2019. Our effective tax rate is expected to be around 24% in fiscal 2018 and 2019. We're planning approximately \$1.2 billion to \$1.3 billion in CapEx in fiscal 2018 and approximately \$1.6 billion in fiscal 2019, as we focus on growing and improving our business.

Based on our average share price in Q3, we expect our average diluted shares to be around 368 million before any share repurchases. We plan to continue growing volume while stripping out costs, generating cash, and providing good returns on capital expenditures. And we have the balance sheet flexibility to drive growth.

That concludes my remarks. Now back to Tom.

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

Okay. Thanks, Stewart. Our retail Core 9 outpaced total food and beverage volume, though it did decline slightly. Total Tyson retail declined 1.3%, while volume tipped negative, dollar performance was positive, pricing that was intentionally moved ahead of our peers, was the primary driver of the volume decline.

Within the Core 9, volume softness was driven by two specific retail categories, hot dogs and poultry. In hot dogs, we executed our profit improvement plan that saw expected volume declines driven by strategic pricing. Share declines were based on more aggressive competitive pricing during the Memorial Day period, but more recent share performance has been improving.

In retail value-added poultry, volume declines were also driven by more aggressive competitive activity during what is traditionally the slowest quarter for this category. Our focus in the back half of the year has been on winning the strategic back-to-school season, and it's already off to a strong start. Other retail poultry volume challenges were driven by a declining frozen raw poultry category, as consumers continue to move to fresh poultry.

In the retail channel, innovation is important and we have introduced several new products focused on convenience. In their early days of the market, Jimmy Dean Protein Packs and Jimmy Dean Egg'wiches are doing well with consumers. Refrigerated Ball Park cooked burgers that are sold next to our Ball Park hot dogs are also doing well. For the in-store deli, we have a new pulled white meat rotisserie chicken product that's a labor saver for customers. In addition, continuing innovation in the dynamic meal kits sector is showing high consumer appeal on a more convenient Tyson Tastemakers item called the One-Pan Dish.

In foodservice channel, labor remains a challenge for operators and Tyson Foodservice offers solutions to help free up back of the house labor and improve efficiency with cost effective products. Our Focus 6 products in foodservice distribution continue their positive volume trend, up 2.9% over last year. Our growth relative to our competitors has changed as we lapped strong performance period and our competitors lapped a period of decline.

As the QSR burger wars heated up this summer, we saw fewer limited time offers promoting chicken, which had a temporary impact on our sales growth. Relatively low beef prices and a public focus on burgers among QSR competitors led to some customers making late changes to the promotional schedules and opting to feature burgers rather than chicken. We're looking forward to the foodservice back-to-school season, when we expect chicken will return to playing a bigger role with key customers.

Finally I'd like to talk a bit about M&A. We're refining and growing our company as part of our strategic plan to sustainably feed the world with the fastest growing protein brands. As we focused on protein, we sold several non-protein businesses this year and anticipate selling our pizza crust business in the fourth quarter.

The acquisitions we've made are changing our company in a positive way, and AdvancePierre Foods is a great example. The integration has gone extremely well and APF has contributed an incremental \$1.6 billion in revenue in its first full year as a part of Tyson. Together we've unlocked savings and created new opportunities with customers and consumers.

In May, we announced our plan to acquire American Proteins, which should provide additional stability to our Chicken margins. We received regulatory approval and expect to close this month. In June, we acquired Tecumseh Poultry, producer of the Smart Chicken brand. This acquisition gives us a well-known brand of organic chicken with national distribution and the ability to scale up in this fast growing category.

So as we wrap up our prepared remarks, I'd like to reinforce the rock solid foundation of this business. Tyson Foods is an advantaged leader in the pure growth market of protein. A unique model allows us to activate deep insight and great brands to go all-in on the upside of value added growth. A balanced presence in the major protein stabilizes our positions across commodity markets. This model has consistently grown our operating cash flow and we've taken advantage of the options that creates through prudent capital allocation on the behalf of our shareholders. We will embrace the reality of today, while simultaneously innovating for tomorrow. Our steadfast commitment to a long game ensures we'll continue to generate returns over time.

That concludes our prepared remarks. And, Denise, we're ready to begin the Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you, Mr. Hayes. [Operator Instructions] And your first question will be from Ken Zaslow of Bank of Montreal. Please go ahead.

Ken Zaslow

Analyst, BMO Capital Markets (United States)

Q

Hi. Good morning everyone.

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

Good morning, Ken.

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Good morning, Ken.

Ken Zaslow

Analyst, BMO Capital Markets (United States)

Q

So my question is what is driving 4Q to such depressed levels? But more importantly, how does it change to get to 2019 numbers? Are you being overly conservative, as you pass through the freight costs, you see the hog curve, you get more synergies? Can you talk about that and frame it a little bit? Because it just seems like there's a little bit of a disconnect.

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

Certainly. The biggest disappointment, as I said in my prepared remarks, is relates to our businesses, Chicken we can talk certainly more about that, but why don't I tackle 2019 and maybe, Stewart, I'll kick Chicken margins to you. The 2019 environment is going to be very similar to what we faced here, but I see certainly the protein growing throughout the world. One of the things that we're very focused on is continuing to take advantage of exports where we can. The tariff and trade noise has impeded that a bit, particularly as it relates to Mexico, but we feel like we're in good shape.

Prepared Foods segment and Beef, obviously, are doing very well and continue to see that into the future. So our challenges really come down to Pork and Chicken. Pork is off to a bit of a slow start, but improving. And we see livestock supply will be plentiful. So we need the exports to come through and that's the one thing we need to make sure that happens in order for us to really maximize the model.

Demand in Chicken is soft. There is competing proteins at those low prices I spoke of. And we are concerned about the ability for us to continue to drive that demand up and we want to make sure that our team is focused on doing that. But that's probably the area where we are a bit cautious. We just want to make sure we deliver those results and do it with confidence.

The value-added businesses are expected to continue in a growth trajectory. Prepared Foods and Chicken will benefit from a higher value-added mix and we're happy with the mix improvement. And we expect to continue to

have the Financial Fitness savings come through, of course. So, yeah, few headwinds as we go into the year. Yes, are affecting us now, but continued higher freight cost, food inflation, all those we're used to dealing with those issues. Getting the freight costs and prices pass-through certainly affecting volume, but we're conservative. By your comments, Ken, that's the reason why is we have some issues to tackle and we're all about tackling. Talk about Chicken.

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Yeah. Maybe just a couple of thoughts on both of those, Ken. First of all, Q4, I mean, as Tom's mentioned, some of trends we saw in Q3 Chicken and Pork, we expect those to continue to Q4. And so if look at the relative performance of our Q3 to last year, and I think you'd see the same thing in Q4. On the businesses that are performing well, Prepared Foods we feel great about it. The business I just point you to is Beef as you look at Q4. We've given 8% return on sales for Q3 and we're giving you 6% guidance for the full year. So while we expect Q4 to be really good for Beef, perhaps not as powerful as Q3, right? So, I mean, I think that'll allow you to dimensionalize Q4.

On 2019, we've given you the guidance on all the return on sales. One of the drivers that you'll see in Chicken specifically is the forward curve on grains and the forward curve on grains points to higher chicken prices for next year, and that's flowing into some of that estimate. So depending on how that moves around, our own numbers will move around. Specifically in Q4 also we expect to see higher grain prices flowing through on Chicken. So, hopefully that helps you with some of the detail.

Ken Zaslou

Analyst, BMO Capital Markets (United States)

Q

Very helpful. And just my follow-up is, you guys have a lot of cash coming in. And I remember that you did say that there was an opportunity for you to think about buying back stock. This seems to be a good time to buy back stock. Any follow-up thoughts on that? And then I'll leave it there. Thank you.

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Well, I mean, I'd just say – Ken, thanks for the heads up on that. We have got a great record of buying back stock. I mean, we bought \$120 million in last quarter, almost \$370 million year-to-date; in the last three years \$3.3 billion of the shares. I think you can expect to see us that our – we'll continue to pull the various levers of capital allocation and stock buyback will be part of that. I want to speak to the specific quarter, of course.

Ken Zaslou

Analyst, BMO Capital Markets (United States)

Q

Thank you.

Operator: The next question will be from Adam Samuelson of Goldman Sachs. Please go ahead.

Adam Samuelson

Analyst, Goldman Sachs & Co. LLC

Q

Yes, thank you. Good morning, everyone. I guess, my first question, I wanted to dig a little bit deeper on the Chicken business, thinking about some of – just the year-on-year declines that you're seeing in profitability and margins in the third quarter and fourth quarter. And maybe if you can bracket those a little bit by feed costs, labor,

freight, grow-out expense, and there were some derivative losses, and then mix. And I think one of the things that a lot of people have looked at your company over time has been kind of the diversity across business segments in Chicken between small bird and tray pack and prepared and the impact of buy versus grow and thinking that in the current environment there would have been more of an offset. So any way to dimensionalize some of those pieces will be helpful.

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

Sure, Adam, I'll give you some headlines and I'll talk about buy versus grow. I think the three main categories to think of in terms of the Chicken results are the weak domestic demand, the one-time events that we called out, and then short-term headwinds that certainly are competitive factors for us. On the weak domestic demand, the LTO shifts had a significant impact for us in the quarter, protein switching. The export uncertainty didn't help our leg quarters, for sure. Estimate that most of that deviation in that area is hopefully behind us, but this is something that is affecting us.

I would say, the weak demand and the export uncertainty, about 200 basis points, maybe about \$0.10 EPS. The one-time events, the fire and the shift in production capability at one of our plants, which is a good thing for us long term, did have some effect, as well as the mark-to-market reval when we talk about grains. Total, that's about \$0.10 EPS, I'd say. And then the short-term headwinds, that will increase. Certainly we will see those as it pertains to Chicken being competing with other proteins, so we see the value of the proteins in Beef and Pork certainly coming down, that's going to be a headwind.

Buy versus grow, it's a benefit for sure and it is ongoing, a long-term benefit. But we expected more from this past quarter. We had unusual occurrence this summer with the weakness in demand caused by cheaper Pork and the LTOs I talked about. And so, our Chicken volume dropped enough, where we didn't have to buy as nearly as much as we normally do, so we couldn't take advantage of those low priced products. And that prevented us from fully capitalizing on the market. So that's the story on those two.

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Yeah. The only thing I'd add is just to say, if you looked at Q3, about 60% or so is driven by feed and logistic costs. So that gives you a sense of impact to those, it might be helpful.

Adam Samuelson

Analyst, Goldman Sachs & Co. LLC

Q

Okay. That's helpful color. And then just on the Pork segment, just to be clear on the guidance, 8% year-to-date on margins to get to 6% for the full fiscal year, it would imply the fiscal fourth quarter to be near breakeven. And, I mean, I know packer margins are weak right now. I wouldn't have expected that magnitude of weakness. And you talked about – is it just the export issues with Mexico or on the tariffs beginning in July or something else?

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

Yeah. Certainly the margins are tight right now. We don't expect to be exacting on our forecast. One of the things that you can appreciate is that there is a lot of volatility right now. So it's why we have such a wide range as it relates to the full year performance. What we have seen, as we don't have trouble getting the hogs, more hogs are coming to the market. But the supply, for sure, there has been an imbalance with demand. And so we want to

make sure that that shores up and we have full confidence that in 2019 it will, based on what we know today. But right now we're certainly making sure that we give you the number we think we can hit.

Adam Samuelson

Analyst, Goldman Sachs & Co. LLC

Okay. I appreciate the color. I'll pass it on.

Q

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

Yeah.

A

Operator: The next question will be from Alexia Howard of Bernstein. Please go ahead.

Alexia Jane Howard

Analyst, Sanford C. Bernstein & Co. LLC

Good morning, everyone.

Q

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

Hi Alexia.

A

Alexia Jane Howard

Analyst, Sanford C. Bernstein & Co. LLC

Hi. Can I ask about the outlook for the margins on the Prepared Foods business for next year? If you're maintaining it at the 11% level, despite the cost saving programs coming through, is the idea that you're going to be spending an awful lot more on marketing or is there some other offset that I'm missing? And then I have a follow-up.

Q

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

Yeah. So the margins that we have in Prepared Foods, we are happy with where we are, but we want to continue to make sure that we are continuing to invest. We will make sure that our MAP spending is hitting the right levels in order to keep the growth. As you saw in the hot dog category, we had lost some shares. Although we did improve the margins, our intention is to make sure that we are continuing to get behind our brands. And so there will be a bit of that MAP spending. But also innovation efforts are paying back. We're in right categories, right part of the store. But we are continuing to focus on MAP, and that's a short answer.

A

Alexia Jane Howard

Analyst, Sanford C. Bernstein & Co. LLC

Great. And then as the follow-up, in terms of your acquisition strategy, you've, obviously, done the AdvancePierre acquisition relatively recently. Do you have big appetite to do more in the not too distant future? What kind of assets are you looking for right now? And what's the highest leverage you've been prepared to take on to do another deal? Thank you. And I'll pass it on.

Q

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

Yeah. So I'll talk about the same filters as it relates to acquisitions. Stewart, maybe talk about our leverage. So we are focused on the same areas, are they assets that are going to bring brands, new capabilities, or new geographies to Tyson? And to the extent that they deliver some scale, so we can take some synergies that puts us in a really strong position. So those are the filters that we use without, of course, talking about specific properties. We will be acquisitive where we believe it's going to be in the best interests of our share owners and it's focused on continuing to try to stabilize margins, improve margins over time. And that's what we've done with APF, that's what we're doing with American Proteins, and that's the strategy we're taking. Talk about leverage.

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Yeah. Relative to leverage, I would say there's not a specific number that we'd be willing to go to. It is sufficient, I think, to say that it will depend a little bit on the type of asset, number one. And number two, just to note that being investment-grade is important to us, and so we've worked closely with the rating agencies.

Alexia Jane Howard

Analyst, Sanford C. Bernstein & Co. LLC

Q

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

Operator: The next question will be from Farha Aslam of Stephens Inc. Please go ahead.

Farha Aslam

Analyst, Stephens, Inc.

Q

Hi. Good morning.

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

Good morning.

Farha Aslam

Analyst, Stephens, Inc.

Q

My first question relates to Prepared Foods. I think 2019 is when your pizza toppings plant really comes on and starts delivering the benefits of the restructuring. Could you share with us color on where we are with that pizza topping plant?

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

Sure. Things are looking good. We have the plant. It's up and running. And the volumes are returning back to normal levels. We're making great headway. It's much more automated than the process we have. We look at the product quality, most importantly in the right place that we want it. And so we're locking in some volume commitments for our comeback and things are looking good.

Farha Aslam

Analyst, Stephens, Inc.

Q

And so do you expect to get the \$100 million or so benefit from that revamped pizza strategy?

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

We haven't broken out exactly what the margin improvement's going to be, Farha. But, suffice to say ,it's baked into our guidance or projections as it relates to the margins for F 2019.

Farha Aslam

Analyst, Stephens, Inc.

Q

Okay. And then just as a quick follow-up. That CapEx expenditure for next year, \$1.6 billion, it's a pretty material step-up. Could you provide color on what incremental projects you're going to be pursuing next year with that or break down that \$1.6 billion?

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Yeah. I mean, what you're seeing there is the carry-through mostly from this year. There are a number of large projects too I would point to that are noteworthy. One is the new chicken plant in Humboldt, Tennessee. That's a very large plant. A lot of their expenditure will land in this year, so all in one big project. The other one is a project we have underway to redo our distribution network, and those are some pretty heavy investments which have a powerful payback and are important as we move forward.

Farha Aslam

Analyst, Stephens, Inc.

Q

And those savings are captured in your kind of \$600 million Financial Fitness, or would that be incremental?

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Some of the savings – yeah, they're – well, they're captured either in our Financial Fitness or in our total forecast. So I wouldn't add that to the top of any of the guidance that I've given you.

Farha Aslam

Analyst, Stephens, Inc.

Q

Right. Thank you for the added color.

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

You're welcome.

Operator: The next question will be from Ken Goldman of JPMorgan. Please go ahead.

Kenneth B. Goldman

Analyst, JPMorgan Securities LLC

Q

Hi. Good morning.

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

Hi, Ken.

A

Kenneth B. Goldman

Analyst, JPMorgan Securities LLC

Tom, I know you don't have your long-term guidance for each segment anymore, so I'm not going to press on the specific numbers. But there was a time not that long ago when you were sort of saying, well, maybe 12% to 14% long term is in the cards, maybe we should be thinking about that. Not to put words in your mouth, but that was the range that we were thinking about. But now we seem to have the need for a little bit higher marketing spending than what we had in the past, and this is not uncommon. A lot of packaged food companies are talking about that. I'm just curious, is that 12% to 14% that some people still have in their mind as a reasonable range, is that still reasonable or does it cost more now to get the kind of sales you once needed?

Q

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

You're not putting words in my mouth, because I actually did say it. And it is a longer term view that we have for the potential of the Prepared Foods business as we continue to do the things that we have been doing, which is invest in the business, make smart acquisitions, and continue to execute the plan that Sally and the team has in place. What I've also said is that we aren't going to move margins up, and then not grow the business. So we want to continue to grow EBIT in the Prepared Foods business.

A

So if there is a time in which we need to invest in MAP, we need to amp it up or we need to pull back in some other areas, that is going to be certainly a lever that we'll use. So that is exactly where we think the business can head, but it's going to continue to grow. And I don't want to sacrifice having a 12% or 13% margin, but having a business going backwards in terms of total EBIT, because we're pushing too hard for the margin specifically.

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

Yeah. I would just add on top of that, Tom, to say that really we're focused on what's the best return for our shareholders, right? And so Tom's exactly right, we could push margins even higher. The question is, is that on a growing bottom line and is that delivering more earnings against our capital base? And I think that's the last point that I'd really leave you with, which is our focus is driving the highest earnings against our capital base.

A

Kenneth B. Goldman

Analyst, JPMorgan Securities LLC

Thank you for that. And then my follow-up, Stewart, I thought I heard you say the forward curve on grains points to higher chicken prices. Was that specifically on the small birds where you're at least partially cost plus? I just wanted to get a sense of what that statement meant for the whole company.

Q

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

Yeah. So the question that there to come from Ken was, gee, what's driving the dynamic in 2019? And my answer was that one of those dynamics is higher grain costs. I wasn't pointing to the impact of pricing on birds. Just simply to say that if you looked at grain costs next year as compared to this year, when you look at the forward price curve, they're higher. And so we, obviously, need to consider that higher cost as we give you guidance.

A

Kenneth B. Goldman
Analyst, JPMorgan Securities LLC

Q

Great. Thanks so much.

Operator: The next question will be from Robert Moskow of Credit Suisse. Please go ahead.

Robert Moskow
Analyst, Credit Suisse Securities (USA) LLC

Q

Hi. Thank you. A couple of questions. For fiscal 2018, I think you're saying raw materials flat for Prepared Foods compared to 2017. But for fiscal 2019, there is no guidance yet for raw materials. And I was just thinking with all this excess supply of pork and maybe some beef, could you foresee that being deflationary and positive to margins for fiscal 2019? Have you incorporated any thoughts into your margin guidance for 2019 there? And then I have a follow-up.

Stewart F. Glendinning
Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Yeah. So I would say that there are lot of moving pieces here, some of which we don't want to break out at their lowest level. That's the reason why we give you the margin guidance. We've incorporated all the factors, including the raw material costs, and we think that's a simpler and a good way for us to get that message across.

Robert Moskow
Analyst, Credit Suisse Securities (USA) LLC

Q

Okay. So you don't want to get into the specifics yet?

Stewart F. Glendinning
Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Yeah, I don't want to really break that apart, one, because I think there is lot of moving pieces; and two, I think there's a competitive sensitivity to talking about some of the specifics.

Robert Moskow
Analyst, Credit Suisse Securities (USA) LLC

Q

Okay. A different question. In chicken value-added business, I thought I saw a lot more announcements coming of new capacity being added by competitors, and I even thought I heard of one of your competitors picking up some tray pack business at Tyson's expense. When you're talking about the demand kind of disappointment in the quarter, did any of that come from competitive intensity? And also, are you keeping track of all these capacity additions and how do you feel it compares to demand, given that demand has been kind of soft?

Thomas P. Hayes
President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

Absolutely we are keeping track well of the capacity expansion, and that's – for us we're focused on our supply against our demand. And we do certainly win some battles and lose some battles in the marketplace. But the focus is on the long haul what kind of capacity do we need, not just in value-added, but also through fresh tray pack and the other businesses that we are trying to drive. So the way to think about our capacity expansions for Tyson, what are we going to need down the road, what about two and three years out? That's the way that we

look at it. But, yeah, this is a competitive business and, of course, there's going to be some areas that we will sometimes lose, but most of the time we win.

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Yeah. The only thing I'd say on top, Tom, is that we were expecting – when we say it's weak demand, I mean, our volume was flat, right? So it wasn't a bad outcome. It was weaker than we were expecting. We expected to see volumes up, and so it's all a matter of where you start from.

Robert Moskow

Analyst, Credit Suisse Securities (USA) LLC

Q

Okay. So, no change to your capacity expansion timing?

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

No change.

Robert Moskow

Analyst, Credit Suisse Securities (USA) LLC

Q

Okay. Thank you.

Operator: The next question will be from Michael Piken of Cleveland Research. Please go ahead.

Michael Leith Piken

Analyst, Cleveland Research Co. LLC

Q

Yeah, hi. I was just wondering if you could talk a little bit about the dynamics between small bird, tray pack, and obviously, we've seen a lot of the big bird softness. But how much of the softness in – maybe recent softness in tray pack is due to weakness in big bird and just how the various segments kind of play off each other?

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

Yeah. So certainly the big bird components, as we talk about or I talked about, when we go into a time in which it's countered to how it's been in the past, where those supplies are coming down and we can't take advantage of it, that does hurt our buy versus grow model in terms of having the ability to maximize the potential.

In terms of the other elements, we feel pretty good about the mix of our business, although we'd always want it to be absolutely as we planned. As Stewart called out, we have big plans and we want to make sure we hit those. But I can't give you probably, Michael, the color that you want in terms of all the individual pieces. We don't do that or haven't done it for competitive purposes and won't break that out specifically.

Michael Leith Piken

Analyst, Cleveland Research Co. LLC

Q

Okay. I guess then maybe let me try to swing at this one more way, though. It seems like your Chicken business probably has more value-added components between AdvancePierre, your recent acquisitions. And, I guess, just even if you don't want to break out the various segments – their percentage of that Chicken business, that's

commodity versus value-add that you could break out without kind of segmenting tray pack versus small birds versus other things or...

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

Well, one of the things we talked about is what we plan for ongoing is trying to make sure that the margins are stable and growing. So we continue to believe that we have advantaged model, where in markets where potentially the margins are high and we probably won't be as high as some of our competitors, and certainly when they're lower, we won't be as low. And we sort of refer to that internally as stabilizing our margins. That doesn't mean we're not immune to conditions of the competitive marketplace. So our mix is good. We are hitting the lows in the industry right now and we aren't necessarily going down to that level. But as you've seen in the highs, we don't go all the way up as well.

We do have some level of insulation in our business and our brands. If we talk about value added, that is a clear focus for the team is to continue to build that and continue to drive the Tyson brand and more innovation. And I feel strong about the innovation plan that we have, I like the success. But certainly when you have conditions like this, it puts pressure on the model.

Michael Leith Piken

Analyst, Cleveland Research Co. LLC

Q

Okay. Thank you very much.

Operator: The next question will be from Heather Jones of The Vertical Group. Please go ahead.

Heather Jones

Analyst, The Vertical Trading Group LLC

Q

Good morning. Just want to clarify something you said earlier. Did I understand you correctly when you were saying that some of the short-term challenges in Chicken, specifically the fire, things like that, et cetera, were going to abate, but you expected the pressure related to demand to accelerate into Q4?

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Well, I think, obviously, pressure from the fire, given that it was a onetime event, certainly that will be better, because we don't expect to have it again. But just in terms of demand for Q4, I'd point you to the USDA numbers, which do show an increase for Q4. We're not speaking specifically to our demand in the fourth quarter.

Heather Jones

Analyst, The Vertical Trading Group LLC

Q

Okay, okay. But...

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Sorry, let me just be clear against what I said earlier. The way in which you should think about Q4 is the following. That the trends you saw in Q3 in the Chicken business you should expect to see continue into Q4. That's probably the easiest way to just think through it.

Heather Jones

Analyst, The Vertical Trading Group LLC

Q

And given your 8% rough guidance for 2019, you're assuming that continues then to 2019 as well?

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

That's correct.

Heather Jones

Analyst, The Vertical Trading Group LLC

Q

Okay. And then on the Pork side, I don't want to beat a dead horse and all, but like when I look at the figures out there and a lot of your plants are in the Western Corn Belt. And if you look at the spread there, I mean, it's way better than it was in your late Q3, and actually up year-on-year. So I'm just trying to get a sense of, is this just conservatism on your part to make sure that you make the guidance, or are you more exposed to export markets, like Mexico, that maybe I understood? Just trying to get a sense of why we're seeing such an improvement in the markets, but your guidance actually implies a much worse Q4 than Q3.

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Well, let's go through a couple of things. So, first of all, again, I go back to the point that I expect some of the trends to continue in our business from Q3 into Q4 relative to Pork and Chicken. When you take the Q4 specifically, I go back to the answer I gave earlier, which is to say that the Q3 margins in Beef were 8% and our full year are 6%. And so the only way the math works there is the Beef is that – is expected to be strong in Q4, but not as strong as Q3. And that's the easier one to overlook just because of the size of Beef.

Heather Jones

Analyst, The Vertical Trading Group LLC

Q

My question was on Pork. I'm...

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Oh specifically on pork?

Heather Jones

Analyst, The Vertical Trading Group LLC

Q

Specifically on Pork, because on pork market specifically there has been a really, really dramatic improvement in the last few weeks. But [ph] yeah, you alls (00:45:56) guidance is for it to get materially worse. And I'm just trying to figure out is that just you all being conservative or is there some other factor that we can see that will drive that kind of deterioration?

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

I mean, for us, the trends that we are seeing in the market and we have, of course, the benefit of July under our belts already is that we see those trends continuing through Q4. There are some differences, of course, between the various processes in the marketplace. Of course, we are less integrated than others, and so our price may

float around a little bit more. We had expected to see some improvement in Q4 and we do expect to see some improvement in Q4. But relative to last year, we don't expect to get back to the same levels that we saw then.

Heather Jones

Analyst, The Vertical Trading Group LLC

Q

Okay. Thank you so much for the clarity.

Operator: The next question will be from Michael Lavery of Piper Jaffray. Please go ahead.

Michael S. Lavery

Analyst, Piper Jaffray & Co.

Q

Good morning. Thank you. Just sticking with Pork, if you are seeing some of these 3Q trends continuing, how much does a recovery for you depend on improvement in exports and what would be the catalyst for that, if so?

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

Yeah. Certainly exports are huge. Let me talk about Beef and Pork for a minute just to put some perspective there. The value of the cutout was down about 4% in Beef Q3 versus last year. Pork was about 9-ish percent Q3. So that's total for Tyson of about \$600 million lower in Beef revenue and \$400 million lower on Pork revenue. The majority of that is due to the pressure that the issues with Mexico has created.

So for us, in the Pork business and the Beef business, having those markets return to stable, not the uncertainty that exists today, is critically important. So for us that's where we're focused on. We need to have those markets clearly open to us. And by the way, those numbers I gave you are annualized numbers. But the thing that is most concerning is to have all this disruption continue. So exports, absolutely, are a huge part of the equation.

Michael S. Lavery

Analyst, Piper Jaffray & Co.

Q

And just to be clear, your assumption is for improvement or not necessarily? What's in your 2019 guidance number for Pork?

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

We don't have an assumption that they are going to improve. It's kind of the steady-state that we have today, because we just don't know. It's hard to predict. If you have an answer on that one, I'm happy to hear it. But for us, as it relates to trade and tariffs, it's an open debate and we expect it's going to stay open for some time.

Michael S. Lavery

Analyst, Piper Jaffray & Co.

Q

And how much opportunity do you see for grain market adjustments or sort of third party country workarounds? Is that something you see evolving? Is that an offset that could help, or is it too early to say or [indiscernible] (00:49:04) how much of a factor could that be?

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

I mean, that is a question actually that would be very, very difficult for us to answer. This whole tariff scene has just sort of emerged. Various protein producers are trying to wrestle with it, and it would be difficult for us to give you an accurate answer on that.

Michael S. Lavery

Analyst, Piper Jaffray & Co.

Q

Okay. Thank you very much.

Operator: The next question will be from Ben Theurer of Barclays. Please go ahead.

Benjamin M. Theurer

Analyst, Barclays Capital Casa de Bolsa SA de CV

Q

Very good morning and thanks for taking my question. Just wanted to follow-up quickly on Beef and the comments you've put out with the expectations for the upcoming quarter. So if we put it on into context, and if we take a look at the volume change performance, I mean, clearly there seems to be an incremental demand for beef, just because the pricing environment is so attractive and we've seen it in the quarter volume was up almost 3%, but price was down roughly 3%, which brings you to that more or less flattish sales figure.

But if we take a look at that on a year-to-date basis, actually volume is up 3%, prices are up 2%. So to get to your guidance, what you talk about was that weakness into 4Q, right? What are you expecting to see in terms of volume and price on Beef specific in order to actually get to the point that margins are, well, significantly lower on a sequential basis to make up that just 6% plus margin? If you could clarify that would be much appreciated. And then I have a follow-up. Thanks.

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Yeah. Thanks for the question. I think it's a good one. So far we've tried to stay away from giving specific quarterly guidance. And I think that's one of the reasons why we give you that bottom line estimate and some of the sense of what the trends are. But beyond that, I wouldn't want to get in and sort of break out specifically what I see is going to happen in price and volume.

Benjamin M. Theurer

Analyst, Barclays Capital Casa de Bolsa SA de CV

Q

Okay. And the environment into next year then, I mean, assuming basically a similar environment in Beef as for 2018 full year, would you expect the dynamics to continue to be the ones that you have, Beef as a cheaper overall source of protein becoming just more attractive and hence a more conservative outlook on such of the segments, such as Chicken, but definitely a more optimistic outlook on Beef? Is that a fair assumption?

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

We do have an optimistic outlook, Ben. I would say that we have good visibility into 2021. And at this point what we've talked about in our prepared remarks, that's good, because we do see the number of animals that are out there. Going back to the export discussion, we need to make sure that that is a continually open access to those countries absorbing the increased production. Our business is a spread business, and so when the margins will come through and we have the calendar process and we have a good balance. And by the way, we are in the right regions, as we talked about in the past. It's a very good environment. You might feel us be a little bit hesitant,

because we want to make sure that we're giving the right projections for you. But we do like where Beef sits right now and all the way out until 2021.

Benjamin M. Theurer

Analyst, Barclays Capital Casa de Bolsa SA de CV

Okay, perfect. Thanks.

Q

Operator: The next question will be from David Palmer of RBC. Please go ahead.

David Palmer

Analyst, RBC Capital Markets LLC

Thanks. Good morning. Just to follow-up on Chicken. It looks like Tyson's margin gap to the peer processors in that Chicken segment converged margin-wise. In the past, your value-added mix, that small/midsize bird mix were helpful really as we thought versus those peers. You mentioned a couple times in your prepared remarks where you led off with that promotion bias by chains towards burgers lately and that's certainly been the case by couple of the big guys. But, I guess, I'm a little surprised by that being sort of your header as to a reason for the margin decline in Chicken. So could you give us a sense of sort of a ranking of the factors for Chicken? Is that really looming large? And should we think about LTOs from the big chains going forward as a big factor? Thanks.

Q

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

They are a big factor. I mean, as it relates to our forecast, we had those in and they were out. If you think about the burger LTOs, David, those were up 23-ish percent, something like that. Chicken LTOs in foodservice were down 13%. So when you look at the national accounts, it was a huge number. That's, of course, a big part of our business. So it does affect our margins, in that we need to have the right mix around us and we are focused on what we can do to influence that, but for sure, you're right, it is a big impact.

A

David Palmer

Analyst, RBC Capital Markets LLC

And as far as the midsize, small bird margins, just particularly on that side of the business, is that holding up okay? And is that going to be more of essentially a feed cost dynamic going forward?

Q

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

Again, we don't break out our margins by bird size. I get you're coming at it from another angle. But we do like where we're positioned as it relates to our small bird business for sure.

A

David Palmer

Analyst, RBC Capital Markets LLC

Okay. Thank you.

Q

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

You're welcome.

A

Operator: The next question will be from Akshay Jagdale of Jefferies. Please go ahead.

Akshay Jagdale

Analyst, Jefferies LLC

Q

Hey. Good morning. Thanks for taking the questions. I wanted to ask about your value-added strategy, specifically as it relates to Chicken. In the context that the market – your forward multiple has compressed significantly, where now your entire business is being valued like a commodity, right? So in that context, I mean, what you've said so far today is there is both external and internal factors that are driving the margin to come down as much as it has, right? Like the value-added businesses that we follow don't have 30% swings in margins over a quarter and that's what seemed to have happened in the Chicken business.

But I'm in agreement with you guys that your business long term is actually a stable, higher margin business. But can you just put into context how much of the guidance change going from plus 10% to 8% for the full year is external versus internal roughly, right, ballpark just so that we get a sense of how much this is sort of long-term versus short-term. Thank you.

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

We haven't broken it down that way. Stewart's looking at the page here. What I would tell you, Akshay, is that the model is intact, but it's been stressed. It's been stressed by the competitive marketplace. So we will continue to do what we have been doing. And I would say that the changes that we're going to be implementing will be really focused on driving even more value-added growth. We've had a bump in the road, but the model does hold up. So in terms of the breakout...

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Yeah, I mean, I'd just give you a rough sense. I'd say about – relative to the full year change about 35% or 40%, I'd say, is sort of internal factors and the balance is external. That's sort of the rough numbers.

Akshay Jagdale

Analyst, Jefferies LLC

Q

Got it. And just one follow-up again related to demand planning. Obviously, Tom coming from Hillshire, I mean, that was a key competency, area of competency for the company and he's been a hallmark here at Tyson so far. But you're building a new plant, right, during the time when demand curve has moved lower. Can you help us understand what if anything you're changing internally, such that your demand forecasts internally could somewhat project the things that have happened? I know it's difficult, but are you doing anything differently there?

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

A

So we are getting some more technology around this. And I would say, it's not just in Chicken, but we are looking across the entire portfolio, and particularly the more commoditized portions, to understand how we can better predict what some of the performance is going to be. And it is hard, it's the – where they're commoditized, they are. I would say on the customer front, we do need to get somewhat better. And I would say, frankly, we were a bit surprised and that's not something we'd like to be in a position of. The overall, I mean, S&OP process, Sales and Operations Planning process, I would say, is very sound. But there is always things we can be doing better.

For us, the challenge that we have is trying to make sure that the model will stand up through difficult periods, and this is a difficult period for Chicken. And that's where we're going to continue to put the stress on our team is to make sure that we are managing every single detail as tightly as we possibly can. I do feel good that they have it in hand. But if I told you I was pleased with our forecasting in every part of the business, I wouldn't be being honest. And we need to make sure that our forecasting continues to get better.

Akshay Jagdale

Analyst, Jefferies LLC

Q

Thanks a lot. I'll pass it on.

Operator: The next question will be from Jeremy Scott of Mizuho. Please go ahead.

Jeremy Scott

Analyst, Mizuho Securities USA LLC

Q

Thanks. Maybe just a follow-up on that and the relationship on your margins of your value-added products versus the underlying price of the commodity, specifically in Chicken. I think there was an expectation heading into the summer that as prices came under pressure, there would be that insulation both with your value-added, as well as the buy versus grow, which you talked about before. So, I guess, the first question is, is the elasticity of your value-added pricing living up to your expectations? And if it is or isn't, what is the breaking point in breast meat prices, where the marginal cost of your further processing is outpacing the marginal revenue? And then secondly, have we become too reliant on the buy versus grow model with regards to the level of insulation it provides to Tyson when you have such demand destruction as we had this quarter?

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

So, first of all, I don't think we're going to talk to kind of what point we reach marginal profitability, just because I think that's competitively sensitive. We do think that our mix of products is positive, right? I mean, having value-added products gives higher margins. And certainly the kinds of customer relationships that we have also provide some of that stability. But ultimately there's no getting away from the fact that if the – expecting the market to hold a certain amount of volume, and it will ultimately have that volume, because those chickens are coming through. That when there's not as strong a demand, that you're going to see some of the downward pressure on price relative to where you thought you would be. But this is still a good model we have. There's no question about that. I mean, if you looked at our relationship within the competitive U.S. group, you'll frequently find us near the top of the rankings.

Jeremy Scott

Analyst, Mizuho Securities USA LLC

Q

Okay. And just maybe on Chicken for next year, I guess, I was surprised a little bit that you called out margins are going to be the same as this year, considering that you had two accretive potentially acquisitions rolling on your books. Can you give an update there? And on the net \$150 million that you called out, because they roll through different segments, can you help us out with the gross impact of M&A next year?

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

I don't have a number specifically for the gross M&A, because we didn't break out the specific size of those acquisitions. But relative to the total size of Chicken, they're not that big relative to total Chicken, which is why you

don't see moving the average so much. The external factors from – just seeing in the back half of this year are the ones that are going to be the most significant as we work through to next year.

Jeremy Scott

Analyst, Mizuho Securities USA LLC

Q

Okay. And then maybe just lastly on earnings for next year, I appreciate the visibility might be a bit low for now, given the issues on trade. But if we assume every \$1 billion in sales is equivalent to about \$0.25 in earnings, would you be comfortable with the fiscal 2019 number that's at or above \$6.25?

Stewart F. Glendinning

Executive Vice President & Chief Financial Officer, Tyson Foods, Inc.

A

Well, we haven't given any EPS guidance, and I'm not going to speak to that at this point. But I think I've given you the right building blocks so that you can make the right estimates.

Jeremy Scott

Analyst, Mizuho Securities USA LLC

Q

Okay. Thank you.

Operator: And, ladies and gentlemen, this will conclude our question-and-answer session. I would like to hand the conference back over to Mr. Tom Hayes for his closing remarks.

Thomas P. Hayes

President, Chief Executive Officer & Director, Tyson Foods, Inc.

Okay. Thanks, again. Thanks for the questions today. I will say that the fundamentals of our business model haven't changed. We have a diversified portfolio, strong brands. We're set up well for long-term growth. Really appreciate you joining us. And our team keep focus. We're very excited about what 2019 will bring in the way of continued improvement, and we'll talk to you later on this afternoon. Thanks, everybody.

Operator: Thank you. Ladies and gentlemen, the conference has concluded. Thank you for attending today's presentation. At this time, you may disconnect your lines.

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