

Q3 2012 Earnings Call

Company Participants

- Andre Nogueira, CEO
- Jeremiah O'Callaghan, Director
- Unidentified Speaker, Company Representative
- Wesley Batista, President, CEO

Other Participants

- Alan Alanis, Analyst
- Bryan Hunt, Analyst
- Carla Casella, Analyst
- Evam Submerges, Analyst
- Farha Aslam, Analyst
- Jose Yordan, Analyst
- Reza Vahabzadeh, Analyst
- Wesley Brooks, Analyst

Presentation

Operator

Good morning, everyone. Welcome to JBS SA's Conference Call. During this call we will present and analyze the results for the Third Quarter of 2012. (Operator Instructions)

Taking part in this conference call, we have Mr. Wesley Batista, President and CEO of JBS Global Operations; Mr. Don Jackson, CEO of JBS USA; Mr. Andre Nogueira, CEO and like[ph] of JBS USA; Mr. Daniel Semolina[ph], CFO of JBS USA; and Mr. Jerry O'Callaghan, Director of Investor Relations. I would now like to turn the call over to Mr. Jerry O'Callaghan. Please sir, you may now begin.

Jeremiah O'Callaghan

Thank you. Thank you, very much and welcome to our Third Quarter earnings release. We this morning we had our JBS day here in Sao Paulo in Brazil. And so we spoke with the local investors in Portuguese in public. And now we are providing the information for our investors in English, basically the same information that we discussed in public in Portuguese this morning.

We put a presentation on our web page. So I'm going to go through this presentation rather briefly. At the end of the presentation we will talk about the quarterly highlights. But at the beginning we will discuss a little bit about JBS, about the Company and the strategy, a little bit about the dynamics of the market globally. And then finally we will talk about the quarter and results.

So as we go through the presentation I will mention the pages so that those of you who have downloaded the presentation from our site you can follow it page by page. Starting on page three just to remind everybody we are a company that are almost 60 years old, founded in 1953 in West Central Brazil. So we will be celebrating our 60th anniversary next year.

We were the first beef company in South America to go public. We listed the Company on the Sao Paulo Novo Mercado Stock Exchange in March 2007. Since then we've made significant acquisitions and done some significant growth on the international market. And today we are a leading protein company.

Our net revenue for the first nine months of 2012 we talk about the quarter at the end. But for the first nine months accumulated almost BRL54 billion. And we had an EBITDA of BRL3.2 billion and during this period. And I think it's quite relevant to highlight also the fact that independently of the acquisitions that we made or any expansion we did through new facilities in this period we had organic growth in terms of revenue, organic growth of 16% in the first nine months of this year when compared with the first nine months of last year.

So on page four, the rankings, we are the largest beef and lamb producers globally. We're also the largest processors of hides into leather. It's primarily in Brazil, processing more than 80,000 hides per day. And today with our Brazilian chicken operations we're also the largest producer of chicken, of poultry made of chicken in the world. And with our pork operations in the US we are the third largest pork producer in the US.

On page five of our presentation a little bit about each phase in the Company over the last almost ten years, the last seven, eight years. We raised some debt through bond issuances prior to the IPO between 2005 and 2007, basically as working capital. And then with the issuance of equity in 2007 we have grown the acquisitions we have made as primarily through equity while we've got to the debt capital markets to finance our working capital. So we've had that balance and that we've been able to grow without leveraging the Company, overly leveraging the Company in this period.

Between 2008 and 2009 and we made some relevant acquisitions as most of you know. We've been integrating those acquisitions over the last couple of years. So very little M&A activity in 2010/2011 and 2012. And a lot of integration. And now as we move through 2012 we see the results of that with more cash generation, gradually a better balance sheet. And this is basically what our focus is going forward.

Our strategy has been to grow our production capacity in regions around the world which are cost competitive. And so that's why we are in South America, primarily in Brazil. That's why we are in North America, a very cost conscious and efficient production base. That's we were in Australia as well. And we can talk a little bit more about the dynamics of domestic consumption in the next forts[ph] going forward in this presentation.

But on page six we have a little bit more about our strategy, which is more of a focus nowadays in sales and distribution, not only domestically in the markets where we operate, which is relevant. But also in the international market, more value-added products. If you look at the results for this quarter you will see that there has been a substantial increase in the volume of industrialized further processed products that we are producing. And then we have quite a number of regional brands which we are gradually leveraging to use more on top of our further process than our industrialized products.

On page seven of our presentation a little bit about our global reach, basically the message is JBS really looks at consumers as global consumers. So we try to be as close as we possibly can be to those consumers having regional sales offices and distribution centers as broadly as we possibly can with the sensitivity of understanding consumers and providing them products which are customized for each region around the world.

A good portion of our business, particularly for the low-end products that we produce like minced beef, there's a lot of value to be added to those sort of products. So a lot of for instance our patent[ph] burger or patty business is growing quite a lot, also a lot of cooked products, canned

meat items. So that's a big portion of our business and as it's a growing portion of our business. And we have some examples of those products on page eight of our presentation.

On page nine the brands that we have regionally in South America some very, very strong brands like Friboi, like Swift, which is a global brand. But it's very strong regionally in South America. And then we have brands in Argentina, in Uruguay and Paraguay as well. And in North America with our Pilgrim's brand, also our Swift brand in North America. And quite a selection of Australian brands as well.

As from page 11 onwards in our presentation a little bit about the global dynamics of supply and demand of meat and meat products, just to situation where JBS is in relation to where we see market trends going. On page 11 very interesting dynamics in terms of where there was surplus supply, not only of animal protein but of vegetable protein as well. And we see North America, South America and then third place Australia they stand out as regions which have surplus production in relation to their domestic consumption.

And then we look at the Middle East, Africa, Asia and a good portion of Europe, a growing portion of Europe we see a deficit in terms of production and consumption. So obviously that augurs for increased trade between those regions in the world that have a surplus to those regions in the world that have the deficit. And that is basically where JBS is located. And it's within that scenario that we see our business growing and our export business growing.

On page 12 a little bit about global beef production, we see some growth. It's marginal in relation to the other proteins. It's primarily in South America, production growing from about 60 million tons global beef production to about 76 million tons, 76.5 million tons over a 20-year span. And a lot of that and there would be a lot of exports involved in that. And basically we are located in the countries where we see most of that expansion.

On page 13 of our presentation a little bit about the US herd and beef production in the US, a topic which is quite popular over the last couple of years. The USDA and we are forecasting a recovery in the herd in the US. And quite substantial growth between now and 2020. The moment is that the cycle is bottoming out and so we see some calf prices in the US are up quite substantially. We see good dynamics towards a growing herd over the coming ten years.

Page 14 of the presentation a little bit about meat consumption generally. So we've got poultry, pork, lamb and beef. And if we look at how much consumption has grown between the 1960s and projecting it forward to 2013, there is quite substantial growth, quite substantial growth. And where is that growth? As we look at the next decade in terms of where we see demand growth, 81% of all demand growth is going to come from the emerging markets, just 19% from the developed markets. So again that we are located to a great extent in the emerging markets and we have a lot of sales penetration in the emerging markets.

On slide 16 of our presentation just a little bit about what are recommended consumption per capita of meat is, which is about 80 kilos per capita annum. Globally today we are at 42 kilos per capita an annum. So there is a lot of potential consumption growth as income per capita increases in emerging economies and people have more disposable income. They will be looking to eat more meat and we definitely see the average global consumption per capita growing closer to a level which is recommended by the food and agricultural organization, which is 80 kilos per capita annum.

In terms of the largest exporters of meat on slide 17 we just have the major beef exporters, chicken exporters and pork exporters just for us to remember which countries are more relevant. When it comes to beef India has a substantial volume of exports to its neighbors. But it's a specific type of product to a specific region. So from the point of view of competition or from the point of view of the global market it's not very relevant globally.

And the countries that are really relevant is Brazil, Australia, the US, the rest of South America. And Canada is also a substantial exporter. So we see on the chart on page 17 that JBS is inserted in all those countries in Brazil. And Australia. And the US. And the other South American countries and in Canada, more recently in Canada, which are the major exporters of meat product, or beef products.

When it comes to chicken there's a big polarization. It's Brazil and the US, which are the two major exporters. 70% of all chicken exported this year and next year, probably more than 70% is going to originate either in Brazil or in the US. And JBS has relevant operations in both these countries.

And then pork in terms of pork exports the US has been a very robust exporter. And we see some headwinds in terms of costs in Europe, making the US even more competitive on the global market with potential to see US pork exports increasing quite a lot in the coming couple of years.

Now as you get out to the numbers regarding Third Quarter 2012 in page 19 in our presentation, a little bit about net revenue to start with. We had net revenue going from BRL15.6 billion in the Third Quarter of 2011 to BRL19.4 billion in the Third Quarter of this year. That's a 24% increase year-on-year.

We had EBITDA going from BRL787 million to BRL1.38, practically BRL1.38 billion. That's a 75% increase year-on-year. And EBITDA margin going from 5.1% to 7.1%, Third Quarter 2011, Third Quarter 2012.

When it comes to net income the difference is really substantial. Net income in the Third Quarter of 2011 was negative BRL67.5 million and adjusted net income for the Third Quarter of 2012 was close to BRL500 million, BRL495.4 million.

Also we had positive operating cash flow in the period and free cash flow generated of almost BRL160 million. And another point which I think is very important, particularly for the debt market and for the rating agencies, our leverage declined quite substantially from 4.27x down to under 3.7x, 3.68x.

When we look at -- when we compare the nine months, first nine months of 2012 against the first nine months of 2011, the numbers are also quite, quite substantial. And looking at the numbers on page 20 of our presentation net revenue accumulated in the nine months of 2012 almost BRL54 billion against BRL44.9 billion in the same period last year, accumulated EBITDA in the period BRL3.24 billion this year against BRL2.2 billion last year, EBITDA margin for that period of nine months going from 4.9% to 6.0%. And net income of BRL100 million negative in the first nine months of last year to almost BRL1 billion positive the first month reals -- the first nine months of 2012.

Also during recently there were a couple of strategic events on slide page 21. We mentioned those strategic events and I will go through them briefly here. There were three.

Firstly is signature of an agreement to manage and operate assets of XL Foods in Canada with a purchase option on those plants in Canada and also the plants in the US. So this is JBS' first incursion into Canada, the ninth largest global beef producer and the sixth largest global beef exporter.

The -- we also announced recently that we had signed a term sheet to acquire 100% of a Southern Brazilian chicken company called Agroveneto, very much focused on exports in the State of Santa Catarina, a modern facility which will fit in well with our already existing facilities that we operate in the south of Brazil. And then the third strategic event which we announced is we will be opening, phasing in the opening of six different beef production facilities in Brazil in the coming six months,

increasing our processing capacity in Brazil by 1.2 million head of cattle per annum as a result of the opening of these six facilities.

On page 22 of the presentation is consolidated results over the last five months. One can see that how we have progressed over those five months in terms of the five quarters, excuse me, five quarters, over the last five quarters in terms of net revenue growth, in terms of EBITDA growth. And EBITDA margin as well.

Speaking briefly about each one of the business units, South America to start with, JBS Mercosul as we call it, revenues went from BRL3.9 billion to BRL4.6 billion Third Quarter '11 to Third Quarter '12, 3.9 to 4.6, 17.7% revenue increase year-in-year. Total EBITDA increased by almost 47% to BRL665.6 million, also the Third Quarter 2012. And EBITDA margin for the South American business very similar to the Second Quarter at 14.5%.

If we look at our North American business, the beef business in North America including Australia, we had revenue growth of 1.6% year-on-year from \$4.2 billion to \$4.3 billion in quarter -- in Third Quarter '11 to Third Quarter '12, quite substantial EBITDA, \$175.1 million EBITDA with an EBITDA margin of 4.1% in the Third Quarter 2012. So that's quite a recovery from the first half of this year. And we see quite strong performance out of Australia and performance out of Australia also in the period.

Our pork business we had marginal decline in revenues and also in EBITDA. Revenues came in at almost \$850 million for the period with EBITDA just over \$40 million. We believe that that business will see some advantages let's say in the international market in the coming quarters and in the coming year with margin improvement.

Our chicken business we had substantial revenue increase from the Third Quarter 2011 to this last quarter, almost 10%, BRL2.1 billion in revenues with an EBITDA of \$105.6 million in the quarter and an EBITDA margin of 5.1%. We see that business quite strong, regardless of higher main prices.

On page 27 of our presentation a little bit about the global exports very briefly here, a little over \$2.5 billion in exports in the period, \$2.5 billion in exports in three months. The main destinations are the emerging markets as we mentioned earlier, Africa, the Middle East, Mexico, China, Hong Kong, Vietnam, Russia, South Korea. And in between there there's Japan and the European Union. But most of the destinations are to those emerging markets where we see increased per capita income.

A little bit about our debt profile on pages 29 and 30 of our presentation, on page 29 our leverage decreasing from 4.27x to 3.68x, as I mentioned at the beginning. And quite strong liquidity, regardless of the amount of cash available, just over \$5 billion and of reals, excuse me, BRL5 billion available. There was also \$1.2 billion in available lines at JBS USA which are untapped. But 100% available. So that's quite substantial liquidity.

And then our debt maturity schedule and profile is on page 30 with very little debt maturing in the coming quarter and in 2013. And then we have got the breakdown at JBS SA and at the subsidiaries in reals and in US dollars in bonds and in others. I don't need to go through that in detail with all of you.

So just briefly before I hand over to our CEO for his comments, just a little bit about sustainability, which is a subject which always comes up in a lot of our meetings with investors and with stakeholders in general, we wanted to highlight the fact that we are monitoring our suppliers in Brazil in such a manner that which is really groundbreaking. We use satellite imagery to control our suppliers in Brazil and this is a very important aspect for a lot of our customers around the world. This is such that we do in a pioneering manner and we can guarantee the origin of all the product that we process in Brazil.

And then finally just a little bit about our social responsibility and our involvement in the community, here in Sao Paulo in Brazil we are financing through an institute, a learning center, a school which has a capacity for 630 students. We are ramping up every year, 90 more students every year until we reach 630 students. So we have this involvement in the community here in Sao Paulo which is pioneering an initiative of ours. And we've had many of our customers. And of our stakeholders and of our shareholders come and visit us and see this project. And some of them are copying this project in other parts of the world. So it's something we like to highlight with our investors our social responsibility.

With that now I'll hand you over to our CEO, Mr. Batista, for his closing comments before we open for Q&A.

Wesley Batista {BIO 15243148 <GO>}

Thank you, Jerry. So thank you all to participate on our Third Quarter earnings call. Jerry already mentioned all the numbers here.

We are talking about the Third Quarter that we believe we are delivering our satisfied results. We are seeing a good growth, a good organic growth in our top line. So our growth is around 24% year-over-year. That is a substantial growth.

We did a strong -- we are delivering a strong EBITDA on this quarter, almost BRL1.4 billion at 7.1% EBITDA, almost BRL500 million on net income. We are deleveraging our balance sheet. So we were at 4.2x leverage and now we are below 3.7x leverage, actually 3.68x leverage.

So overall we are satisfied and by the quarter. We are looking every day our operation and we will be very focused to run our business to improve our results and should deliver better numbers. We are very focused to deleverage our balance sheet. We want to keep deleveraging our balance sheet and we are very focused on this to generate cash.

So this is the things that we are looking every day and focused to do these points here. We will keep growing our business in Brazil. We are announcing that we are going to open six new processing beef plants these coming months. This we will add like Jerry mentioned 1.2 million head in 2013 on top of the number that we are going to close this year in terms of beef volume.

We are ready to announce that we did the deal in Canada. We believe that the Canada deal -- this transaction in Canada has a lot of synergy and a lot of things that we can benefit from being an operator in Canada and also in the US.

And also we announced expansion in our chicken business in Brazil. We will be very focused to expand -- export in the chicken business in Brazil. We believe that we can operate this business in a very low cost structure and being very focused on export. We believe that this can benefit our results on the chicken operation in Brazil.

It was right you all already know the numbers that it was published the numbers weeks before we are publishing our Third Quarter. Even though the grain market is completely different than the beginning of this year we have been able to deliver results that we believe with this scenario with the grain scenario the reasonable results. And we believe that our team and our structure can handle the Company and can deliver results even with the grain market that is working against to the chicken industry around the world.

So with that I like to open to Q&A. Thank you.

Questions And Answers

Operator

Thank you. (Operator Instructions) Our first question comes from Ms. Farha Aslam from Stephens.

Q - Farha Aslam {BIO 6151888 <GO>}

Good morning.

A - Wesley Batista {BIO 15243148 <GO>}

Hi, Farha.

Q - Farha Aslam {BIO 6151888 <GO>}

My question focuses on beef. And --

A - Wesley Batista {BIO 15243148 <GO>}

Hello?

Q - Farha Aslam {BIO 6151888 <GO>}

Hi. Can you hear me?

A - Wesley Batista {BIO 15243148 <GO>}

We can't hear Farha.

Q - Farha Aslam {BIO 6151888 <GO>}

Hi. Can you hear me now?

Operator

Excuse me. Ms. Aslam, your line is open.

Q - Farha Aslam {BIO 6151888 <GO>}

Hi. Can you hear me? Hello?

A - Wesley Batista {BIO 15243148 <GO>}

Hello.

A - Unidentified Speaker

Hi, Farha.

Q - Farha Aslam {BIO 6151888 <GO>}

Hi. My question focuses on beef. And could you comment on cattle supplies in Brazil given that you're expanding production in Brazil. And also in Canada given your new facility there, as well as the US and some commentary on beef margins in the US here in this Fourth Quarter of the year?

A - Wesley Batista {BIO 15243148 <GO>}

Farha, this is Wesley. So in Brazil we are in a positive cycle in terms of cattle supply. We are seeing more cattle available. The cycle is positive in this regard and we believe we will keep seeing this in these coming years, 2013, '14 and '15.

So we are expanding our beef operation in Brazil. And we of course are looking to gain market share because the cattle supply will not grow in the same magnitude that we are growing our capacity in Brazil. But we believe that we have a very efficient operation and a very competitive operation that can compete and can gain some market share.

In Canada we -- I mentioned we believe that the Canada that operation has a lot of synergy with our operation in the US. Canada ex -- 75% of the Canada export is to US, to the US. So we believe that we can get a lot of synergies being operating this business in Canada with our presence in North America.

About the US we I think as you -- we all know that we are going to see a tight supply in the US in these coming quarters and in these coming years. We will see less cattle available. The industry we will need to work out to adjust supply. And capacity and supply to be able to give margins, to give positive margins. And I think we that we are seeing more balance in terms of supply and demand in this Third Quarter. And we are seeing also in the Fourth Quarter a better balance in terms of supply and demand.

So we -- you all know we had a difficult First Quarter and a difficult Second Quarter for the beef business in North America. But we are delivering in a good Third Quarter and we believe we can deliver a reasonable and good third -- a Fourth Quarter as well.

Q - Farha Aslam {BIO 6151888 <GO>}

Great. Thank you, very much.

A - Wesley Batista {BIO 15243148 <GO>}

Thank you, Farha.

A - Jeremiah O'Callaghan

Thank you.

Operator

Excuse me. Our next question comes from Alan Alanis from JPMorgan.

Q - Alan Alanis {BIO 15998010 <GO>}

Thank you. So much. Hi, everyone. Congratulations on the results.

A - Jeremiah O'Callaghan

Thank you, Alan

Q - Alan Alanis {BIO 15998010 <GO>}

My question has to do with how do you envision your role in the Brazilian poultry sector going forward in the year and then three years from now? That would be my first question.

A - Wesley Batista {BIO 15243148 <GO>}

Alan, with the Frangosul operation and also with this acquisition that we announced last week or the week before last.

A - Unidentified Speaker

Yes.

A - Wesley Batista {BIO 15243148 <GO>}

We intend to grow our presence and our business, our chicken business in Brazil. But we are going to another part of the business that we believe that will be better for JBS at this point. That is export. So we are not going to dispute the domestic market for industrialized products. We believe that the market is already --

A - Unidentified Speaker

Crowded.

A - Wesley Batista {BIO 15243148 <GO>}

-- crowded on this area. So we -- our strategy is to build a chicken operation that is a very low cost structure and a very low cost operation very dedicated to export to the Middle East, to Europe, to Japan. And we are seeing the results running our chicken business in this way. So and this is the way that we intend to expand our chicken business in Brazil, different than the biggest players in this market that have different structure. So this is our strategy going forward, Alan.

Q - Alan Alanis {BIO 15998010 <GO>}

Thank you. Now the and a little bit more into this question, Frangosul is either related to that we -- it would become part of Canada. We can say that these were basically troubled operations. So there were good opportunities for acquiring them because they were struggling. If there were other operations in Brazil or for example for more processed foods that they were to for whatever reason got into trouble, would you consider continuing expanding and going to this idea of doing the acquisitions in an opportunistic way? That would be my next question. And then one last more and then that's it.

A - Wesley Batista {BIO 15243148 <GO>}

Alan, we did show to grow and grew our chicken business in Brazil step-by-step. So we believe that this is the right way to grow. And now our business we announced this acquisition is a small acquisition in terms of capacity or in terms of spending. But we -- our intention is to grow step-by-step, to do -- to grow. And digest and grow again. But we are not looking. Look. Sure we have lived and we have opportunity in Brazil to grow doing regional acquisitions or to expanding our business regionally.

Q - Alan Alanis {BIO 15998010 <GO>}

Got it, okay. And my last question is what's your capacity utilization right now in Brazil in beef? And how will that evolve once you complete this expansion that you're doing? And what do you think can happen to margins of beef once you are -- once you roll out and complete that capacity expansion for 2013 and 2014?

A - Wesley Batista {BIO 15243148 <GO>}

Alan, today we are running -- the plants that we are operating today we are running our business at around 85% capacity utilization. So with these new facilities that we are going to open that is six new processing beef plants that we will add 1.2 million head on top of our volume for 2013. So our capacity in Brazil will go to around 10 million head of cattle for 2013.

In terms of beef and beef margin, Alan, we believe we have a very competitive structure and a very efficient operation in Brazil today. We believe we can handle this growth and keep being delivering good results. Of course I cannot say different that we will be putting more competition in the market.

So when you plan to grow and to grow market share you of course you put some pressure on the market. But we believe that we have a very efficient operation and, look, we will add volume and revenue almost without to add any cost because to handle this 1.2 million head of cattle, more than

the volume that we handle today, we will handle this with the same cost, almost the same cost in terms of SG&A and in terms of a lot of areas that we will not add any costs. So we can be more competitive than we are today. So this is the reason and our plan. And again we are very, very confident that our structure is very efficient in Brazil and we can do this and keep being delivering strong margins.

Q - Alan Alanis {BIO 15998010 <GO>}

Okay. That was very clear. Thank you. So much. And again congrats for the results.

A - Wesley Batista {BIO 15243148 <GO>}

Thank you, Alan.

A - Jeremiah O'Callaghan

Thank you, Alan. Thank you.

Operator

Excuse me. Our next question comes from Mr. Wesley Brooks from Morgan Stanley.

Q - Wesley Brooks {BIO 16407564 <GO>}

Good morning, Jerry, Wesley. How are you doing?

A - Jeremiah O'Callaghan

Good morning.

Q - Wesley Brooks {BIO 16407564 <GO>}

Good. So just coming back to the six plants, can you give us your thoughts on the working capital investment that it's going to take you to get those businesses up and running over the next couple of quarters?

A - Wesley Batista {BIO 15243148 <GO>}

Around BRL150 million.

Q - Wesley Brooks {BIO 16407564 <GO>}

Okay. And then on the Brazilian chicken business, can you give us an idea, just a bit more color sort of around how much the sales were during the quarter. And how the margins were and where you see the Fourth Quarter panning out relative to the Third Quarter both in terms of the sales contribution and the EBITDA contribution and margin please?

A - Wesley Batista {BIO 15243148 <GO>}

So, Wesley, basically and from through today we are running at around BRL120 million in sales every month per month. So that is around BRL1.5 billion in an annualized base.

And we are running Frangosul today in this level at 90% capacity utilization. So probably we will expand a little more the volume in Frangosul. But it is marginal. It is not meaningful. So probably we will see this the revenue going to around BRL140 million in terms of net sales --

A - Unidentified Speaker

Per month.

A - Wesley Batista {BIO 15243148 <GO>}

-- per month. And in terms of margin, Wesley, look we don't disclose at this point a margin on our chicken segment in Brazil. But what I can tell you that in the way that we are organizing our chicken business in Brazil that is very focused on export, very low cost structure, very low spending in terms of marketing or in terms of building brands or this kind of thing that really we are more in the export market for the chicken business in Brazil.

What I can tell you that we are running this business is a very strong margin in the structure. So we are very satisfied by the margin that we are seeing in the chicken business in Brazil. But we are apologize. But we don't disclose the margin.

Q - Wesley Brooks {BIO 16407564 <GO>}

Okay. Excellent, thank you. And if I could ask one more just around the acquisition of XL in Canada, it seems there's been some resistance from the US cattle raises with you buying the whole business and getting the new US capacity as well. What is the status there and how -- do you see some risk to you being able to complete that acquisition when you choose to?

A - Wesley Batista {BIO 15243148 <GO>}

No we -- look. Our legal advisors and we don't believe that we will see an issue on this regard. Of course the Department of Justice in the US and the antitrust department in Canada are reviewing the transaction. But we don't believe that we will have or face any problem, when you see in the US there is only one plant that is operating today. That is the plant in Omaha. And the volume that we will add on our volume and it is not meaningful. So we don't believe and our legal advisors also don't believe that we will face or issue any problem.

Q - Wesley Brooks {BIO 16407564 <GO>}

Excellent. Thank you, very much.

A - Wesley Batista {BIO 15243148 <GO>}

Thank you.

Operator

Excuse me. Our next question comes from Mr. Bryan Hunt with Wells Fargo Securities.

Q - Bryan Hunt {BIO 1530288 <GO>}

Good morning.

A - Wesley Batista {BIO 15243148 <GO>}

Good morning, Bryan.

A - Jeremiah O'Callaghan

Good morning, Bryan.

Q - Bryan Hunt {BIO 1530288 <GO>}

Well that was one of my questions on XL. So I'll shift gears and I was wondering if you could talk about given the tightness of the cattle supply in the United States your outlook for margins over the next couple of quarters, as well as do you plan on taking any capacity out of your operations to maintain capacity utilization in your other facilities.

A - Wesley Batista {BIO 15243148 <GO>}

Right. Bryan --

Q - Bryan Hunt {BIO 1530288 <GO>}

Yes. And all in North America is my reference.

A - Wesley Batista {BIO 15243148 <GO>}

Yes, yes. So basically, Bryan, we don't intend to close any plant, or we don't intend to, yes, to reduce, we to reduce our output in our business. And so what we are doing is to manage how many hours we are running our business and too but we are managing how many hours with the supply that we are --

A - Unidentified Speaker

Observing.

A - Wesley Batista {BIO 15243148 <GO>}

-- observing. So this is the way that we are managing the business. And we believe that the industry, the industry can handle the reduction in terms of cattle supply working how many hours and adjusting how many hours the industry is running. So basically this is the way that we believe the industry will be managing the business going forward.

Q - Bryan Hunt {BIO 1530288 <GO>}

Okay. And then my next question is and I'll hand it off, when you look at your hedge positions on animals as well as feed given the outlook for, one, very tight corn and soy markets in North America as well as, two, tight animals supplies, how have you adjusted your hedging strategies over the last six months?

A - Wesley Batista {BIO 15243148 <GO>}

In the last six months or going forward?

Q - Bryan Hunt {BIO 1530288 <GO>}

Yes, going forward.

A - Wesley Batista {BIO 15243148 <GO>}

Oh look, look. Look, Bryan, we in terms of grain we don't have any big position in grains or any big futures position. So we are buying grain more in a spot base. In the level that grain price and is today we believe it is already a very high price level that we are not very keen to lock ourselves in, or in and also buy grain in these levels. So we are handle this in a very short -- or handle a very short position in terms of grain.

Cattle, look, we -- our policy is to hedge our future sales. So when we sell futures like beef for future delivery we hedge. So this is the way that we are handle our hedge strategy.

A - Jeremiah O'Callaghan

Bryan.

Q - Bryan Hunt {BIO 1530288 <GO>}

Thank you, very much. I appreciate your time.

A - Wesley Batista {BIO 15243148 <GO>}

Thank you, now.

Operator

Excuse me. Our next question comes from Mr. Reza Vahabzadeh from Barclays.

Q - Reza Vahabzadeh {BIO 5842551 <GO>}

Good morning.

A - Wesley Batista {BIO 15243148 <GO>}

Good morning, Reza.

A - Jeremiah O'Callaghan

Good Reza.

Q - Reza Vahabzadeh {BIO 5842551 <GO>}

I'm just trying to get some clarification from your comments earlier on this call as well the prior call. So for 4Q '12 would you anticipate US beef margins to be comparable to 3Q '12? Or how would you look at 4Q '12 US beef margins?

A - Wesley Batista {BIO 15243148 <GO>}

Look. We will be positive and we will be a reasonable quarter. I will not say exactly the number. I cannot tell you the exactly the number. But we will be positive.

Q - Reza Vahabzadeh {BIO 5842551 <GO>}

Got it. And as far as the Australia business this was noted in your press release as improving year-over-year, can you provide some color on the improvement in Australia and the outlook going forward?

A - Wesley Batista {BIO 15243148 <GO>}

I will hand this to Andre.

A - Andre Nogueira {BIO 19941317 <GO>}

Hey, Reza. Our summer, Reza, as you know very well suffered with the drought since 2007, then last two years. Covering the number of cattle have been strong. That is starting to come to production size now. So it's clear that our stride is improving, is improving the strong way. And this will create for the next three years in our start up program very positive signs.

We never publish the Australian numbers separately so I will not give you any specific figures. But the situation that the operation in Australia is an important contribution for the margins in the beef business. And in this quarter. And will be very positive for next year. The number of production of Australia for next year and cattle available for next year will be around 4% to 5% more. And this is very relevant for the Australian business.

Q - Reza Vahabzadeh {BIO 5842551 <GO>}

All right. And then my last question is did you make a comment about how you expect to address the 2014 JBS USA debt maturity?

A - Wesley Batista {BIO 15243148 <GO>}

The bond in 2014 --

Q - Reza Vahabzadeh {BIO 5842551 <GO>}

Yes.

A - Unidentified Speaker

-- is the first step that we can face. So the goal, the goal for our team now is generating cash and pay down the debt. We do not at this stage refinance debt. Our intention is to pay down with the cash that we are generating from now until the maturity of the debt. That's our view now because that's the only debt that's considered that we are not using the ABL. The (inaudible) is pretty small. That's the only debt or the first step that we can pay down. So yes it is today our most expensed debt in JBS. So they go in the packages to pay down the debt with the cash that we're generating now.

Q - Reza Vahabzadeh {BIO 5842551 <GO>}

Got it. Thank you.

A - Wesley Batista {BIO 15243148 <GO>}

Thank you.

A - Jeremiah O'Callaghan

Thank you, Reza.

Operator

Excuse me. Our next question comes from Mr. Evam Submerges from Barclays.

Q - Evam Submerges

Hi. Good morning, gentlemen. Thank you for the call.

A - Jeremiah O'Callaghan

Hi, Evam. Good morning.

Q - Evam Submerges

Good morning. I have just a couple of questions. Most of my questions have already been answered. The CapEx guidance for 2013, is that something you guys can discuss already?

A - Wesley Batista {BIO 15243148 <GO>}

Evam, we are finalizing our budgets. Probably we will finalize at the end of November for 2013. But we will be around and below, is likely below BRL1 billion. But we are not -- this is not a hard number yet. But we can provide this number in the beginning of December or this in the first weeks of December that when we finalize all the budgets for 2013.

Q - Evam Submerges

Okay. And just specifically for the six plants you guys are opening for cattle processing in Brazil, are you buying those plants? Are you building them? Or how are you -- what are you doing there?

A - Wesley Batista {BIO 15243148 <GO>}

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No. These plants we already own or lease these plants. So we are not buying these plants. Three of these plants we already own and three of these other -- another three plants is the plants that we are coming from the Net Anancia[ph] deal that we already announced. So this is already is not a new acquisition.

Q - Evam Submerges

All understood, okay. And one, just one last question and a clarification about something you guys said earlier, you intend to get in Brazil the full is watering[ph] capacity of 10 million heads by the end of 2013. Is that correct?

A - Wesley Batista {BIO 15243148 <GO>}

Yes, correct.

Q - Evam Submerges

And what is the capacity -- what's the capacity currently?

A - Wesley Batista {BIO 15243148 <GO>}

Capacity currently in a run rate base is around 8.8 million heads of cattle.

Q - Evam Submerges

Okay, understood. Thank you, guys.

A - Jeremiah O'Callaghan

Okay. Thank you.

Operator

Excuse me. Our next question comes from Ms. Carla Casella from JPMorgan.

Q - Carla Casella {BIO 2215113 <GO>}

Hi. It's Carla Casella from JPMorgan.

A - Jeremiah O'Callaghan

Hi, Carla.

A - Wesley Batista {BIO 15243148 <GO>}

Hi, Carla.

Q - Carla Casella {BIO 2215113 <GO>}

Hi. I'm wondering on the Canadian agreement is -- was part of the agreement or your entering into that deferred by the expected tight cattle supplies over the next few years? And does this help you out in terms of using for that Canadian cattle to fill some of the demand in the US as well?

A - Wesley Batista {BIO 15243148 <GO>}

Carla, I'm not sure that I understood the question. But do it's four plants, two in Canada, two in the US. And a feed lot in Canada that has the capacity for 70,000 heads a day. We see the supply for that plant in Canada that operates 4,000 heads a day in a pretty comfortable level. So we are not concerned about the supply there. But the strategy, Carla, with this was -- the strategy is not

because cattle supply, is more because we believe that it has a lot of synergy between Canada and US, how we operate our business.

We can move product from Canada to US to put this in our distribution structure in US and to add value on our presence in US. And also and Canada export products you are not a countures[ph] that we have a strong presence like Mexico. So it's not because the tightment of the US cattle supply. So it's more because other synergies and other things.

Q - Carla Casella {BIO 2215113 <GO>}

Okay. That sounds great. And then is there any I guess run time in getting that up and running? Or when will you start to see the results from that business?

A - Wesley Batista {BIO 15243148 <GO>}

We are ramped and plus now, Carla. We do not close the acquisition yet. But it was part of the deal that we have operational agreement. So we are running the facilities. This is the third week that we are running the plants and this is already part of our results now. We will finish the deal as soon as we can, as soon as we have the authorization of the Canadian department.

Q - Carla Casella {BIO 2215113 <GO>}

Okay. That's great. And then I have one question on poultry in the US. There's been two --

A - Wesley Batista {BIO 15243148 <GO>}

Carla, only to add on this on this point. So the results of the Canada and all the XL transaction will be in the First Quarter less than next year. So this year we will see some additional revenue from coming from Canada. But we are ramping up the volume in Canada. So the full results and the full numbers we will see the First Quarter 2013.

Q - Carla Casella {BIO 2215113 <GO>}

Okay. Great. That's helpful. On the poultry side there's been two recent poultry bankruptcies in the US. And I'm wondering if you see any direct benefit for potential business you can pick up with Pilgrim's Pride.

A - Wesley Batista {BIO 15243148 <GO>}

Look, Carla, we are not looking to buy or to do any transaction or any acquisition in Pilgrim's Pride. We believe Pilgrim's -- we still have a lot of things that we need to capture. We still have a lot of opportunity to be captured now on Pilgrim's Pride. So we are very focused on building the business that we have today.

And we are not looking to acquire or to expand through acquisition our Pilgrim's Pride operation. But of course we -- the market can see some benefit that in terms of volume on the market the when or you see some plant that is being closed. So actually the industry is seeing a little benefit that is not a meaningful benefit. But the industry is benefiting some on this regard.

Q - Carla Casella {BIO 2215113 <GO>}

Okay. Great. Thanks a lot.

A - Wesley Batista {BIO 15243148 <GO>}

Thank you.

A - Jeremiah O'Callaghan

Thank you, Carla.

Operator

Excuse me. Our next question comes from Mr. Jose Yordan from Deutsche Bank.

Q - Jose Yordan {BIO 1496398 <GO>}

Hi. Good morning, everyone, a couple of follow ups on recent questions. I guess we hear that the industry beef prices in the US are falling to negative territory in the last three, four weeks. And that of course that's an industry-wide number. But if you can kind of talk us through how or how much you can be above that industry average. And I guess you've already said you're going to be positive. But not necessarily -- it's a level of when do you expect the margin between that zero and 4% or 5%.

We would also be interested in a little more detail on, or a little more guidance on where your PBC margins are going to fall in the Fourth Quarter given the -- that you're paying spot prices now. And I guess in a more and long-term question in your page 13 in your presentation you were showing a pretty sharp economy of the herd in 2013.

And it's we're kind of looking here that that's kind of tough to do biologically because of the lack of enough had for a retention over the last year or two. And so how are you reaching that number? It wasn't clear whether that was a USDA number or a JBS number.

A - Wesley Batista {BIO 15243148 <GO>}

Yes. This is USDA projection. So we believe that the cattle herd size in US is in the bottom. We believe -- we expect you'll see in '13/'14 you'll start you'll see a recover in terms of the herd size in US. And this is USDA numbers.

Let me try to remember all of your question. But you mentioned about PBC. Look, what I can tell you we don't provide guidance. But what I can tell you that the Fourth Quarter the numbers that we are seeing today is but positive numbers week by week. And is numbers that we are going to have a reasonable quarter also. So of course we cannot say now how the quarter will look like.

We still have half quarter to go. But even though the market condition and the grain price in US we are seeing a good, reasonable numbers from PBC. And we are optimistic about the Fourth Quarter results. We believe we will for sure we will have a positive quarter in terms of EBITDA and we believe also we can be reasonable numbers for the quarter in PBC. We in terms of beef is your other question, look, we will see a positive quarter also in the Fourth Quarter.

I cannot tell you the guidance and we don't provide guidance. But in the way that we are seeing the business progressing we believe we will see a reasonable number for the Fourth Quarter as well. So overall I think, look, PBC in the Third Quarter you already know the number. And I think we are making progress inside of our business, not only dependent of the grain market or the chicken market.

So I think we are improving our operation to be more efficient and to operate the business with less cost. We strongly believe that market condition is for everybody, grain prices for everybody and chicken market is for everybody. So we need to be efficient inside of our doors. And this is in the way that we are looking our business every day and trying to get as most from each operation every day.

Q - Jose Yordan {BIO 1496398 <GO>}

Great, fair enough. If I can just follow up real quick on can you give us an idea, a sense of what percentage of PBC sales are cost plus that type of arrangement?

A - Wesley Batista {BIO 15243148 <GO>}

Cost plus type of arrangement I cannot tell you the top of my head. I apologize. So we can follow up this with our team in US that is how much is cost plus type of sales. So I don't remember top of my head.

Q - Jose Yordan {BIO 1496398 <GO>}

All right. We'll follow up with it. Thanks.

A - Wesley Batista {BIO 15243148 <GO>}

Okay. Thank you.

A - Jeremiah O'Callaghan

Thank you, Jose.

A - Unidentified Speaker

Thank you.

Operator

Excuse me. Ladies and gentlemen. this concludes today's question-and-answer session. I would like to invite Mr. Wesley Batista to proceed with his closing statements. Please, sir, go ahead.

A - Wesley Batista {BIO 15243148 <GO>}

So I would like to thank you all to participate in our Third Quarter earnings call. Like I mentioned before we are satisfied by the quarter, by the numbers, the results, top-line growth in terms of EBITDA margin, in terms of by leveraging our balance sheet. We will be -- keep looking and running our business to generate more cash, to deleverage more our balance sheet and to add more value to all of our shareholders and to create value on our Company. Thank you, all and have a good day.

Operator

Thank you. That does conclude our JBS update on your conference for today. Thank you, very much for your participation. Have a good day. And thank you for using Chorus Call.

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