Q2 2015 Earnings Call

Company Participants

- Andrew Murchie, Chief Executive Officer-Marfrig Beef
- Frank Ravndal, President & Chief Executive Officer
- Marcelo Di Lorenzo, Investor Relations Officer
- Marcos Antonio Molina dos Santos, Chairman
- Martin Secco Arias, Chief Executive Officer
- Ricardo Florence dos Santos, Chief Financial & Administrative Officer, IRO

Other Participants

- Alexander Robarts, Analyst
- Jose J. Yordan, Analyst
- Lauren Torres, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good morning, ladies and gentlemen. At this time, we would like to welcome everyone to Marfrig Global Foods SA Conference Call to present and discuss its results for Second Quarter of 2015. The audio for this conference is being broadcast simultaneously through the Internet in the website marfrig.com.br/ir. In that address, you can also find the slide show presentation available for download.

We inform that all participants will only be able to listen to the conference call during the company's presentation. After the company's remarks are over, there will be a Q&A period. At that time, further instructions will be given.

Before proceeding, let me mention that forward-looking statements are being made under the Safe Harbor of the Securities Litigation Reform Act of 1996. Forward-looking statements are based on the beliefs and assumptions of Marfrig's management and on information currently available to the company.

Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions because they relate to future events and, therefore depend on circumstances that may or may not occur in the future. Investors should understand that general economic conditions, industry conditions, and other operating factors could also affect the future results of Marfrig and could cause results to differ materially from those expressed in such forward-looking statements.

Now, I will turn the conference over to Mr. Martin Secco, Marfrig Global Foods' CEO. Please, Mr. Secco, you may now begin the conference.

Martin Secco Arias {BIO 18098476 <GO>}

Good morning to everybody. First of all, Marcos Molina, our Chairman, is here with us, and he wants to share a message with all of you.

Marcos Antonio Molina dos Santos {BIO 15363967 <GO>}

Good morning to everybody. It's a great satisfaction for me to share with you the result of the second semester of - second quarter of the company.

This result shows our compromise to all in Marfrig, with the best cash generation, the reduction of our debt, and the greater value for our shareholders. In this quarter we show, with the sale of Moy Park, we keep Marfrig more simple and a very good defined strategy, but also with a huge opportunity to grow; with a very high respect for our financial discipline, and this is - reinforce our compromise with the strategy of the growth of the company.

I would like to invite Martin Secco, our CEO to start the conference with you.

Martin Secco Arias {BIO 18098476 <GO>}

Okay. Good morning, everybody. Thanks for staying with us today to share the results of the second quarter. I would like to say that this quarter was marked by many accomplishments for which I like to congratulate and thank all of our employees and teams all over the world for their excellent performance.

This quarter performance shows the first results of our strategy we are implementing at Marfrig, which clearly aims to create value for our shareholders. The Focus to Win a strategy is based on the three key pillars. First pillar, constant pursuit of operation improvement and higher operation cash flow. We have expanded our productivity agenda, which aims to reduce cost and expenses as well as improve efficiency, and which is an integral of our corporate DNA, a continuous exercise. This improvement is clearly visible in our SG&A expenses, for example. You can see the ratio of net revenue decrease if you compare with a SG&A expenses for the same quarter of the last year. Despite this progress, there are many opportunities to tap, and they should be reflected in the next two quarters, including an important optimization of our production capacity at Marfrig Beef.

Over the past few months, we shut down five slaughtering units for a total of 15; in other words, approximately 30% of our capacity in Brazil. This reduction in capacity was achieved without reducing our slaughtering volume. As such, we believe we adjusted our capacity to the current level of the capital supply in Brazil. And now, we're operating our factories in the rate above of 90%. Amongst the other opportunity we are aiming to explore, the synergy between our unit, especially with this opening of the U.S. market and the Chinese market.

The second pillar, adjusting the capital structure and reducing borrowing cost. Although the Moy Park is divested, it is a strategic decision. Given its great focus on the retail market, lower growth potential, and fewer synergy within the other units. It solves our capital structure as it lowers the debt to be more adequate levels along with a significant reduction in exposure to the U.S. dollar.

Once we conclude the sale of Moy Park, we will begin a liability management exercise in order to reduce our gross debt by approximately $1.2 billion and reduced the costs of servicing the remainder. These will increase our free cash flow generation at least in BRL 300 million for the next year.

The third pillar, profitable growth, focusing on that global foodservice industry. With our more adequate capital structure, we will be able to focus on an organic growth opportunity available in Keystone in Asia and also in United States, and to strengthen the Marfrig Beef operation especially by growing export, which now benefit from the weaker Brazilian real and the opening of our new market.

On the slide 2, in the second quarter of 2015, we posted a strong growth in the net revenue and EBTIDA adjusted. Revenue grew 26% over a year, and EBITDA advanced 41%. Overall our operations performed very well, with full positive margin, combined adjusted EBITDA margin at 8.7%. One very important highlight is that the quarter, we will be able to deliver free cash flow of a BRL 136 million, bringing our free cash flow in the first six months of the year to BRL 48 million, which is fully in line with our guidance to the year.

Looking at the individual units, Keystone posted a strong growth driven by Asia and continues growth in our key account. Keystone posted EBITDA of BRL 165 million, up to 65% year-over-year. In U.S. dollar, Keystone EBITDA grew 20%.

Marfrig Beef posted the adjusted EBITDA margin of 9.7%, driven a better sales mix with a great focus on exports and foodservice charge, and by capture the operating efficiency gains, which has yet to reflect to close the slaughtering unit. The prospects for the Brazilian division are positive due to the opening of Chinese that is already working this market properties and the agreement between Brazil and U.S. for the opening of the American market. And last, at the end of June, we divested more BRL 1.5 billion which will enable us to significant reduce of leverage and exposure of the balance sheet through exchange variation.

On a pro forma basis, considering the Moy Park divested, our leverage ratio will be on the (11:31) 3.3 times. Slide 3 shows how our year-to-date result is in line with the guidance that we shared with you at the beginning of the year. Combined net revenue in the first six months was BRL 12.3 billion, approximately half of the upper limit to the target range of BRL 25 million.

Adjusted EBITDA margin in the period was 8.3%, within the guidance range of 8% to 9%. Note, historically our margin are higher on the second half of the year due to the seasonality of our business. CapEx in the first six months were BRL 339 million, 4% above to the target of BRL 350 million. It's just a small variation for the strong impact in the exchange. And our free cash flow in the year-to-date was BRL 48 million, which is in line with a lower limit of the guidance range. It's also important to note that we will revise our 2015 guidance to reflect the effect from the Moy Park divestment after the closing of the transaction, expected at the beginning of the fourth quarter.

I will now turn this call over to Marcelo Di Lorenzo, our Relations Officer.

Marcelo Di Lorenzo {BIO 16117381 <GO>}

Thanks, Martin. Good morning to all. On the slide 4, first I'd like to highlight that the Moy Park operation is being treated as a discontinued operation. And so – but for comparison purposes, we're also showing the financial performance of the Marfrig Group on a combined basis including Moy Park.

As mentioned by Martin, this quarter's results were very good, with strong growth in revenue, which achieved BRL 6.5 billion, up 26% year-over-year. This growth was mainly due to the solid performance of Keystone, the strong increase in average prices at Marfrig Beef, and the impact from the Brazilian real depreciation in our international units.

In the first six months, revenue came to BRL 12.3 billion. The group's gross profit was BRL 752 million, increasing 20% year-on-year. Despite this increase, gross margin contracted 60 basis points from a year earlier, impacted by lower margin at Marfrig Beef, which despite the recovery, and I'll say strong recovery compared to the first quarter, ended the quarter a 140 basis points lower than the same period of last year. The ongoing efforts to capture operating efficiency gains via our strategic plan Focus to Win led to a reduction of a 140 basis points in SG&A expenses as a ratio of net revenues, from 7.2% to 5.8%.

I think the result attests to our efforts in improving the efficiency. As you can see, despite of a sharp depreciation of the Brazilian real and high inflation in Brazil SG&A expenses raised at only a nominal increase of 2%. As a result, the group's EBITDA reached BRL 560 million in the quarter, advancing a strong 41%. Combined EBITDA margin was 8.7%, up significantly from the 7.8% versus with the last year.

With these results, we managed despite a very challenging first quarter to deliver EBITDA margin of 8.2% in the six-month period, which is in line with our guidance range for the year and up 20 basis points on the margin before six months of 2014, resulting in EBITDA growth of 28%.

If you go to slide 5, we're going to present there our results from the continuing operations; in other words, Keystone and Marfrig Beef. The results reflect the solid performance of Keystone and Marfrig Beef as I mentioned before. I'd like to highlight that the Marfrig Group remains a global company even after the Moy Park divestment. 58% of our second quarter sales or BRL 4.7 billion of continuing operations come from international operations and 78% of our revenues are pegged to currencies other than Brazilian real. We continue to operate in 11 countries with 46 units installed across the Americas, Asia, and Oceania; and we continue sending our products to clients in approximately 100 countries.

EBITDA from continuing operations was BRL 450 million in the quarter and BRL 759 million in year-to-date. EBITDA margin from the continuing operations is 8.8% in the second quarter for an EBITDA margin 10 basis points higher than when including Moy Park.

On slide 6, we show how the operation improvements combined with more effect common from the change of variation reduced our loses to only BRL 6 million. This represents a reduction of 99% from first quarter and an 89% reduction from the same period of last year. More importantly, the results have yet to reflect the impact from the Moy Park divestment on our leverage and financial expenses. If we assume annual savings of roughly BRL 300 million in interest expense, without taking into account a potential smaller foreign exchange impact on our reduced exposure to the U.S. dollar in our balance sheet, we'd have posted a solid profit in this period.

I will now hand the call over to Frank Ravndal, CEO of Keystone Foods, who will comment on the results of his unit.

Frank Ravndal {BIO 19230519 <GO>}

Thank you, Marcelo.

Good morning everyone. The second quarter was a strong one for Keystone, despite some market challenges. We grew adjusted EBITDA 20% in U.S. dollars terms and improved adjusted EBITDA margin by 60 basis points over the last year. Significant improvements in commodity input cost in the U.S., continued volume growth in Asia, and double-digit key accounts growth were all key drivers for our success this quarter.

As a U.S.-based international operation, we opted to present Keystone's results this period in U.S. dollars. The results translated into Brazilian reals clearly are even more impressive with the currency's sharp depreciation.

On the top portion of slide 7, you can see that net revenue increased 10% over last year's quarter, rising to BRL 698 million. 25% volume growth in our APMEA Business was a key driver to that growth. Our businesses in China, Thailand, and Korea all posted solid double-digit growth and led our gains in the region.

In the U.S., higher selling prices for beef in the foodservice channel due to higher raw material costs contributed to higher revenues, as is strong performances in the retail include service channels for our key account business in the U.S.

Gross profit for the quarter was $53 million, a 47% increase over last year resulting in a 190 basis point increasing gross margin to 7.6%. There were three key drivers to the improvement in margin. First, lower commodity input costs in the U.S. bolstered our results. Outside meat costs for chicken was lower by 21% per pound and feed cost declined by 14% per ton. Second, we had an unrealized mark-to-market gain on grain hedge contracts of $450,000 compared to last year's unrealized mark-to-market loss of $3 million resulting in a $3.5 million positive swing this year. The 25% volume growth in APMEA also positively contributed to the margin improvement.

Moving down to SG&A, SG&A as a percent of net revenue came in at 2.4%, which is in our normal range. Last year's result included a number of one-time cost savings and adjustments which resulted in a 1.3% ratio. When adjusting for these one-time items, we're in line with last year's quarter on SG&A. All of these factors drove a 20% increase to adjusted EBITDA and our EBITDA margin rose 60 basis points to 7.7%.

On slide 8, you can see the strong volume growth of 25% in APMEA and 7% in the United States. As result, revenue from APMEA, which accounts for 28% of the total was a BRL 198 million. In the U.S., revenue in the quarter reached BRL 500 million. We continue to focus on one of our main strategic pillars which is to grow our Key Accounts business. As you can see, Key Accounts revenue increased 19% from the second quarter of 2014 and reached to $163 million, with double-digit growth in both the U.S. and APMEA.

Now I'd like to pass the call over to Andrew Murchie, CEO of Marfrig Beef Brazil, who will comment on the results of his unit.

Andrew Murchie {BIO 18098471 <GO>}

Thank you, Frank. Good morning to everyone. The second quarter was of a lot of hard work and sharp focus at Marfrig Beef. As you'll see, we have been taking on important measures in our frozen capacity in Brazil. But first let's go over the highlights. The Brazil beef division posted new revenues of BRL 2.6 billion, up 9% from BRL 2.4 billion in the same quarter last year. In the first six months, net revenue was BRL 5 billion advancing 13% year-over-year. In general, this performance is explained by higher average prices due to the various initiatives we have taken to boost our export sales in more profitable channels. Later, I will provide more on this.

In the second quarter, gross profit was BRL 398 million, increasing a slight 2% from BRL 391 million in the same quarter of last year. Gross margin recovered significantly on the previous quarter, but the gross margin of 15.4% was still 110 basis points lower than in the same period last year. This difference of 110 basis points is explained mainly by the high animal cost in Brazil. According to (23:47), the average fair cattle price in Brazil rose 20% this quarter from a year earlier, which was partially offset by the decline in production costs due to the many initiatives implemented at Brazilian production unit sites since under our productivity agenda.

SG&A expenses as a ratio of net revenue in the quarter stood at 7.6% compared to 10% in the same period last year. The significant drop of 240 basis point reflect the ongoing process to better manage expenses and costs launched in the second quarter of last year, part of our Focus to Win project.

This quarter they were BRL 23 million in savings, which are in addition to the BRL 14 million in sales obtained in the first quarter of this year. The company therefore on this are ongoing, and the expectation is to capture additional savings in cost and expenses of between BRL 25 million and BRL 30 million in the second half of the year.

And last, adjusted EBITDA was BRL 250 million, increasing an important 29% from a BRL 193 million from the second quarter of last year. The margin expansion of 160 basis points from 8.1% to 9.7% was driven by revenue growth, reduced industrial cost, and lower SG&A expenses. Year-to-date adjusted EBITDA margin stood at 9.0% expanding 40 basis points year-over-year.

On the next page, we can see that the net revenue from the Brazil operations accounted for 76% of the total. Despite the lower contribution, net revenue from Brazil operations in the quarter came to BRL 2 billion, up 5% year-over-year. The international operations accounted for 24% growing by 22% to BRL 625 million or $204 million.

The period highlights were the local market performance on the international units, which posted growth of 41% year-over-year, and the export by the Brazil operations, which after facing a difficult scenario in the first quarter, posted a recovery in sales volume of 18% year-over-year.

Note that other products lost ground as a percentage of the division revenue, which is due to the fact that we did not process leather but sold raw hide since the end of last quarter. And last, as part of our strategy to grow international sales, export accounted for 48% of our sales.

Let's talk briefly about our strategy for the Brazilian operations. On slide 11 you can see that slaughtering volume at Marfrig Beef in the first six months of the year was statically stable, falling 0.5% when compared to same period last year. The decline is due entirely to the lower cattle slaughtering volume in Brazil, which decreased by 1.1%. Based on the current level of availability of finished cattle, which we expect to remain stable over the coming quarters, we made a strategic decision to adjust our production capacity from this new scenario. Therefore we closed five units in Brazil, which effectively reduced the number of slaughtering plants to 10 and eliminated approximately 29% of authorized operation slaughtering capacity.

This capacity adjustment allowed us to increase our capacity utilization rate, which should over the coming quarters reduce our fixed production costs. Capacity utilization in the quarter stood at 83% of authorized capacity. The objective is to achieve capacity utilization rate above 90% while maintaining current production levels. In line with the footprint adjustment, we are changing our sales mix to focus on more profitable channels. A weaker real, the opening of the Chinese market, and the expectations that the U.S. market will be finally open to Brazilian beef indicate the brighter outlook in terms of profitability for our exports in Brazil.

In the domestic market, we are highly focused on the foodservice and small mid-sized retail channel reducing the sales to distributors which presents low margins.

On slide 12, we can see the initial results of this strategy. The contribution from the foodservice and small retail channels to the domestic revenue of Marfrig Beef in Brazil increased to 35.4% in the second quarter from 32.1% in the same period last year. With this, we were able to increase average prices by 3% from the first quarter from BRL 12.14 to BRL 12.15 while maintaining sales volume at the 70,000 tons. Despite the challenging microeconomical environment in Brazil, we were able to grow our revenues from domestic sales of fresh and processed meat by 1% to BRL 872 million.

Last, on page 13, we can see the result of our stronger focus on export from the Brazil operations. The effectiveness of our commercial strategy helps us to boost our market share in fresh beef to nearly 22% this year. These results demonstrate a consistent market share gain since last year and improvement of 260 basis points over the same period last year. As a result, Brazilian export accounted for 46% of the revenues of Marfrig Beef Brazil compared to 41% in the first quarter of 2015 and second quarter of 2014.

Our export volumes increased 7% over last year and revenue in U.S. dollar did not increase only because prices are still recovering. We believe that the opening of the Chinese and the U.S. market to fresh beef from Brazil will lead to gradual recovering prices in the high currency.

I would like now to hand the call over to Ricardo Florence, our CFO.

Ricardo Florence dos Santos {BIO 20008948 <GO>}

Thank you, Andrew.

Good morning, everyone. Going now to page number 14, in this quarter all figures that are related to Moy Park are already allocated in the cash flow as discontinued operations because of the sale of Moy Park.

The gross debt consolidated decrease to BRL 11.9 billion from BRL 13.4 billion in the previous quarter, already reduced of the Moy Park gross debt and of the exchange variation registered in the period.

Cash and equivalents of the group do – not considering the Moy Park cash was BRL 2.6 billion. And with this, we ended the quarter with a net debt of continued operations BRL 9.4 billion. If we consider the proceeds of the sale transaction with Moy Park, the pro forma net debt of the continued operations falls to BRL 5.6 billion or approximately BRL 1.8 billion with nominal net leverage of 3.8 times.

We expect that the sale transaction is finalized up to the beginning of the fourth quarter and from this point on we will give continuity to order further operations that will reduce the gross debt of the company in more than BRL 1 billion.

Go to now page number 15. We have here our pro forma cash position with the proceeds of the sales operations and the maturity of our prospects. The pro forma cash position is

BRL 6.3 billion, and this is more than enough to cover the short-term debt up to BRL 1 billion. This amount of BRL 2 billion is related mainly to export financing in the next 12 months, and of this amount it's important to stress that we intend to reduce it by BRL 500 million and to keep the proportion of the short term around 15% as compared to the total debt of the company. Our long-term debt is very comfortable, and we do not have any peak of that until 2018.

Going to the page 16, we've here all the ratios of Marfrig. I'd like to emphasize that the pro forma net leverage of 3.8 times translates the transformation of Marfrig's balance sheet after Moy Park sale, and also that you can consider like we've done in all of the recent release of the results, analyzing the second quarter 2015 EBITDA, we'd have then this pro forma index fall into 3.4 times. Why is this very important? Is because the average exchange rate in the quarter 3.07 is much closer to the quarter-end exchange rate of 3.10, which is 16% higher than the one that we had in the last 12 months, BRL 2.69 per $1. That's why we understand that 3.4 times is what actually translates the current net leverage of the company.

The average costs of that – of the continuous operations is 8.2% per year and this is the level that we intent to decrease after given continuity to the liability management operations to be performed up to the end of 2016.

If we go to page number 17, we can see that the free cash flow generation was positive in BRL 136 million. It's important to emphasize that Moy Park is treated as a third party for cash flow generation purposes because of the concept of discontinued operation. Do not considering this effect, the free-cash flow would have been positive by BRL 90 million in the continued operations and by BRL 46 million in the discontinued operation.

We have focused in this quarter in improvement of several working capital accounts, like inventory because of the optimization of industrial plants of Marfrig Beef and also in suppliers because, of increased in the average term in cattle purchases at least 9 days to 10 days and also as consequence of the higher supply in this quarter.

We believe, that we're in the right path to deliver our free cash flow guidance for the total of the year between BRL 100 million and BRL 200 million to this year of 2015.

Now I would like to hand over to Martin again to give the message of the company.

Martin Secco Arias {BIO 18098476 <GO>}

Thank you, Ricardo. And I'll now make my closing remarks. The second quarter was marked by many achievements. We generated strong free cash flow trends for Marfrig Beef Brazil and we signed an agreement to sell Moy Park.

The strategic decision to divest Moy Park leaves Marfrig with a strong focus on food service channel and offers an excellent opportunity to grow and increase both cash flow and shareholder return. This transition, as Ricardo explained to you, reduced Marfrig's net debt, which ended the quarter with a ratio pro forma net EBITDA from a continuous operation of 3.8 times. It's important to know that this effect on the weaker Brazil real have yet to be fully reflect in this rate.

On an annualized basis, leverage will be 3.4, a figure which better reflect at more normalized foreign exchange environment. Cash generation in the quarter confirmed our determination and financial discipline and was the result of our pursuit of operation efficiency gains and better working capital management.

This higher efficient enable Marfrig Beef to pose adjusted EBITDA margin of 9.7%. The result is a combination of a measure adopted to optimize production and improve sales mix, with a great focus on exports and more profitable channels in the domestic market. We believe the second quarter result is only partially reflective of these changes, since many are still in the implementation phase.

The opening up on the quarter to the U.S. and Chinese market, to Brazilian beef to generate a more strong value for our product in the middle term. We already began shipment to the China and I hope our first shipment to the United States market will be before at the end of the year.

Marfrig international operation continue to make a positive contribution on the division with excellent profitable and a strong free cash flow generation. In the quarter, Keystone not only continued to make a significant contribution on the free cash flow, but also post a revenue growth in U.S. dollar of 10% and EBITDA margin of 7.7% up to 60 basis point from the same period of the last year.

The results basically reflect the good performance of Asia, but also were supported by the continued growth in the key account. In line with our focus to win strategy, Keystone continue to post accelerate growth benefit from the reputation on the customer service and execution of excellent in investor operation.

Our priority in Marfrig are expanding the Keystone food service business in Asia and U.S., optimizing our production capacity at Marfrig Brazil, growing the business Brazil and strengthening the capital structure and increasing our free cash flow. We would like to thank you all of you for sharing this time with us, and now we're open for your questions. Thank you very much.

Q&A

Operator

Thank you. Ladies and gentlemen, we'll now begin the question-and-answer session. Our first question comes from Lauren Torres, UBS.

Q - Lauren Torres {BIO 7323680 <GO>}

Yes. Hi, everyone. My question relates to your confidence and achieving your full year free cash flow target. I guess going from negative to positive cash flow, first quarter and second quarter, and thinking about second half. I was hoping you could just talk a little bit about the components of getting to that on BRL 100 million to BRL 200 million guidance. You talked about the benefits of operational gains, and also better working capital.

So could you talk a little bit about that, I mean that the working capital benefits in the second quarter were quite good. I'm curious if those were sustainable and how do you think about reaching that full year target? That would be helpful. Thank you.

A - Ricardo Florence dos Santos {BIO 20008948 <GO>}

Hi, Lauren. Good morning, this is Ricardo speaking. We have had significant improvements also in all the divisions. We have had improvements yearly, in the reduction of the SG&A, better margins here also. In Marfrig Beef we're working with the sustainable supply year term here. We understand that all this they came to stay. In order to do this, it's because of the seasonality, we always have a fourth quarter which tends to be better than the other quarters of the year.

This is why, and we had this in our budget since the beginning of the year, that after first quarter – in that we had the negative forecast in our budget. We were seeing some sequent improvements in the other quarters as well.

This is what I could say, it's fine. I've no crystal ball, but I can say that all the teams here remains very committed and through this improvements in the operational – in operations in all the business units. There's a link it to the financial operations that we've done as well, that have helped it also our cash flow. We will do our best to deliver the free cash flow at the year end.

Q - Lauren Torres {BIO 7323680 <GO>}

Can I ask another follow-up? What typically makes your fourth quarter better than the quarters, what would that benefit be coming from?

A - Ricardo Florence dos Santos {BIO 20008948 <GO>}

Better sales that we are at the end of the quarter, some seasonal products as well. Usually the terms that we have at year end, they translate a positive impact in the cash flow, this is all together. It's a combination of all these effects. Okay.

Q - Lauren Torres {BIO 7323680 <GO>}

Okay. Thank you.

A - Ricardo Florence dos Santos {BIO 20008948 <GO>}

You're welcome.

Operator

Our next question comes from Alex Robarts, Citigroup.

Q - Alexander Robarts {BIO 1499637 <GO>}

Thanks. Hi, everybody. Question relates really to the cost structure. In the Portuguese call, there was a lot of discussions on your progress and effort in Brazil, but Keystone came in with a better cost structure than we were looking for and you talk about the lower feed cost, the lower poultry meat cost that are pretty substantial. Can you tell us a little bit about what's driving or how you're seeing the outlook for this inputs in Keystone. You asked – do you think the double digit year-on-year reductions of these key commodities that kind of tailwind. Do you see it continuing into the second half? And any kind of thought on the cost structure going into 2016 will be helpful? So kind of the question is really focused on the Keystone USA cost structure.

A - Frank Ravndal {BIO 19230519 <GO>}

Thanks, Alex. It's Frank here. I think relative to a couple of those main drivers. First on the commodity input side relative to grain or corn and soybean meal. As I'm sure you are aware. We had a really nice decline through most of the beginning part of the year and then a pretty significant rally in the June timeframe and then that came off quite a bit and then you had a more recent rally over the last week. So a lot of weather concerns entering into the last seven weeks or eight weeks. Frank, the big number coming out today from the USDA report. So what we would look for is really some continued volatility in those markets over the next couple of months, until there some more clear picture of what the harvest looks like. So rather than really having a clear directional signal on what that looks like, we are just anticipating some greater volatility over that period. And clearly, the market is saying and signaling that same thing. And then relative to the meat input costs, some of the factors there – our overall cost structure and really on that margins, we've a couple of things that we're looking at relative to when I mentioned at the beginning comment, some of the market challenges, despite the good quarter performance, we're looking at a lot of different balances.

So we had – for instance, we had some better prices on wings than we'd have anticipated, that help to kind of offset some of the lower leg quarter pricing, that really kind of heard us on the revenue side. We're a net buyer of meat in the market as you know. So as prices have come off a little bit more recently, that's been a benefit rather than really be able to get a sense as to whether that's going to continue, I'd talk about sort of macro SMBs being the markets looking at about 5% increase on the supply side and then still continuing a little bit smaller percentages into 2016 and we're still seeing pretty good demand out there to support that supply, but just sort of how that takes shape over the next few months. We'll have to see. So we haven't really put together a solid budget on what we'd expect from that cost structure going forward.

Q - Alexander Robarts {BIO 1499637 <GO>}

Okay. Fair enough, if we assume though the meat prices – meat input cost for instance poultry stay at current levels likely then would we be able to assume that our third quarter cost relief tailwind can continue in U.S.A. could you say is that a fair statement?

A - Frank Ravndal {BIO 19230519 <GO>}

I think there's a lot of other inputs in there too. So I don't really want to be providing guidance at this point, Alex.

Q - Alexander Robarts {BIO 1499637 <GO>}

Okay. So fair enough. And just the second and last question just relates to the timing issue on the European approval of the Moy Park fair I mean, I guess the summers is now, August is obviously a tough month to get anyone to be anti-trust folks are probably happening we think and you stated at some point after the summer, I mean is that still your thinking as well and should we think about the anti-trust approval of the timing kind of in September, October or might it be something that happens later in the year? Thanks very much.

A - Marcelo Di Lorenzo {BIO 16117381 <GO>}

Alex, Marcelo here. We have our first filing with the anti-trust European Commission done and so that's a process that is well known in terms of time. So the expectation now is that we'll be able to close the transaction in the beginning of the fourth quarter.

Q - Alexander Robarts {BIO 1499637 <GO>}

Okay, got it. Thank you.

Operator

Our next question comes from Jose Yordan Deutsche Bank.

Q - Jose J. Yordan {BIO 1496398 <GO>}

Hi. Good afternoon, everyone. My question was about I mean in the last quarter in the conference call, avian flu was one of the main subjects we talked about, and obviously the situation has come down a bit. But I was just wondering if you could give us an update from the point of view of your business? How that situation continues or not to impact your operations and your sales to some countries in Asia that closed to U.S. imports et cetera? And any idea, you can give us about the potential impact of Yuan devaluation on your business probably some positives and some negative, but just to review in general as to the net impact would be great? Thanks.

A - Frank Ravndal {BIO 19230519 <GO>}

All right. Perfect. Hey. Thanks. It's Frank again. So we've about six weeks about since the last reported case of AI on June 17. So that's positive relative to getting closer to potential market reopening for the U.S. exports, but he somewhere obviously helps and then concern that we in the industry have us around what happens is the cooler four months comment, you have some increasing migratory bird traffic that can help spread that.

So that's the overall situation. So typically, you might see maybe three months between our last reported piece and opening of some of the markets, depending on whether they're really completely economic drivers or maybe there's some political drivers mixed in. So we'll have to see how things progress with the cooler weather coming and whether those markets reopen by the end of the year or not. Relative to the impact, I would say that the nature of our business helps to mitigate that in terms of the reducing our overall exposure. So let's say lower prices on the late quarters from those being just having following the way they have. And we've been able to handle the impact of that lower late quarter pricing pretty well, due to some offsetting positive events like the corn and soybean mill input prices and higher than expected prices like I mentioned earlier and some other parts. And then, we'll continue to look for ways to reduce our exposure to continuing weakness in the late quarter, pricing should export markets remained close to the balance of 2015. We look at maybe greater deboning and also just our pricing arrangements with some customers allow us to have some protection against those pricing.

Relative to keystone, on your second question and then if there is a broader other maverick input relative to that I'll let it open. But relative to keystone and the devaluation of the one over the last couple of days, really not a big impact. We, over time, our bigger concern will be what are the underlying impacts on economic growth in China and underlying demand for protein, but over the last year or so, some of the exports that we did have out of China to Japan slowdown substantially.

Over time, again, that could make it a little more competitive where maybe some of those markets come back to China origin product. Our chicken for instance is locally sourced, so not a big impact there. Our beef is both the mix of imports and local, but in some of the cases, we have the opportunity with different customers to maybe able to have - be able to pass some of that costs through.

Q - Jose J. Yordan {BIO 1496398 <GO>}

Okay, that's very helpful. Thanks.

Operator

This concludes today's question-and-answer session. I would like to invite Mr. Martin Secco to proceed with his closing statements. Please go ahead, sir.

A - Martin Secco Arias {BIO 18098476 <GO>}

Thank you. I would like to thank you again all of you for your time. And we keep in touch in the next day to a more question or analyze about our quarter results. And thanks again and keep in touch.

Operator

Thank you. That does conclude our Marfrig conference call. Thank you very much for your participation and have a nice day.